



## **November 2021 Examination**

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**PAPER 6**

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**VAT**

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Part I Suggested Answers

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1. (4 marks max)

There must be reasonable grounds for believing that the value of taxable supplies will not exceed £1.35 million in the next 12 months. (1/2 mark)

Manning & Co's turnover is £850,000 in the year to 31 January 2021 and expectation of 20% rise per annum means the turnover for the following year will be £1,020,000 and the year after £1,224,000 – the turnover condition will therefore be met to allow Manning & Co to use the scheme. (1/2 mark)

The business must have no outstanding VAT returns or debts due to HMRC (1/2 mark). Manning & Co have always submitted VAT returns on time. While there was a debt due to HMRC, it was settled by 31 March 2020. Therefore this condition will be met. (1/2 mark)

The business must not have committed any VAT offences in the previous 12 months (1/2 mark) and the business must not have had VAT penalties relating to dishonestly evading tax in the previous 12 months (1/2 mark) Both these conditions are met also.

As all the conditions have been met, Manning & Co can use cash accounting (1/2 mark)

The main advantage of the scheme is automatic bad debt relief (1/2 mark). This will help as Manning & Co have a number of late paying customers and older debts therefore output VAT does not have to be paid to HMRC until customers pay. (1/2 mark)

2. (2 marks max)

Once a farmer is within the flat rate scheme no VAT returns are made. (1/2 mark)

A flat-rate addition of 4% is added to the selling price of supplies of 'designated activities' (1/2 mark), but only if the customer is a VAT registered person. (1/2 mark)

The farmer keeps this 4% flat-rate charge as 'compensation' for losing the ability to recover input VAT (1/2 mark)

The VAT registered customer recovers the 4% flat-rate charge (1/2 mark) as if it was input tax provided they have an invoice from the farmer showing the 4% charge and his farmers' certificate number. (1/2 mark)

3. (4 marks)

- 1) Reduced rated (1/2 mark)
- 2) Zero rated (1/2 mark)
- 3) Zero rated (1/2 mark)
- 4) Standard rated (1/2 mark)
- 5) Zero rated (1/2 mark)
- 6) Standard rated (1/2 mark)
- 7) Zero rated (1/2 mark)
- 8) Standard rated (1/2 mark)

4. (4 marks)

- 1) Rhodes Property has both taxable and exempt income and so is partially exempt and therefore may not be able to recover all input VAT incurred. (1/2 mark)

Input tax incurred on expenses related to making taxable supplies is recoverable. (1/2 mark).

Input tax incurred on the expenses related to making exempt supplies is irrecoverable. (1/2 mark)

Input tax which relates to both taxable and exempt activity is only partially recoverable. (1/2 mark)

If the de minimis limits are met, Rhodes Property may be able to reclaim the VAT related to exempt activity. (1/2 mark)

(Max 2 marks available)

- 2) VAT of £800 on the repair to the holiday property roof is recoverable as it relates to taxable activity (1/2 mark) and the VAT of £600 on legal fees for the residential lease is irrecoverable as it relates to exempt activity. (1/2 mark)

However the de minimis limits may allow the exempt related VAT to be reclaimed.

The simplified de minimis test 1 is met as:

Total input tax of £1,400 is no more than £625 per month (£1,875 for quarter) (1/2 mark)

and

The value of exempt supplies is no more than 50% of total supplies (1/2 mark)

So, the total VAT of £1,400 can therefore be recovered from HMRC (1/2 mark)

Alternatively, under the standard de minimis test, input tax on the legal fees is fully recoverable as it is no more than £625 per month and no more than 50% of input tax incurred (1/2 mark).

(Max 2 marks available)

5. (4 marks)

- 1) Red Ltd, Blue Ltd and Green Ltd can all form a VAT group as Red Ltd has a controlling interest (1/2 mark) in both Blue Ltd and Green Ltd and they all have UK fixed establishments (1/2 mark).

