PUBLIC POLICY AND TAXATION

Professional 2
December 2001

MARKING SCHEME

CIPFA

Question 1

(a) The following arguments come from the OLM.

For the Euro

It reduces transaction costs, facilitating trade amongst Eurozone members. *1*

It introduces greater price transparency, encouraging the minimization of production costs in order to remain competitive. *1*

Offers prospect of substantial economic, monetary and political stability. *1*

Against the Euro

Concerns over the surrender of the political sovereignty of the UK government. *1*

Concerns over the surrender of the economic sovereignty of the Bank of England (monetary policy) (and possibly the UK government – fiscal policy). *1*

Fears of greater and more harmonized regulation (business, social and employment) in more unified Europe. *1*

(6)

Note:

There are many other arguments, both for and against, that students may come up with in addition to or instead of the above. Full credit should be given for all plausible arguments, but the maximum available mark for Section A remains at 6 marks.

(b) **The European Commission**

Comprises 20 commissioners and a president. Work is divided into 23 Directorates General, roughly equivalent to ministries in a country. *1*

Ensures EU legislation is upheld in nation states (a watchdog role). *1*

Initiates EU policy by formulating proposals that go to the Council of Ministers. *1*

Has a broad executive role (in terms of supervising and implementing EU policies, and managing the EU budget). *1*

The Council of the European Union

Each EU member country has representation on this Council which is headed by the president (a role that rotates between member states on a 6-monthly basis). *1*

Central function is to decide EU law on the basis of proposals received from the Commission. *1*

Is supported in work by permanent delegations of diplomats (COREPER) from each member country. *1*

Council's work is divided up into 23 policy areas. Decisions made by unanimity, qualified majority or simple majority. *1*

The European Parliament

Comprises 626 directly elected (proportional representation) MEPs (87 from the UK). *1*

Is not a parliament in the traditional sense – does not produce a government or any pro-active legislation – is part of the consultative process. *1*

The EU parliament is able to amend/reject draft laws and influence the Budget. But it can only reject draft laws if the Council of Ministers and Commission agree. The Parliament has little/no democratic control over either the EU Commission or EU Council of Ministers – is a good example of the "democratic deficit". *1*

Main real powers are to dismiss the Commission (but this has never been exercised and may be a formal rather than a real power); confront the Commission over budget proposals; and to reject draft budgets. *1*

Note:
There are other/alternative aspects of institutional structure and function that candidates may discuss in 1(b). Full credit should be given for all plausible discussion, but the maximum available mark for each part of Section B is 4 marks. *(12)*

(c) **Parliamentary Sovereignty**

Explanation of the term Parliamentary Sovereignty (refers to the UK parliament as being the country's ultimate legal authority and, in the UK's external relations, parliament's ability to function as an independent entity). *1*

Arguments supporting view that UK Parliamentary Sovereignty has been impaired

European Communities Act (1972) gave the force of law within the UK to obligations arising under the EU treaties. EU law now has general and binding authority in the UK. *1*

EU law takes precedence over all inconsistent UK law. It precludes the UK parliament from legislating on matters within EU competence, where the EU has formulated rules to "occupy the field". *1*

The role/power of the EU Council of Ministers has had an especially major impact in diminishing UK parliamentary sovereignty. It is the EU's crucial decision-making institution that converts proposals from the Commission into EU legislation. The various voting methods (unanimity, qualified majority and simple majority, dependent on the issue under consideration) are frequently the subject of heated debate in the context of parliamentary sovereignty. In particular, the increase in majority voting has diminished sovereignty *1*

Arguments against the view that Parliamentary Sovereignty has been impaired

EU membership has not broken the principle that parliament cannot bind its future action (ie acts of one parliament are not binding on acts of future parliaments; hence the European Communities Act is overturnable). *1*

If the UK refuses to pass amending legislation where its law is inconsistent with EU law, Test Cases imply that the European Court of Justice cannot hold national legislation void. *1*

Conclusion

On balance, the present constitutional position is that the UK's membership of the EU has impaired the doctrine of parliamentary sovereignty. However, opinion about whether or not this is desirable remains divided. Parliamentary sovereignty, vis-à-vis the EU, can only be fully restored by the UK's withdrawal from the EU by repealing/overriding the 1972 European Communities Act; the negative impact of any such move could well massively outweigh the benefits of restored parliamentary sovereignty. *1*

