



November 2018 Examination

PAPER 6

VAT

Part I Suggested Answers

Q1 (3 marks – ½ mark for each)

- 1) Exempt.
- 2) Standard rated.
- 3) Standard rated.
- 4) Exempt.
- 5) Exempt.
- 6) Zero rated

Q2 (2 marks)

Item	Charge	VAT chargeable
Consultancy service	£3,000	£600 (1/2 mark)
Advertisement in local paper	£200	£40 (1/2 mark)
Train fares to and from client	£60	£12 (1/2 mark)
Printing costs	<u>£120</u>	<u>£24</u> (1/2 mark)
	£3,380	
Total output VAT charge		£676

Q3 (4 marks)

- Purchase of a car for the Finance Director
The car will be available for private use therefore no VAT can be recovered. (1 mark)
- Repair to Finance Director's car
The blocking order relating to VAT recovery on motor cars used for private use does not extend to repairs to the vehicle therefore the VAT can be reclaimed. (1 mark)
- Lease of a car for one of the sales team.
While the vehicle may be available for private use, the blocking order does not apply to vehicles that are being leased and by concession 50% of the input VAT on the lease payments can be reclaimed. (1 mark)
- Dinner for one of the Directors with a new French client
VAT on business entertaining, including entertaining of clients, is blocked from recovery, however this does not extend to entertaining overseas customers so the VAT can be reclaimed in full. (1 mark)

Q4 (4 marks)

1. Year ended 30 April 2017

70% - baseline recovery of 75% = -5% (1/2 mark)

VAT incurred of £56,000 / 10 (1/2 mark) x -5% = (£280) due to HMRC (1/2 mark)

Should have been included on VAT return to 31 October 2017 (1/2 mark)

Year ended 30 April 2018

85% - baseline recovery of 75% = 10% (1/2 mark)

VAT incurred of £56,000 / 10 x 10% = £560 (1/2 mark) due from HMRC (1/2 mark)

To be included on VAT return to 31 October 2018 (1/2 mark)

Q5 (4 marks)

1. The partial exemption recovery rate using the standard method is:

$100,000 / (100,000 + 350,000) = 22.22\%$ (roundup to) 23% (1 mark)

Based on how the office floor space is used 50:50, the standard method does not represent a fair reflection of how costs are consumed (1/2 mark) and accordingly a special method, based on floor space usage, would result in a 50% (1/2 mark) partial exemption recovery rate which would be a fairer apportionment.

2. The charity must apply to HMRC to use a special method. (1/2 mark).

It must provide HMRC with precise details of how its proposed method will work in practice. (1/2 mark)

It must make a declaration to the effect that to the best of its knowledge the method fairly and reasonably represents the extent to which the goods or services are used in making taxable supplies. (1/2 mark)

It must obtain written approval from HMRC before starting to use a special scheme. (1/2 mark)

Q6 (4 marks)

The sale of kites to a customer in the US will be a zero rated export of goods (1 mark).

In order for zero-rating to apply the supplier must ensure that they retain evidence that the goods have been exported This must be commercial or official evidence that demonstrates/proves that that the goods have left the UK (1 mark). ; Without such evidence that proves the goods have journeyed from the UK to a non EU destination, HMRC would deny zero rating and recoup the undercharged VAT from the supplier (1 mark). The goods must be exported within the specified time limits (1 mark).

Q7 (4 marks)

Conditions to be met to use the annual accounting scheme:

The annual value of taxable supplies is expected to be less than £1,350,000 (VAT exclusive) **(1 mark)**

The trader must not have ceased to operate the annual accounting scheme in the past 12 months. **(1 mark)**

The trader is not a member of a VAT group registration. **(1 mark)**

A trader must not have any outstanding VAT debt that continues to increase. Businesses with a small debt and who have agreed a repayment plan with HMRC may be able to join **(1 mark)**

Max 3 from any of the above

Benefits:

Less administration due to having only one VAT return per year **(1/2 mark)**

Cash flow advantage as the trader will know how much they are paying and when **(1/2 mark)**

Penalty for late VAT returns are less likely as only one VAT return per year **(1/2 mark)**

Max two benefits for 1 mark in total from above

Q8 (3 marks)

A zero rating relief can apply to the construction services in relation to a building to be used for a relevant charitable purpose (RCP) **(1/2 mark)**, this includes use as a village hall **(1/2 mark)**

The contractor carrying out the works is responsible for ensuring that the zero rating is in order **(1 mark)** Therefore the contractor must obtain a signed certificate from Green Gables Community Council certifying that they meet the conditions for zero rating as an RCP building, being used as a village hall. **(1 mark)**

Q9 (4 marks)

The Finance Director in this instance has made deliberate error but has not concealed it therefore the maximum penalty will be 70% **(1/2 mark)** of the potential lost revenue of £7,500. **(1/2 mark)**

The minimum penalty if an unprompted disclosure of the error is made is 20%, **(1/2 mark)** whereas the minimum penalty for a prompted disclosure is 35% **(1/2 mark)**. Therefore the Finance Director should disclose the underpayment to HM Revenue & Customs as soon as possible. **(1/2 mark)**