Despite Red Ltd also having controlling interest (1/2 mark) in Pink Corp, it cannot be part of the VAT group as it does not have a UK fixed establishment (1/2 mark)

- 2) Max 2 marks for part 2)

A VAT group is treated in the same way as a single entity VAT registered on its own (1/2 mark)

The representative member of the VAT group is responsible for all VAT accounting (1/2 mark)

All members are jointly and severally liable for any VAT due, not just their own share (1/2 mark)

Supplies between members of a VAT group are disregarded. (1/2 mark)

An exempt member joining the group may make the whole group partially exempt (1/2 mark)

Voluntary disclosure limit applies to group as a whole (1/2 mark)

6. (4 marks)

The penalty for failure to notify is based on the behaviour of the person concerned and is a percentage of the 'potential lost revenue' (PLR). (1/2 mark)

If Peter had registered for VAT at the correct time, output VAT would have been due on the income in:

July of £10,000/6 = £1,667 and

August of £9,000/6 = £1,500

Total Potential Lost Revenue (PLR) is therefore £3,167. (1/2 mark)

This would likely fall into the "deliberate but not concealed failure" (1 mark) category so the maximum penalty is 70% of the PLR, being £3,167 x 70% = £2,216.90. (1 mark)

Reductions in the amount of the penalty are available for both 'unprompted' and 'prompted' disclosures. (1/2 mark)

As Peter notified HMRC, this would be an unprompted disclosure meaning reductions are available – to 20% of PLR if deliberate but not concealed – penalty would therefore be reduced to £633.40. (1/2 mark)

7. (4 marks)

1. The freight company invoice alone is not sufficient to allow Charles & Co to reclaim the VAT (1/2 mark). However if Charles & Co have the C79 certificate from HMRC, then the claim for import VAT is valid. (1/2 mark)
2. Invoice for services was dated more than six months prior to the effective date of VAT registration so the VAT should not have been claimed (1 mark)
3. Invoice for goods dated within four years of effective date of VAT registration and still in use now, so claim is valid. (1 mark)
4. Provided expense is genuine business expense, VAT on expense incurred by an employee can be claimed by employer. (1 mark)

8. (2 marks)

The Australian supplier should not charge [either GST (Australian equivalent of VAT) nor] UK VAT on the invoice for the services received by the UK business.

The UK business must therefore account for UK VAT using a reverse charge adjustment by adding an amount equivalent to 20% of the sterling value of the services per the invoice, to Box 1 of their UK VAT return (1 mark), with the ability to reclaim the VAT via Box 4 on their UK VAT, subject to any partial exemption restriction. (1 mark)

9 (4 marks)

- 1) No basic tax point as continuous supply of services. (1/2 mark)

Actual tax point is date of invoice – 22 October 2021 (1/2 mark)

- 2) Basic tax point is date goods are delivered to customer - 23 July 2021 (1/2 mark)

Invoice issued in advance of basic tax point creates actual tax point - 21 July 2021 (1/2 mark)

- 3) Basic tax point is date survey report emailed to client - 16 September 2021. (1/2 mark)

Actual tax point is same as basic tax point as neither payment received nor invoice issue in advance of basic tax point, nor is invoice issued within 14 days of basic tax point – 16 September 2021. (1/2 mark)

- 4) Basic tax point when entertainer performs - 22 August 2021. (1/2 mark)

Actual tax point created when payment made in advance of basic tax point - 22 June 2021. (1/2 mark) Even though invoice is issued within 14 days of the basic tax point, the earlier receipt of payment overrides this to create the actual tax point.

10. (4 marks)

HMRC must offer Casey & Co a review of the assessment. Casey & Co then has 30 days to notify HMRC of their wish to have a review. (1 mark)

HMRC should carry out this review within 45 days or such longer period as is agreed with Casey & Co. (1 mark)

Casey & Co can still appeal to the First-tier Tax Tribunal if they disagree with the outcome of the review. Casey & Co can appeal to the tribunal within 30 days of the HMRC review. (1 mark)

Casey & Co does not need to request a review and can instead appeal directly to the tribunal within 30 days of the original disputed assessment. (1 mark)

11. (4 marks)

- 1) Reduced rating 5%. (1/2 mark)

Qualifying conversion of commercial property to dwelling (1/2 mark)

- 2) Standard rated – 20% (1/2 mark)

Although wholly non business activities carried on by the charity, the extension to the building is not classed as a new build. Works to the existing building including an extension are standard rated. (1/2 mark)

- 3) Standard rated – 20% (1/2 mark)

Works to construct new commercial property is standard rated. What Mrs C will do with the properties on completion is irrelevant. (1/2 mark)

- 4) Zero rating – 0% (1/2 mark)

Construction of a brand new property to be used for relevant residential purpose; nothing of the former property will exist. (1/2 mark)



## **November 2021 Examination**

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Part II Suggested Answers

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**12. (12 marks)**

**1(a) (1 mark)**

Big and Small Ltd had no input tax to repay in its December 2020 VAT return as the expiration of six months from the due date of payment had not yet been reached (1 mark)

**1(b) (2 marks)**

As at 31 March 2021, Big and Small Ltd had made one payment only for £25,000. This was not specified against any particular invoice so the payment should be allocated to the oldest invoice first.