(7)

(25)

Question 2

(a)

(i) House of Commons Functions

Representation. Represents political parties, pressure groups and the constituencies/electorate. *1*

Legislation. HoC no longer makes policy in either the sense of initiation or strongly influencing (this now done by government). But HoC must approve legislation (it frequently amends and occasionally defeats legislation). *1*

Scrutiny and Influence of the Executive. HoC acts as an arena for constitutional opposition. It is in parliament that the government must explain and defend its actions (in practice, recent opposition parties have been too small to do anything other than to resort to delaying tactics). *1*

Forum for National Debate. HoC acts as a focus for national debate on many different kinds of occasion (eg PM Question Time, Queens Speech, normal legislative business). *1*

Recruitment of a Government. Parliament no longer selects Ministers, but it is a "school of statesmanship". Ministers are invariably drawn from parliament, especially the HoC. *1*

(Some candidates may mention the function of Legitimation (authorising the actions of government) in addition to/instead of those above – this is quite acceptable, but overall maximum for 2(a)(i) is 5 marks).

(ii) House of Lords Functions

Legislation. HoL can revise HoC bills, giving Ministers the opportunity for second thoughts. But it cannot delay or amend money Bills. It can delay non-money Bills for up to one year and can veto Bills to prolong the life of parliament beyond the statutory 5-year period. (It can also veto private bills and delegated legislation). *2*

Scrutiny and Influence of the Executive. HoL subjects government policy and administration to scrutiny through questions and through the work of its select committees. *1*

Forum for National Debate. HoL acts as a Forum for National Debate on matters of current interest. *1*

Supreme Court of Appeal. The HoL is the UK's ultimate Court of Appeal. *1*

(Some candidates may mention the function of Legislative Sovereign (HoL is, by convention, the "Queen in Parliament".) – this is acceptable, but overall maximum for 2(a)(ii) is 5 marks). *(10)*

(b)

(i) House of Commons Reform

Candidates are required to describe any two significant reform proposals. These proposals could be either drawn from the three listed below, or from the list in Box 16.5 (page 320) of Coxall and Robins, or from a combination of these examples.

There is a maximum of 2 marks available for each of the two chosen reform proposals.

Jopling Reforms (1994) changed the working hours of the HoC. It provided for fewer Friday sittings to make way for constituency work, morning sessions on Wednesdays, early 7pm finishes on some Thursdays, a 10-minute limit on speeches from 18.00-21.00, and a formal timetable for government bills after they have won a second reading.

Blair (1997) changed PM Question Time from a twice-weekly, 15-minute event on Tuesdays and Thursdays to a once-weekly, 30-minute event on Wednesdays. Aim was to transform the nature of PMQT from its "bearpit" conflictual atmosphere to one involving more considered and reflective exchanges between the PM and the Leader of the Opposition.

Extend the scrutiny and debate of EU documents and policies beyond the present-day Select Committee on European Legislation and two special Standing Committees to the entire HoC. This would improve scrutiny and debate of European legislation and policies.

(ii) House of Lords Reform

Candidates are required to describe any two significant reform proposals. These proposals could be either drawn from the three listed below, or from the list in Box 16.6 (page 326) of Coxall and Robins, or from a combination of these examples.

There is a maximum of 2 marks available for each of the two chosen reform proposals.

Announcement in Queen's Speech of November 1998 that the Government would introduce a Bill to remove the automatic rights of hereditary peers to sit in the Lords. Shortly after that, the government reached agreement with the Opposition that some 92 hereditary peers (around 10%) would retain their seats until the reform process was finally complete. The Bill subsequently became law, and the majority of hereditary peers lost their seats in the Lords in November 1999.

In January 1999, the Government published a White Paper, *Modernising Parliament: Reforming the House of Lords* and announced that it was establishing a Royal Commission to look into the matter. The Royal Commission's report was published in January 2000 and proposed a number of options. These included a partially directly elected Lords with the remainder of members appointed.