The extent of any reduction from 70% to 20%/35% will depend on the quality of the disclosure made by Violet Bakery Ltd. **(1/2 mark)**. Reductions in the penalty percentage are given for telling HMRC about the error, helping HMRC to quantify the error and providing access to records **(1 mark)**

Q10 (4 marks)

Customer A

The basic tax point is when the goods are fitted in the customer's property – 1 September (1/2 mark)

The receipt of the deposit of £1,000 in advance of this basic tax point creates an actual tax point. (1/2 mark) The VAT of £200 (assuming £1,000 is the VAT exclusive amount) on the deposit paid on 20 August 2018 must therefore be accounted for in the August 2018 VAT return (1/2 mark)

The invoice is raised and the balance paid at the same time as the basic tax point is created, 1 September 2018, therefore the balance of £300 of VAT falls within the November 2018 VAT return (1/2 mark)

Customer B

The basic tax point is when the goods are fitted in the customer's property – 29 August 2018 (1/2 mark) however an invoice is raised within 14 days of this meaning there is an actual tax point on 3 September 2018 (1 mark) at which point payment is also received. VAT of £750 on the full amount will therefore go into the November 2018 VAT return. (1/2 mark)

Q11 (4 marks)

VAT suffered in another EU member state can be recovered using the electronic cross border refund scheme (1/2 mark). The electronic claim must be completed and submitted via HMRC's website (1/2 mark) and it is then forwarded to the relevant member state to process and make the refund (1/2 mark).

The conditions for making a claim are:

- The claimant must not be registered or required to be registered in that member state. (1/2 mark)
- The refund is determined under the rules of that member state. (1/2 mark)
- The refund period must not be for more than one calendar year or less than three calendar months. (1/2 mark)

Emerald Consultancy must make the claim to HMRC by 30 September of the calendar year following the refund year at the latest. (1 mark)



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VAT

Part II Suggested Answers

1.

1)

If Penelope opts to tax the barn, she will be able to reclaim the £60,000 VAT incurred on the renovation costs. **(1 mark)** However as a consequence of opting to tax the property, she will need to charge VAT on the rental income **(1 mark)**. As the tenants are not expected to be VAT registered they will not be able to reclaim the VAT charged to them **(1 mark)**. Therefore the additional VAT charge is likely to be borne by the landowner. **(1 mark)** As this would be £10,000 per year, the benefit of opting to tax the properties would be eroded after six years and it would not therefore be beneficial to opt to tax them **(1 mark)**

2)

The sale of the freehold in a new commercial building is subject to VAT and therefore the sale of the first building will attract VAT at the standard rate. **(1 mark)**

The rental of facilities to store goods is an exception from the general exemption for property transactions and therefore income from the second building will also be liable to VAT at the standard rate. **(1 mark)**

3)

The construction costs of the shop will be standard rated, **(0.5 mark)** but the construction of the flat above the shop will be eligible for zero rating as the construction of a new dwelling. **(1 mark)** Costs relating to both parts should be apportioned between standard and zero rated supplies. **(0.5 mark)**

The rental of the shop will be exempt from VAT **(0.5 mark)** but Penelope could make it subject to VAT by opting to tax the property. **(0.5 mark)**

The rental of residential property is always exempt from VAT **(0.5 mark)** and any option to tax over the whole property would not affect this part. **(0.5 mark)**

Income from renting chairs to hairdressers is excluded from the exemption and is therefore subject to VAT at the standard rate. **(1 mark)**

4)

Where expenditure items in the financial statements include amounts of irrecoverable VAT, the gross cost of these items should be included as expenditure. **(1 mark)**

Amounts of VAT due to be paid to HM Revenue & Customs but not yet settled, would appear as a liability in the total value of creditors. **(1 mark)**

2.

1)

In order to qualify as a transfer of a going concern, the sale of a business must meet the following conditions:

- The business must be a going concern;
- The assets must be used by the purchaser with the intention of carrying on the same kind of 'business' as the seller;
- Where the seller is VAT registered, the purchaser must also be or become VAT registered;
- Where only part of the 'business' is sold it must be capable of operating separately;
- There must not be a series of immediately consecutive transfers of 'business';
- If the sale includes land with an option to tax, the purchaser must also opt to tax the land and confirm that their option will not be disapplied.

(Any five of the above 1 mark each – 5 marks total)

2)

The sale of shares does not constitute a transfer of a going concern as the assets of the business remain in the ownership of the business itself. **(1 mark)**

The potential sale of assets would qualify as a transfer of a going concern as sufficient is being transferred to enable the purchaser to carry on the same kind of business and the purchaser is VAT registered. **(1 mark)** There is no stipulation as to how long a business must continue once transferred and therefore closure in 3 months would not prevent the transfer from qualifying. **(1 mark)**

3)

'Negligence' is the breach of a legal duty to take care, which results in often unintentional damage to another. **(1 mark)**

To establish negligence, the client must prove that:

- The adviser owed a duty of care; and
- There was a breach of that duty to take adequate care; and
- The client suffered loss or damage as a result.

(1 mark each)

3.