As such:

Invoice dated 15 August:  $6,000 \times (11,000/36,000)$  OR  $11,000 \times (1/6) = £1,833.33$  (1 mark)

Invoice dated 5 September: £3,600 (1 mark)

Total input VAT to repay to HMRC = £5,433.33

**1(c) (2 marks)**

As at 30 June 21, Big and Small Ltd has made two further payments: £12,000 followed by £25,000.

£11,000 should be allocated to the remaining 15 August invoice.

£20,000 should be allocated to the 1 September invoice (VAT-free).

£6,000 should be allocated to the 5 September invoice.

As such:

Invoice dated 15 August: £1,833.33 to recover (1 mark)

Invoice dated 5 September:  $3,600 \times (6,000/21,600)$  OR  $6,000 \times (1/6) = £1,000$  (1 mark)

Total input VAT to recover from HMRC = £2,833.33

**1(d) (2 marks)**

As at 30 September, Big and Small Ltd has made a further payment of £3,000.

As such:

Invoice dated 5 September:  $3,600 \times (3,000/21,600)$  OR  $3,000 \times (1/6) = £500$ . (1 mark)

Invoice dated 5 July 21: Input VAT to recover of £1,600 (1 mark)

Total input VAT to recover from HMRC = £2,100



**2) (2 marks)**

**(1.5 marks max, 2.5 available)**

The conditions for Trystich (as the supplier) to make a Bad Debt Relief claim are:

- It has supplied goods or services and has accounted for and paid the output tax to HMRC; **(1/2 mark)**
- The whole or part of the consideration has been written off in its account as a bad debt (i.e. there is an entry in the bad debt account); **(1/2 mark)**
- The value of the supply must not exceed its open market value; **(1/2 mark)**
- The debt itself must not have been paid or sold on; **(1/2 mark)**
- The debt must be at least six months old (i.e. six months have elapsed since the due date for payment as specified on the invoices being 5 March 2021 and 26 March 2021); **(1/2 mark)**

Provided the above conditions are met, Trystich can make a bad debt relief claim for £5,433.33 (£1,833.33 + £3,600) in the 31 March 2021 VAT return **(1/2 mark)**

**3) (3 marks)**

- 1) The tax practitioner owed them a duty of care **(1/2 mark)**. A tax practitioner owes a duty of care to those with whom they have a special relationship under the 'neighbour' principle **(1/2 mark)**
- 2) The tax practitioner breached that duty of care **(1/2 mark)**. This requires the claimant to show that the practitioner failed to do what a reasonable person would have done **(1/2 mark)**.
- 3) The claimant suffered a loss as a result of the breach. **(1/2 mark)**. The claimant must show that the loss would not have occurred but for the breach of duty **(1/2 mark)**.

**13. (18 marks)**

**1(a) (12 marks max, 13 marks available)**

**Answer in email format (1 mark)**

To: Miss Anderson

9/11/2021

Subject: Queries re: your properties/Future input tax recovery

Thank you for your email of 2 November 2021.

**Property queries**

Please find below the answers to the queries regarding your properties:

- 1) 20 High Street: It is not possible for you to revoke your option to tax (1 mark). This is because the option to tax can only be revoked within the six-month cooling-off period (1 mark). The other two conditions for revocation are not relevant to you considering you have only owned the building for a year.
- 2) 8 Mitre Square: you should charge VAT on the rental supplies (1 mark). Despite the fact you have not specifically opted to tax the building itself any option to tax over bare land will automatically extend to any building constructed upon it (1 mark). This would only be otherwise if you had specifically excluded the new building from the effect of the option and notified HMRC (1 mark). The fact that the accountancy firm has opted to tax the building is not relevant to the VAT treatment of your supplies, only to its own supplies (of subletting). (1 mark)
- 3) 107 Forder Drive: In order for you to exempt the supply of this building the developer must certify in writing that the building is intended for use as dwellings (1 mark). The certificate (form VAT 161D) must normally be given before the price for the grant to the recipient by the seller is legally fixed (e.g. by exchange of contracts). (1 mark)
- 4) 56 and 57 Allied Green: 56 Allied Green - the sale of the freehold in a commercial property less than three years old is automatically standard-rated (1 mark). However, if the charity provides a certificate to you stating that the building will be used for relevant charitable purposes the supply is zero-rated (1 mark). 57 Allied Green - VAT should be charged to the charity (1 mark). This is because an option to tax can only be disapplied where the building is intended for a relevant charitable purpose but not as an office (1 mark).