In its 1997 election manifesto, Labour promised to review the system of appointment of life peers. This, along with the abolition of hereditary peers in the Lords, would create a second chamber of parliament that more accurately reflected the proportion of votes cast at elections. It specifically ruled out simply replacing a Conservative-dominated Lords with a Labour-dominated one. *(8)*

(c)

(i) Representative government is a form of democratic rule in which government is by representatives (eg MPs or Congressmen) elected by popular votes. The exercise of authority is legitimated ultimately (although not solely, since it must be exercised also according to constitutional rules) by the popular election of power holders. *2*

Up to 1 mark for answers that describe Representative Government in terms of "proportional representation" in Parliament.

(ii) The HoC seat distribution, following the 2001 election shows that;
Labour won 40.7% of the votes cast (only 24.1%* of the enfranchised electorate voted for Labour) but gained 62.7%* of the HoC seats.
Conservatives won 31.9% of the votes cast (18.9%* of the enfranchised electorate voted Conservative) but gained 25.1%* of the seats.
Lib Dems won 18.3% of the votes cast (10.8%* of the enfranchised electorate voted Lib Dem) but gained 7.9%* of the seats.

** these figures are not explicitly given in the question's table of data, but can be easily calculated from that table* *2*

The distribution of seats in the HoC, following the 2001 election, does not conflict with the broad concept of representative government (ie government is by representatives (MPs) that have been elected by popular vote). *1*

However, it might be argued that there is some conflict in that power holders (eg prime minister, secretaries of state) are not directly elected by popular vote. Instead, the prime minister is elected by the MPs of the largest HoC party, and ministers are appointed through a system of patronage. *1*

The HoC seat distribution does conflict with the concept of equity/liberal democracy in that the distribution of seats does not limit the powers of government which are not, therefore, checked effectively by minority interests. The situation, relative to liberal democracy, looks especially distorted if Labour's share of the electorate (rather than its share of votes) is considered: Labour won 24.1% of the electorate's support, but gained 62.7% of the HoC seats. *1*

(7)

Give credit for answers which, based on the "proportional representation" understanding of representation government, state that there is a conflict in parliament with the concept of Representative Government.

(25)

Question 3

(a) *Note: Flexibility is needed when marking 3(a) – plausible aims, other than those in the marking scheme, may be suggested and should be awarded credit – but the* ***balance of marks should remain as a maximum of 4 for explaining the aims and a maximum of 4 for highlighting the differences in Parties' policy approach, subject to an overall maximum of 6 for part (a).***

The broad aims of privatisation/marketisation are to improve the efficiency and effectiveness of public services. *1*

Efficiency – refers to the cost of a service relative to its output (unit costs of production). *1*

Effectiveness – refers to quality considerations and the extent to which organisations satisfy customer needs and wants. *1*

The broad aims of privatisation/marketisation are common to both the Conservative and New Labour Party. But there are differences in policy approach:

Conservatives have a very strong commitment to the free market and "individualism" principles. They see free market principles as the only way to manage the public sector. *1*

New Labour has not reversed any Conservative principles as they impact on the public sector, but it has considerably softened the approach. *1*

New Labour has replaced the earlier "individualism" principles with ones that embody the notion of a stakeholder society and a more corporatist society (capitalism with a human face – the Third Way). *1*

(6)

(b) *Note: Flexibility is also needed when marking 3(b) – plausible schemes/policies/programmes should all be given credit. It is equally acceptable if some students choose to address several schemes briefly or just a few in more detail. It is suggested that no more than 4 ma rks be allocated to the discussion of any one scheme, implying that students are expected to discuss at least three schemes.*
Overall, marks are available on the basis of 1 mark per relevant point well made, up to a maximum of 11 marks.

Schemes that candidates may discuss include:

Denationalization of public enterprises (over 50 enterprises have been denationalized – eg the utilities, BP, the railways, coal, etc) – most organisations have entirely denationalized, but the public sector retained a share in many, especially in the early years after privatisation.

Deregulation/liberalization of markets to enhance competition (eg bus industry, banking industry).

Contracting out of public services. Associated with market testing and best value (eg school inspection, refuse collection by many local authorities).

Reduction of public sector control (eg youth training, urban redevelopment).