1) Default surcharge will apply as follows:

VAT period ending	Amount due	Calculation
31 March 2017	£1,200	First late return – no surcharge due (1/2 mark) Surcharge liability notice issued, if further defaults in the next 12 months penalties may arise (1/2 mark)
30 June 2017	£3,400	A 2% penalty is due for the second default $2\% \times £3,400 = £68$, (1 mark) but this is not levied as it is less than £400 (1 mark) A surcharge liability extension notice is issued, extending the default surcharge period to 30 June 2018 (1/2 mark)
30 September 2017	£9,000	A 5% penalty is due for the third default, penalty of £450 is due ($5\% \times £9,000 = £450$) (1 mark) . The surcharge liability period is extended to 30 September 2018 (1/2 mark)
31 December 2017	(£1,000)	Nil surcharge – does not apply to repayment returns (1/2 mark) But the surcharge liability period is extended again (1/2 mark) .
31 March 2018	£6,280	A 10% penalty is due for the fourth default (the repayment return did not affect the penalty %) (1/2 mark) . Therefore £628 ($£6,280 \times 10\%$) is due (1/2 mark) . The surcharge liability period is extended to 31 March 2019 (1/2 mark) .
30 June 2018	£120	A 15% penalty is due for this fifth default (1/2 mark) . But $£120 \times 15\% = £18$ (1/2 mark) , the penalty is increased to £30 as this is the minimum charged (1 mark) . The surcharge liability period is extended to 30 June 2019 (1/2 mark) .

(10 marks total)

2)

If the request to transfer papers does not come from the client direct, the member should obtain written consent from his former client prior to providing papers to a successor. **(1 mark)**

Where documents on the member's files belong to the client, the member is required to provide these, subject to any lien the member may have. **(1 mark)** Where the original documents are handed over, the member should first take copies, so that he can maintain proper professional records. **(1 mark)**

Where documents belong to the member, the member should cooperate in providing copies of documents relevant to the client's ongoing tax affairs. **(1 mark)** If a significant amount of work in providing copies is required or if it is provided for in the member's engagement letter, a reasonable charge may be made. **(1 mark)**

If there is a risk that the former client may use the information provided to support a claim against the member, the member should consult his professional indemnity insurers and consider whether to take legal advice. **(1 mark)**

4.

Accountant Firm
Road
Town

Margaret Whippy
Ice cream factory
Road
Town

Date

(1 mark – presentation)

Dear Ms Whippy

Thank you for your letter regarding the VAT registration of your business. You raise a number of points which I will address in order below.

1) *Which items of income should be included within the calculation of liability to register for VAT?*

The liability to register for VAT is determined by the value of a person's taxable supplies. This includes both standard rated and zero rated items so the income from both ice cream and yoghurt would need to be included in your calculation. **(1 mark)**

Income from employment is not within the scope of VAT and your wages can therefore be excluded. **(0.5 mark)**

The grant funding, lottery win and dividend are not consideration for supplies and can be omitted. **(1.5 mark – 0.5 marks each)**

Only income which is made in the course or furtherance of your business is capable of being a taxable supply and we do not consider that one sale of toys within an 18 month period could be described as a business activity. **(1 mark)**

The disposal of capital assets is also excluded from the calculation because it would be distortive to include these amounts. **(1 mark)**

2) *From what date should a VAT registration have been effective?*

You are required to register for VAT if, at the end of any 12 month period, the value of your taxable supplies exceeds £85,000. **(1 mark)** The table below shows your annual taxable turnover in the 3 months prior to exceeding the threshold and the month in which the threshold was breached.

12 months ending	12 month taxable turnover
31 December 2017	£77,500

31 January 2018	£79,000
28 February 2018	£81,300
31 March 2018	£85,500

(2 marks – 0.5 marks each period)

As the threshold was exceeded in March 2018 you should have notified HMRC of this by 30 April 2018. **(1 mark)** You would have been registered from 1 May 2018. **(1 mark)**

3) *Position for output tax due on sales*

Only your ice cream sales would be liable to standard rated VAT and in the months of May and June you had sales of £11,500. The VAT due on this would be $£11,500 \times 1/6 = £1,916$. **(1 mark)**

As your customers are themselves in business, they may be VAT registered and able to reclaim any VAT you charge them **(1 mark)**. In which case, they may be willing to accept a VAT only invoice for £2,300 ($£11,500 \times 20\%$) and you would not bear May and June's VAT as a cost. **(1 mark)**

4) *VAT on pre-registration expenses.*

So far as services are concerned, VAT may only be reclaimed where the service was received in the six months preceding registration. **(1 mark)** As the legal fees you mention were at the start of your business, I assume that these will not be within the six month period. **(0.5 mark)**

Goods must be received in the four years preceding the registration date and must still be on hand at the time of registration. **(1 mark)** Therefore, VAT on the first mixing machine purchased will not be eligible as it has been sold. **(0.5 mark)** but VAT on the replacement machine is within time. **(0.5 mark)** Only VAT on packaging which was still in stock at the time of registration will be eligible for a reclaim. **(0.5 mark)**

I hope this answers your queries, but please let me know if you need any further information.

Yours sincerely,

A Adviser