THE CHARTERED INSTITUTE OF TAXATION

The Chartered Tax Adviser Examination

May 2009

VAT on Cross-Border Transactions & other Indirect Taxes

Advisory Paper

TIME ALLOWED – 3 HOURS

- You should answer all of the questions.
- Start each answer on a new sheet of paper and write on one side only. Do not write in the left-hand margin.
- All workings should be shown and made to the nearest month and pound unless the question specifies otherwise.
- Marks are specifically allocated for presentation.
- Candidates who answer the law elements in this paper in accordance with Scots law or Northern Ireland law should tick the appropriate box on the front of the answer folder.

1. You are the in-house environmental tax specialist at a mid-tier firm of accountants and a colleague from the corporate tax section has referred the following case to you.

   Giles Ltd, a client which specialises in wholesale agricultural products, is now looking to move into production and in the last month has purchased an area of land in the UK from which it has started to extract sand, gravel and rock for processing and sale through its warehouse network. The level is estimated to reach 500 tonnes per month in the start-up phase. Although the land is marshy in part and there will be some water in the amounts extracted, Giles Ltd believes it will still need to use up to 125 tonnes of water to wash the 500 tonnes of rock and sand properly prior to final sale.

   An initial survey of the land has shown that there is a significant quantity of potash which Giles Ltd aims to separate from the gravel and turn into fertiliser at its new processing plant.

   Giles Ltd is in talks with the local council to use the leftover sand towards restoring the beach at Compton-on-Sea where winter storms have washed much of it away.

   Their finance director is particularly concerned that all relevant record-keeping requirements be met as the firm has had issues over this in the past with HM Revenue & Customs for direct tax.

   You are required to prepare a memo to your colleague setting out the environmental tax implications of Giles Ltd's proposed activities. You should provide full statutory references. (10)

2. Your client, Rocky Road Ltd, is a waste solutions company which has recently had an audit visit from HM Revenue & Customs. The finance director, Mr Apollo, has asked you for some advice on the following issues which arose from the visit.

   1) Rocky Road Ltd has been working on the reclamation of some contaminated land for a local authority. This is in part required under an Environmental Protection Act remediation notice prior to sale and re-development. Although this reclamation was notified to HM Revenue & Customs, the officer says that no certificate was issued, this relief has now been withdrawn in any case and that landfill tax is therefore due on all disposals after 30 November 2008. He has consequently raised an assessment for this.

   2) Rocky Road Ltd requested and obtained authorisation for a temporary tax-free area which HM Revenue & Customs specified was to expire after three years. Due to an administrative oversight, this was not renewed. The officer has raised an assessment for all the material held at the site as at the day the authorisation lapsed, which Mr Apollo feels is particularly unfair as all the material was subsequently recycled as planned.

   3) The officer has checked Rocky Road's terms of business. He has noticed that they do not account for landfill tax where they pay for the waste or allow waste to be deposited for free. He has asked for the reason behind this as he feels tax should be payable. Mr Apollo says the waste is used for capping at the end of the day and maintaining site roads and it does not seem right to pay landfill tax on useful material.

   4) On one of its sites the weighbridge has been vandalised and the officer has claimed that they must use the local council weighbridge until it is fixed, even though this is 35 miles away from the site.

   You are required to write a letter to Mr Apollo responding to his queries. (10)

3. Your firm has recently been approached by a US firm, Broadnet, which specialises in internet and broadcasting services and is looking to expand into the EU market.

The finance director, Mr Sernik, has advised you that Broadnet initially plans only to offer digital downloads of its software and web-hosting to consumers across the EU. It is also developing a virtual classroom function which could allow customers either to log in and watch lessons run by Broadnet tutors or, as a cheaper option, access interactive slide presentations and automated teaching materials as part of a "teach yourself" offering.

Mr Sernik is also considering signing up with a US share broker to enable Broadnet to provide a securities dealing service for customers. Broadnet would charge consumers commission for each transaction.

Broadnet's sister company, BroadTV, is also looking to break into the UK and Irish markets with its English-language programming. This would be provided to subscribers over satellite rather than the internet in return for a monthly fee.

Mr Sernik does not believe that any of his companies should have any VAT registration problem as they have no offices or staff based anywhere except the US. He is keen to know whether or not he will be able to recover VAT on his travelling and accommodation costs in the EU as he has spent a lot of time promoting Broadnet and BroadTV at conferences and client meetings in the last year. He has records of the amounts and has asked you where he needs to send them. He is particularly eager to recover VAT on some office furniture Broadnet was forced to buy in the UK for a stall at a trade conference. A client is storing it at the moment but Mr Sernik has an offer from a UK company which buys second-hand furniture. If he can recover the VAT he paid originally he will actually be in profit once he has sold the furniture.

You are required to write a letter to Mr Sernik responding to his points. (10)

4. You are the new indirect tax specialist at NRG Ltd, a gas and electricity producer. The finance director has sent you the following note.

Hi Bill

Welcome to NRG! I am so glad we have finally got an in-house specialist. I have never understood quite how the climate change levy works as we always had consultants deal with it.

I know you have only just joined but I would really appreciate a brief reminder of when the levy applies. I am aware of the rates but know nothing about the principles. I particularly need to understand the regime for combined heat and power stations as we had a large over-claim last year before you joined and I want to try and work out what that means!

I also have two outstanding queries from clients who claim we should not have charged them climate change levy. The first is a chemical company which buys electricity from us for electrolysis. The second is a metals producer which purchases natural gas from us for use in their blast furnaces to make iron. We have had both clients for at least six months but this is the first time they have mentioned this.

I have also received some sort of official notification from a new client which specialises in producing fuel from rubbish. Apparently they have some form of Climate Change agreement with the Secretary of State for the Environment and are expecting some levy relief.

