THE CHARTERED INSTITUTE OF TAXATION

The Chartered Tax Adviser Examination

May 2008

PAPER IID – INDIRECT TAXATION

Suggested Answers

QUESTION 1

File Note: North & West Coastal Quarry Supplies Ltd
Subject: Aggregates Levy on New Contracts

Liverpool

Gravel supplied in the UK will be subject to the levy at a rate of £1-95 per tonne (£1-60 per tonne prior to 1 April 2008), which can be apportioned for amounts of less than one tonne. (s16 FA 2001)

The tax point is when the gravel becomes subject to the agreement, provided that it is separately identifiable at the time when the agreement is entered into.

(s19(1)(b) and s19(6) FA 2001)

Isle of Man

Although the gravel is chargeable to aggregates levy, a tax credit can be claimed for levy paid on aggregate sent to the Isle of Man.

The company must hold documentary evidence that the aggregate has been delivered to the Isle of Man, for example:

- customer order and correspondence
- sales invoice
- transport documents
- packing lists
- delivery receipt
- payment details
- insurance details

The levy payable should be included on the return for the period and a corresponding credit can be claimed on the same return. Evidence of despatch from the UK must be obtained within three months of the aggregate leaving the UK. Otherwise an adjustment in respect of the credit claimed must be made on the next return.

(s30 (1) (a) FA 2001 and regs 13-15 SI 2002/761)

Sand used in ceramic process for Manufacture of Bricks

The company will be entitled to claim a credit as the sand is used in a ceramic process.

They must retain evidence of the use in this prescribed industrial process including:

- customer details
- description of product and its use
- references to invoices and weighbridge tickets
- customer declaration of use
- a declaration to the customer advising that credit has been claimed and that the customer is liable to civil or criminal penalties in the event of an incorrect statement.

Provided the required evidence is held, credit may be claimed on the same return as the levy is paid.

(s30 (1) (c) FA 2001, regs 13-15 and Schedule, SI 2002/761)

In the event of an incorrect claim, the company is liable to a penalty of 5% of the amount of the incorrect credit claimed. In the event of an incorrect declaration, there is a liability to a penalty of 105% of the incorrect credit claimed (s28 and para 9 and 9A Sch 6 FA 2001).

There is also provision for criminal and civil penalties for evasion of levy in appropriate circumstances. (Sch 6 FA 2001)

QUESTION 2

Contract 1

(i) There is no taxable insurance contract for UK tax purposes as the location of the risk is in Malta.

(ii) The loss relates to a monetary loss incurred by Premium Cover Ltd

(iii) There is no liability to register for Insurance Premium Tax or charge it under this contract.

(iv) The situation is similar to DSG International Insurance Services Ltd v The Commissioners for Her Majesty's Revenue and Customs (2007). In this case the repair contracts are for goods and customers based in the UK. The agent who sells the contracts for Premium Cover Ltd and the third party who administers the agreements are located in the UK and this potentially causes them to have an 'establishment' in the UK as well as Malta. However, using the decision of the DSG case the risk itself would be located in Malta at the head office of Premium Cover Ltd.

Contract 2

- In relation to buildings, a risk is situated in the UK if the property is located in the UK. Therefore, part of this contract is taxable in the UK and Insurance Premium Tax will be chargeable on it.
- The invoices for the premiums will need to be apportioned between the risk for the UK and the US properties and Insurance Premium Tax applied to the UK portion. The basis of apportionment should be reasonable and we recommend that it should be based on the values of the risk for the different properties.
- Because there is a taxable insurance contract CPIH Insurance Ltd will be liable to register for IPT in the UK within 30 days of forming the intention of receiving a taxable premium. Failure to notify HM Revenue & Customs at the right time would make CPIH Insurance Ltd liable to a penalty equal to 5 per cent of the relevant tax or £250, whichever is greater. The relevant tax is the tax for which they are liable between the period from the date on which they should have notified to the date actual notification was made.
- As CPIH Insurance Ltd is a non-UK insurer they must appoint a tax representative in the UK. A tax representative must be nominated within 30 days of such a requirement coming into effect. Failure to do so will make the client liable to a penalty of £10,000 subject to a reasonable excuse defence.

Service contracts, Warranties, Extended Warranties and Guarantees

- Service contracts

  A supplier normally undertakes to provide a certain level of service over a specified period in return for an agreed payment. Payment may be in a lump sum or at regular intervals but they will not be subject to IPT because the services are not supplied under contracts of insurance.

- Warranties

  A seller or manufacturer gives an undertaking to the effect that, provided the goods are used for the purpose intended, they will continue to work for a certain period of time and, if they cease to work, the provider of the goods will repair or replace the goods without charge to the purchaser. This is an undertaking that goods comply with the Sale of Goods Act and therefore the seller is complying with his legal obligations, rather than providing insurance. It is therefore not subject to IPT.