**1(b) (3 marks max, 4 available)**

**Future input tax recovery**

Input tax attributable to taxable property disposals is fully recoverable with no requirement to pay back any VAT historically recovered (1 mark).

Historic input tax is potentially affected in respect of the supply of 107 Forder Drive (assuming Mr Jakobs provides the required certificate) as this will be an exempt supply. (1 mark)

If this building is within the Capital Goods Scheme there will be a proportional adjustment of input tax recovered on purchase (or on the refurbishment costs) for the remaining intervals of the 10-year adjustment period. (1 mark)

Input tax on costs such as professional and legal fees which are directly attributable to the exempt disposal of 107 Forder Drive are irrecoverable unless the amount of input tax falls within the de minimis rules. (1 mark)

If you would like to discuss this any further, please do not hesitate to contact me.

Best wishes

VAT advisor

**3) (3 marks max, 5.5 marks available)**

Yes, it is possible for the advisor to act for both parties in a transaction such as this one **(1/2 mark)** provided the following conditions are met:

- The advisor is satisfied that the circumstances of the conflict can be managed. I.e by introducing safeguards (1/2 mark);
- Safeguards that may be considered include: appointing a separate team to act for each client, who maintain ethical 'walls' to prevent confidential information relating to one client becoming known to the team acting for the other **(1/2 mark)**; confidentiality agreements drawn up with each advising team (1/2 mark) and having an independent partner review the safeguards put in place (1/2 mark);
- There is adequate disclosure of all relevant facts to both clients; **(1/2 mark)**
- Both clients are given the opportunity to consider whether or not they wish the advisor to act or whether they wish to seek alternative representation; **(1/2 mark)**
- Where applicable, the advisor should consider seeking independent advice on whether it is appropriate for the advisor to act for both parties; **(1/2 mark)**
- If the member is unable to put separate teams and ethical walls in place, it will only be possible to act for both parties if there is sufficient mutuality of interest between the parties and hence no objection to the sharing of confidential information; **(1/2 mark)**
- Both clients agree in writing that the member can act for both parties; **(1/2 mark)** and
- No preference is shown in advising one against the other. **(1/2 mark)**

**14. (20 marks)**

**1) (2 marks)**

	£ (million)
Dr Bank/cash/debtors <b>(1/2 mark)</b>	720
Cr Income/sales <b>(1/2 mark)</b>	600
Cr VAT (20% x £620 million) <b>(1/2 mark)</b>	120

Plus **1/2 mark** for getting values correct

**2) (4 marks max, 5 marks available)**

Determine input VAT attributable exclusively to taxable supplies and recover in accordance with the normal rules. **(1/2 mark)**

Determine VAT attributable exclusively to exempt supplies and treat as wholly irrecoverable. **(1/2 mark)**

Determine VAT attributable to both taxable and exempt supplies and recover a percentage thereof in accordance with the following calculation:

$$\frac{\text{Value of taxable supplies in the period (excluding VAT)}}{\text{Value of total supplies in the period (excluding VAT)}} \times 100 \quad \textbf{(1/2 mark)}$$

The resulting percentage should be rounded up to the next whole number **(1/2 mark)** (except where the residual input tax is £400,000 per month on average or greater). **(1/2 mark)**

This calculation should be performed per quarter with an annual adjustment at the end of the partial exemption year. **(1/2 mark)**.

Share sales and Forex trading should be included in the standard method calculation as these could not reasonably be described as incidental to one or more of the business activities in the circumstances of the scenario described. **(1 mark for share sales and 1 mark for Forex trading)**

**3) (3 marks max, 3.5 marks available)**

If the standard partial exemption method does not produce a fair and reasonable result the business may want to use a special partial exemption method **(1/2 mark)**.

The business must apply to HMRC **(1/2 mark)** providing precise details of how the proposed method would work **(1/2 mark)**. HMRC will normally approve a special method provided it is fair and reasonable **(1/2 mark)**.