Introduction of market forces into public sector "merit good" areas such as health and education. Involves "realistic" charges and/or "competing for customers" and being run akin to commercial businesses. Associated market testing and CCT in local government and the NHS.

Civil Service reforms aimed at reducing waste, bureaucracy, and over-government (eg reduction in size; curtailment of privileges (replacement of "pay by comparison" by performance-related pay); efficiency reforms (Rayner Scrutinies, FMI, Next Steps, Market Testing, Citizens Charter).

The growth of "Quango Government" – aimed to redistribute power from the "producer" to the "customer" (eg greater power to school governors to reduce power of teachers/unions (the producers) and raise influence of parents (the customers). But the whole issue of Quangos is very controversial (the democratic deficit).

The Private Finance Initiative – aims to get the public and private sectors working more closely together in providing services to the public. Private sector funds the design, construction, maintenance and management of public-sector projects (eg hospitals, motorways) which are leased back to the public sector. Advantage for public sector is investment without public sector borrowing (leasing is cheaper than borrowing). *(11)*

(c) *Part (c) requires candidates to evaluate the impact of policies. The consequential subjective nature of (c) means that there is no simple right or wrong answer, and that there are likely to be significant differences in candidates' answers. Examiners are therefore required to use their discretion when marking Part (c) and to award credit for all well argued answers, up to a* ***maximum of 8 marks.***

As a broad guide, better candidates are likely to discuss some of the following points in their answers.

The results of privatisation and marketisation have been mixed.

Media emphasis tends to focus on problem areas (eg the railways). But some of the difficulties of problem areas have little to do with privatisation (eg Railtrack problems are largely due to its inheritance of a railway infrastructure that had been seriously neglected whilst in public ownership).

Media tends to give relatively little attention to successful areas (eg public utilities have made huge gains in efficiency, though this has been at the expense of shedding 180,000 jobs).

Some sectors that have improved their efficiency have failed to also improve their effectiveness (eg bus deregulation has significantly improved efficiency, achieved largely via withdrawal of conductors from buses – but this often slows buses' progress along routes, makes other traffic slower, and increases passenger perception of their exposure to threats of theft/violence/etc from other passengers).

Since privatisation, consumers have paid less for gas, electricity and telephones in real terms (but was this to do with privatisation or more to do with falling oil prices and technological advances?). Since privatisation, water bills have risen by one-third in real terms (was this because of privatisation or because of the ageing/inefficient system prior to privatisation?).

Perceived problem of "snouts in the trough"/"fat cats" (CEO's of privatized organisations). Connected with this is the huge shareholder gains when on-selling privatised companies (eg Eversholt Leasing sold two years after privatisation for twice its original price).

Fears that old public sector monopolies (especially utilities) are being replaced, through the process of Merger & Acquisition (M&A), by new private sector monopolies. In such instances, the regulatory system (in particular, the Competition Commission and/or the Secretary of State) often seems reluctant to interfere with these moves (through M&A) towards private sector monopolies. *(8)*

(25)

Question 4

(a) 12 months to 31 December 2000 and 3 months to 31 March 2001. *1*

(b) *Plant and machinery:*

		General Pool	Mercedes	BMW1	BMW2	Total allowances	
		£	£	£	£	£	
y/e 31/12/2000							
WDV b/f		117,300	32,420	18,760			
Additions (no FYA)		10,420			29,300		
		127,720					
Disposals		(15,000)					
		112,720					
Disposal				(21,500)			
Balancing charge				(2,740)		(2,740)	*1*
WDA @ 25%		28,180				28,180	*1*
WDA (restricted)			3,000		3,000	6,000	*1*
		84,540					
Additions	72,500						
FYA @ 40%	29,000	43,500				29,000	*1*
WDV c/f		128,040	29,420		26,300		
Total allowances						60,440	
3 months to 31/3/2001							
Disposals		(2,920)					
		125,120					
WDA @ 25% x 3/12		7,820				7,820	*1*
WDA (restricted) x 3/12			750		750	1,500	*1*
		117,300					
Additions	42,000						
FYA @ 40%	16,800	25,200				16,800	*1*
WDV c/f		142,500	28,670		25,550		
Total allowances						26,120	

(There is no restriction for private use of an asset by an employee.)