Can you shed some light on whether the first two clients are right and what this agreement the third client has means for us in practice?

In the current difficult times we have been having problems collecting amounts due from some of our clients. As well as claiming bad debt relief for VAT I wonder whether we could also claim for any levy for which we have accounted? Are there any conditions we would need to fulfil?

I am away on business for the next few weeks so could you pop the responses on to a memo for me?

Many thanks!

Mike Salko

You are required to produce an internal memo for the finance director responding to his queries. (15)

5. Your client, Engineering Solutions Ltd, is a consultancy formed by four civil engineers in 1992. Three of the engineers are based in Birmingham, England, where they have an office with support staff. The fourth engineer is French, and has an office with a secretary in Lyon, France. The office is owned by the UK company and is operated as a branch, rather than as a separate legal entity.

All four engineers travel extensively to carry on the business of civil engineering. During the last quarter, the following issues have arisen in relation to some of their contracts.

John, one of the UK consultants, travelled to Germany to discuss a building project with a German client. The building is to be constructed in the UK for the German company by a British building firm. John is providing expert design assistance on a number of features of the building. During his visit to Germany, he incurred German VAT on hotel bills, and also on a computer program he bought for the business in Germany.

Angie, another UK consultant, travelled to Spain to give a lecture to the annual conference of a British engineering company. The client company organised its own conference, booking travel and accommodation directly with airlines and the hotel, and supplied most of the speakers from its own staff. Engineering Solutions Ltd charged the client company a fee of £2,000 for Angie's services. The client bought Angie's travel tickets (cost £400) and provided accommodation at the hotel where the conference was taking place.

David, the third UK consultant, carried out some design work in Birmingham for a Danish client in respect of a building under construction in Copenhagen. David did not need to travel to Denmark in connection with this project.

Hugo, the French consultant, was seconded to an Italian client for a month to fill in for one of their employees who was injured in an industrial accident. The Italian client is building a factory in southern France, and Hugo worked at the building site under the supervision of the client's chief engineer.

You are required to explain the VAT issues arising from the issues identified above. Your explanation should include statutory references where relevant.

(15)

6. You have received the following letter from a client:

Turbines International plc

4 May 2009

1, Toucan Tower
Canary Wharf

Dear Mr Jones

<u>International Transactions</u>

We need your advice on a couple of upcoming transactions. I have set out the problems below.

We have ordered some new equipment from a supplier based in the US. The following price has been quoted by the supplier for the delivery and installation of the equipment:

	£
The equipment itself	300,000
Installation work, to be carried out in the UK by the supplier's engineers	40,000
Royalty paid by the US supplier to the company that holds the patent for the equipment, charged on to us in addition to the purchase price	5,000
Special containers for the transportation from the US, not reusable	4,000
Transport from the factory in the US to our premises in Blackburn	25,000
Insurance in transit	3,000

The plant is highly specialised and the supplier's own employees are the only people qualified to set it up correctly. The supplier has no place of business in the UK and its engineers will stay here for up to two months while they install the equipment.

I estimate that 80% of the transport cost will be incurred in transporting the goods by sea freight to Liverpool docks, and the remaining 20% will be incurred in transporting the goods by road to our plant in Blackburn, Lancashire. I'm told that the rate of Customs Duty applicable to this classification of goods is 4%.

In addition, we will buy computer software from the same supplier for use in operating the machine. There is an annual licence fee of £40,000 for the use of the software. We will also pay a royalty to the supplier of £10 for each item manufactured using the equipment.

As I understand it, the supplier is not registered for VAT in the UK or anywhere in the EU, and does not wish to register if it can be avoided. They have exclusively supplied the US market up to now, and they say that they don't want to get involved in dealing with foreign tax jurisdictions. It's up to us to suggest how to structure the deal so they don't have to register. Can you tell me whether this can be managed, and if so how the transactions will be dealt with?

Second, once the plant is up and running, there will be a need for periodical maintenance and repair. We intend to establish a store of spare parts in the UK so that there will be minimal delay in carrying out any necessary work and getting the plant running again. Some of the work can be carried out by our own people or by sub-contractors, but it's possible that the supplier's engineers may be required to come over from time to time as well. Again, they don't want this to oblige them to register for VAT here.

Third, an alternative structure has been suggested whereby we lease the equipment from an American bank instead of buying it outright. The plan seems to be that we will sign a contract with the American head office of the bank for a five year lease of the

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6. *Continuation*

equipment. This will be purchased and owned by the American head office, and we will pay them lease rentals in equal monthly amounts over the period. At the end of five years, we expect that the plant will be at the end of its useful life and will be sold for scrap. We will receive a rebate of lease rentals equal to 90% of the proceeds of the scrap sale. I want to know the VAT treatment of this arrangement.

Please explain how much Duty and VAT will be payable on these transactions, when it will be payable and who has to pay it.

I look forward to your views on all the above subjects. I may have to talk this over with the US company's accountants, so if you have any legal references I can quote to them, please include them in your letter.

Yours sincerely

D Johnson

You are required to draft a letter replying to your client and providing advice in relation to Customs Duty and VAT on the transactions outlined in the letter from your client. (20)

7. You are a VAT specialist at a firm of Chartered Tax Advisers. You have been asked to make a presentation to a meeting of local traders and professionals on the subject of "carousel fraud". Your presentation should include explanations of "contra-trading"; measures taken by the UK to reduce losses from carousel fraud; steps which traders should take to avoid being associated with carousel fraud; and the consequences for them if their transactions have unwittingly been part of a fraudulent supply chain.

You are required to prepare detailed notes for your presentation. (20)