Written approval from HMRC is required before **(1/2 mark)** starting to use a special method. The business must make a declaration **(1/2 mark)** to the effect that, to the best of their knowledge, the method fairly and reasonably represents the extent to which goods or services are used in making taxable supplies. **(1/2 mark)**

**4) (8 marks)**

Staff employed exclusively on taxable activity = 850

Total staff = 875

Residual VAT recovery percentage:  $\frac{850}{875} \times 100$  **(1/2 mark)** = 97.14% **(1/2 mark)** if to two decimal places

Attribute VAT as follows:

<b>Cost</b>	<b>VAT (£)</b>	<b>Attributable to taxable (£)</b>	<b>Attributable to exempt (£)</b>
Raw materials (£82,000,000)	16,400,000	16,400,000	- (1/2 mark)
Factory cleaning, security and electricity (£3,680,000)	736,000	736,000	- (1/2 mark)
Factory equipment (£4,200,000)	840,000	840,000	- (1/2 mark)
Legal fees re new sales agreement with retailers (£28,000)	5,600	5,600	- (1/2 mark)
Legal fees re Forex dispute (£38,000)	7,600	-	7,600 (1/2 mark)
<b>Total directly attributable VAT</b>		<b>17,981,600</b>	<b>7,600</b>
		(x 97.14%)	(x 2.86%)
Rent of HQ (£3,000,000)	600,000	582,840	17,160 (1/2 mark)
Cleaning, security and IT services for HQ (£1,640,000)	328,000	318,619	9,381 (1/2 mark)
Electricity for HQ (£85,000)	17,000	16,514	486 (1/2 mark)
Office equipment for entire HQ (£360,000)	72,000	69,941	2,059 (1/2 mark)
Audit and CT compliance (£310,000)	62,000	60,227	1,773 (1/2 mark)
<b>Total residual VAT</b>		<b>1,048,141</b>	<b>30,859</b>
<b>Total VAT</b>		<b>19,029,741</b>	<b>38,459</b>

De minimis test:

Exempt input tax (£38,459) is more than £625 per month. (1 mark)

(exempt input tax is no more than 50% of total input tax but irrelevant as the first test is not met).

So, total recoverable input tax = £19,029,741 (1 mark)

**Note:** if candidate erroneously rounds up the residual percentage to 98% the maximum mark achievable is 7.5 marks. This assumes that the VAT on each cost item is correctly attributed to taxable/exempt/residual and that the calculation  $850/875 \times 100$  has been performed.

**5) (3 marks)**

This company does not meet the conditions to use either of the simplified de minimis tests **(1 mark)**.

Simplified test 1: Total input tax incurred is no more than £625 per month on average AND the value of exempt supplies is no more than 50% of the value of all supplies **(1/2 mark)**.

Input tax greatly exceeds £625 per month on average so this company fails the first part of the test **(1/2 mark)**

Simplified test 2: Total input tax incurred less input tax directly attributable to taxable supplies is no more than £625 per month on average AND the value of exempt supplies is no more than 50% of the value of all supplies **(1/2 mark)**

Total input tax incurred less input tax directly attributable to taxable supplies far exceeds £625 per month on average so this company fails the first part of the test. **(1/2 mark)**

## 15. (10 marks)

### 1) (5 marks)

The VAT liability of sales of adult cycling socks to all types of UK customers are standard-rated (1 mark); sales to the Swiss customer are zero-rated exports provided the conditions are met (1 mark).

The supply of samples is not a taxable supply if they qualify as commercial samples, which these socks appear to be, so they are excluded from calculating whether the VAT registration threshold has been exceeded. (1 mark)

Otis has not exceeded the VAT registration threshold as at 30 Sep 2021 (1 mark). His taxable turnover in the rolling period 25 Mar-30 Sep totals £82,000 and there was no expectation of exceeding the £85,000 limit in the next 30 days alone. (1 mark)

### 2) (5 marks max, 6 marks available)

#### Advantages:

- Principally to recover input tax. Otis would not have been able to present the customs clearance agent with his VAT number/EORI number so the goods would have been cleared under the agent's EORI number. As such, Otis could not recover the import VAT shown on the agent's invoice, nor the VAT on the rental of the storage unit nor on any other costs (such as the design and maintenance of the online shop) (1 mark).
- Credibility. VAT-registered businesses have a degree of credibility that non-registered traders may not have and they can appear bigger than they actually are. Some businesses (particularly overseas business customers such as the Swiss retailer) will only deal with other VAT registered businesses. (1 mark)
- To avoid late registration penalties. (1 mark)
- Exporting - Otis will need its own EORI number (and hence a VAT number) to export the socks to the Swiss retailer so registering for VAT early would be good preparation. (1 mark)

#### Disadvantages:

- Output tax will be charged on all sales liable to VAT at the standard rate. This increases prices by 20%. For Otis's online private consumers this may make the price unattractive. (1 mark)
- VAT administration. VAT registered businesses must file VAT returns (usually on a quarterly basis). This is an additional significant compliance burden for Otis. (1 mark)