(7)

(c)

Disposal of shares

S104 holding	**No of shares**	**Cost**	**Indexed cost**	
		£	**£**	
Bought May 1989	1,000	2,000	2,000	
Indexation to March 1996				
(151.5 – 115.0)/115.0 x £2,000			635	
Bought March 1996	1,000	2,400	2,400	
	2,000	4,400	5,035	
Indexation to February 2001				
(171.7 –151.5)/151.5 x £5,035			671	
			5,706	*2*
Sold February 2001	1,000	2,200	2,853	*1*
c/f	1,000	2,200	2,853	

The gain on the disposal is £3,147 (£6,000 - £2,853). *1*

The gain is covered by capital losses brought forward. There are capital losses left to carry forward of £6,853 (£10,000 - £3,147). *1*

(5)

(d)

	Year to 31/12/00	3 months to 31/3/01	
	£	£	
Trading profits (time apportioned)	775,680	193,920	*1*
Less: Capital allowances	(60,440)	(26,120)	*½*
	715,240	167,800	
Less: Trading losses b/f	630,000		*1*
Schedule D Case I	85,240	167,800	
Schedule D Case III	30,000	10,000	*1*
Chargeable gains	-	-	*½*
	115,240	177,800	
Less: Charges			
Patent royalties	(75,300)	(26,700)	*1*
Charitable covenant	(18,000)	-	*1*
PCTCT	21,940	151,100	
			(6)

(e)

	Year to 31/12/00	3 months to 31/3/01	
	£	£	
PCTCT	21,940	151,100	
FII £49,500 x 100/90	55,000		
£40,500 x 100/90		45,000	
"Profits"	76,940	196,100	*2*

Year to 31 December 2000

The first 3 months of this accounting period fall into FY1999 and the last 9 months fall into FY2000. Profits are beneath the small companies rate lower limit for both FY's (£300,000) and above the starting rate upper limit for FY2000 (£50,000). Therefore corporation tax is payable at the small companies rate.

Corporation tax due 1 October 2001 £21,940 @ 20% = £4,388.00 *2*

3 months to 31 March 2001

This accounting period falls entirely into FY2000. The small companies rate limits are £300,000 x 3/12 = £75,000 and £1,500,000 x 3/12 = £375,000 so corporation tax is payable at the full rate less marginal relief.

FY2000	£151,100 @ 30%	45,330.00	*½*
	Less: 1/40 x (£375,000 – £196,100) x (£151,100/£196,100)	3,446.17	*1*
Corporation tax due 1 January 2002		41,883.83	*½*
			(6)

(25)

Question 5

(a)

	£	£	
Salary		80,000	
Expenses allowance		5,000	½
Living accommodation:			
Annual value	8,400		½
6% x (£140,000 - £75,000)	3,900		½
	12,300		
Less: Contribution	2,400	9,900	½
Use of furniture 20% x £15,000		3,000	½
Ancillary expenses		1,480	½
Company car:			
25% x £32,000	8,000		½
Less: Contribution for private use	1,200	6,800	½
Fuel benefit		3,200	½
		109,380	
Less: Necessary subsistence expenses	2,000		½
Allowable subscription	230		½
Pension scheme contributions: 6% of £80,000	4,800	7,030	½
Schedule E income		102,350	

Notes:

(i) Entertaining expenses are not allowable if paid out of salary or out of a general expenses allowance. ½

(ii) The car was driven for between 2,500 and 17,999 business miles and so the taxable benefit is based upon 25% of list price. Colin does not pay for all private fuel, so the contribution of £50 per month is ignored. ½

(iii) The total amount outstanding on all beneficial loans during the year never exceeds £5,000 so no taxable benefit arises. ½

(iv) The provision of a mobile telephone does not give rise to a taxable benefit. ½

(8)

(b)

	Total	Non-savings	Savings	Dividends	
	£	£	£	£	
Schedule E	102,350	102,350			½
Schedule D Case III £50 + £140	190		190		*1*
BSI £1,320 x 100/80	1,650		1,650		½
Schedule F £2,790 + £310	3,100			3,100	½
	107,290	102,350	1,840	3,100	
Personal allowance	4,385	4,385			½
Taxable income	102,905	97,965	1,840	3,100	

Income tax due:

				£	
Starting rate band	:Non-savings	1,520	@10%	152.00	½
Basic rate band	:Non-savings	28,380	@22%	6,243.60	*1*
Higher rate	:Non-savings	68,065	@40%	27,226.00	½
	:Savings	1,840	@40%	736.00	½
	:Dividends	3,100	@32.5%	1,007.50	½
				35,365.10	
Less: MCA £2,000 @ 10%				200.00	*1*
				35,165.10	
Less: Tax deducted at source (£330 + £33,400)				33,730.00	½
				1,435.10	
Less: Tax credits on dividends				310.00	½
Income tax payable				1,125.10	

(8)

Notes:

(i) The NSB interest is received gross and is taxable under Schedule D Case III. The first £70 of NSB ordinary account interest is exempt from income tax. ISA interest is also exempt from income tax.

(ii) Colin is not yet 65 and so may claim only the basic personal allowance. He may claim MCA by virtue of his wife's age but this is limited to the minimum amount since his income is very high.

(iii) The basic rate band is extended by £1,500 (£1,170 x 100/78) because of the Gift Aid donation.

(c)

	£	
Primary Class 1 contributions:		
8.4% x (£27,820 – £3,952)	2,004.91	*1*

(d) A tax return will be issued because Colin has NSB interest which has not been taxed at source. He is also liable to higher-rate tax on his building society interest and dividends. *1*

Tax returns for 2000/01 must be filed with the Inland Revenue on or before the following dates:

(i) 31 January 2002 (or within 3 months of the date of issue of the return, if later) for taxpayers who have calculated their own tax liability *½*

(ii) 30 September 2001 (or within 2 months of the date of issue of the return, if later) for taxpayers who wish the Inland Revenue to calculate their tax liability. *½*

Penalties are imposed upon taxpayers who do not submit their tax returns by the 31 January following the end of the tax year. The most well-known penalty is the £100 fine for late submission of a return, but as well as this there is another £100 fine if the return is more than 6 months late. If a return is more than 12 months late, a penalty may be imposed of up to 100% of the tax liability for the year. *2*

(4)

(e) Colin's proposed transfer of investments to his wife would be a legal tax avoidance manoevre. The income derived from the investments would be taxed in his wife's name and this would reduce the couple's overall tax liability since the whole of her personal allowance, starting rate band and basic rate band are currently unused (whilst he is a higher rate taxpayer). However, it would be necessary for legal title to the investments to pass to Colin's wife and he would then be unable to prevent her from using them for any purpose that she wished. *1*

In general, tax avoidance (which is legal) involves the sensible arrangement of a taxpayer's financial affairs so as to minimise his or her tax liability. Tax evasion (which is illegal) involves dishonest conduct and includes actions such as concealing a source of income or claiming allowances and reliefs to which the taxpayer is not entitled. *1*

Plus 2 further marks for comment on complex tax avoidance schemes, including reference to relevant case law *2*

(4)

(25)

Question 6

(a)

(i) A person who makes only zero-rated supplies is making taxable supplies and must register for VAT if turnover exceeds the prescribed threshold. The person may register voluntarily if turnover does not exceed the threshold. Having registered, the person charges VAT (at 0%) to customers and may reclaim input tax. Zero-rated supplies include food, water, books and newspapers. *1*

(ii) A person who makes only exempt supplies is not making taxable supplies and cannot register for VAT, regardless of turnover. The person must not charge VAT to customers and cannot reclaim input tax. Exempt supplies include insurance and financial services. *1*

(iii) A registered person who makes a mixture of taxable supplies and exempt supplies is partially exempt. Such a person charges output tax on the taxable supplies made to customers and may make a partial recovery of input tax. Input tax which is attributed to taxable supplies is reclaimable in full. Input tax which is attributed to exempt supplies cannot be reclaimed. A proportion of any remaining unattributed input tax may be reclaimed, depending upon the ratio of taxable supplies to total supplies. *2*

(4)

(b)

(i) Cordelia's cumulative turnover for the 12 months to date, excluding supplies of capital assets, passes the registration threshold of £52,000 at the end of February 2001 (when turnover reaches £53,600). She must notify Customs and Excise of this fact by 30 March 2001 and her registration will probably take effect as from 1 April 2001. *2*

If she registers late, her registration will be backdated and she will have to account to Customs and Excise for output VAT as from the due date of registration. This VAT may prove difficult or impossible to collect from customers in retrospect. She will also be liable to a penalty (minimum £50) of between 5% and 15% of the amount of tax due between the due date of registration and the actual date of registration, depending upon the length of the delay. *2*

Registration will not be required if Customs and Excise are satisfied that taxable turnover will not exceed the deregistration threshold during the 12 months following the end of February 2001. *1*

(5)

(ii) Cordelia may have decided not to register voluntarily because she wished to avoid the administrative costs of maintaining VAT records, supplying VAT invoices, making VAT returns etc. She may also have felt that adding VAT to her customers' invoices would trigger a loss of custom and that this effect would outweigh the benefit of being able to reclaim input tax. *1*

On the other hand, a person who is making only zero-rated supplies or who is making supplies wholly or mainly to other registered persons (who can reclaim any VAT which is charged to them) will not lose customers when voluntarily registering for VAT. Such a person might then feel that the benefit of being able to reclaim input tax more than compensates for the administrative costs of being registered. *1*

(2)

(c) The main conditions which must be satisfied if the output VAT relating to a bad debt is to be reclaimed are as follows:

- goods or services have been supplied for a consideration and the related output tax has been accounted for to Customs and Excise, and *1*
- the debt has been written off in the books of account, and *1*
- at least 6 months have elapsed since both the date of the supply and the due date of payment. *1*

(3)

(d) The annual accounting scheme may be used so long as a registered person's taxable turnover does not exceed £300,000 p.a. A person who has joined this scheme makes only one VAT return each year. The scheme generally operates as follows: *1*

- At the start of each year, Customs and Excise estimate the total VAT liability for the year, basing this estimate on past experience. ½
- During the year, the person makes nine interim payments to Customs and Excise, each equal to 10% of the estimated liability for the year. These payments must be made by direct debit. ½
- Within 2 months of the end of the year, the VAT return must be submitted together with a tenth and final payment representing the balance of the VAT due for the year. ½

No interim payments are required if taxable turnover does not exceed £100,000 p.a. unless the estimated VAT liability for the year is at least £2,000. In this case, three interim payments are required, each equal to 20% of the estimated liability for the year. ½

(3)

(e) A "default" occurs if a registered person submits a late VAT return or makes a late payment of VAT to Customs and Excise. In these circumstances, Customs and Excise may issue a notice specifying a surcharge period. If, within this period, the registered person then makes a further default, a default surcharge is levied. The surcharge (minimum £30) varies from 2% to 15% of the tax paid late, depending upon whether this is the first or subsequent default within the surcharge period. *2*

(f)

(i) Direct taxes are those where the formal incidence of the tax and the effective incidence of the tax are the same. In other words, the person or organisation who is formally required to pay the tax is also the person or organisation who bears the tax. Corporation tax is an example of a direct tax. *1*

Indirect taxes are those where the formal incidence of the tax is different from the effective incidence of the tax. VAT is an indirect tax because formally it is a turnover tax payable by businesses but effectively (since the tax is passed on to customers) it is borne by those who buy goods or services from businesses. *1*

(2)

(ii) A progressive tax is one where the proportion of income or wealth paid in tax increases as the amount of income or wealth increases. Corporation tax is an example of a progressive tax, since (in FY2000) the rate of tax applicable to a company's chargeable profits increases from 10% to 30% as profits rise. *1*

A regressive tax is one where the proportion of income or wealth paid in tax decreases as the amount of income or wealth increases. A poll tax of (say) £300 per annum on each member of the UK population would be regressive, since £300 represents a higher percentage of a poorer person's income or wealth than it does of a richer person's income or wealth. *1*

A proportional tax is one where the proportion of income or wealth paid in tax stays the same as the amount of income or wealth increases. *1*

VAT is essentially regressive, since the amount of VAT payable when a specific item of goods or services is purchased is based solely upon the price of the item and is not influenced in any way by the buyer's financial circumstances. *1*

(4)

(25)