- Extended Warranties

  The insurer in return for a premium takes on the risk to the policyholder that the insured item will unexpectedly break or prematurely wear out. In that case the insurer undertakes to pay for a repair or replacement and this is a contract for insurance which is therefore subject to IPT. The rate applicable to these contracts will depend upon whether the person providing the contract is supplying it within the three trading sectors subject to the higher rate legislation which would make it subject to 17.5%; otherwise it would be subject to the standard rate of 5%.

- Guarantees

  Under a contract of guarantee the guarantor promises the creditor to be responsible for the performance of a third party in paying the debts to the creditor or performing their obligations. Guarantee fees are not liable to IPT. Contracts of guarantee cannot be contracts for insurance but have similarities. The key difference is the absence of a legal requirement for there to be an insurable interest.

QUESTION 3

Overview

The flat rate scheme is designed to make VAT accounting simpler for small businesses. Under normal VAT accounting, you are forced to monitor each individual cost incurred to claim input tax back from HM Revenue & Customs on your quarterly VAT return.

If you use the flat rate scheme, you simply pay over a proportion of the output tax you charge and do not recover VAT directly by relation to purchases, imports or acquisitions. This is because the flat rates are calculated to represent the net VAT you need to pay to HM Revenue & Customs. In other words, an allowance for input tax is built into the flat rates.

There are special rules when you buy high value capital goods to ensure you don't miss out.

Eligibility

You can apply to use the scheme if there are reasonable grounds for believing that you meet both of the following tests:

Test 1

Your **taxable turnover** (excluding VAT) in the next year will be **£150,000** or less and

Test 2

Your **total business income** (including VAT) in the next year will be **£187,500** or less.

In both cases you should ignore sales of capital assets and in the case of Test 2 you should include all exempt income and non-business income too (e.g. re: charitable or educational activities.)

Key Restrictions

- You are not allowed to join the flat rate scheme if you have any capital goods scheme items (single items of computer equipment over £50,000 or land and buildings over £250,000 net of VAT).
- You are not allowed to join the flat rate scheme if you are eligible to join a VAT group even if you have not formed one.

Reduction of 1% for new VAT registrations

If you are in your first year of VAT registration you get a 1% reduction in flat rate. This means you can take 1% off the flat rate you apply to your turnover, until the day before your first anniversary of becoming VAT registered.

Turnover for flat rate scheme

Basic turnover

This is principally for those who deal mainly with other VAT registered businesses. If you are used to accounting for VAT on an invoice basis, this can be the simplest to operate.

Cash based turnover

This method is based, not on the time you make the supply, but on the time you are paid for your goods or services. This can be helpful if you give extended credit or your customers pay you late.

Retailer's turnover

This is essentially the same as a retail scheme and is best if you are a retailer selling goods to the public.

What must I include in my flat rate turnover?

Your flat rate turnover is all the supplies your business makes, **including VAT**.

This means all of the following:

- the VAT inclusive sales and takings for standard rate, zero rate and reduced rate supplies;
- the value of exempt supplies, such as rent or lottery commission;
- supplies of capital expenditure goods; and
- the value of any despatches to other Member States of the EC if you are making intra EC supplies.

You exclude from your flat rate turnover:

- private income, for example, income from shares;
- the proceeds from the sale of goods you own but which have not been used in your business;
- non-business income and any supplies outside the scope of UK VAT; and
- sales of capital expenditure goods on which you have claimed input tax.

Bad debt relief

Bad debt relief arises if you account for and pay output tax on supplies for which you are not paid later. The general principles are that:

- you have not been paid by your customer and it has been six months since you made the supplies
- you have not accounted for and paid tax on the supply
- you have written off the debt in your accounts.

If you use the **basic** or **retailer** turnover methods of flat rate accounting, you can claim relief on eligible supplies at the **standard** rate of VAT, rather than the flat rate. This is because the flat rate includes an allowance for input tax which only occurs if you have been paid by your customer. As you will not have been paid, you will not have had full credit for any input tax.

If you use the cash turnover method of accounting your claim will be for the **difference** between the VAT you charged to your customer and the amount you would have declared to us had you been paid. This is because your flat rate takes account of input tax that you would otherwise have been entitled to if you had been paid by your customer.

Bad Debt Relief – Cash Turnover Method

Step 1 – Identify the VAT in the unpaid supply

e.g. Total price = £1,175

Therefore VAT= £175

Step 2 – Calculate the VAT that would have been paid under the flat rate scheme if your customer had paid you. That is the total owed (including VAT) multiplied by your flat rate scheme percentage.

£1,175 x (say) 10% = £117.50

Step 3 – Subtract the sum of step 2 from the sum of step 1

£175 - £117.50 = £57.50

Step 4 – £57.50 is your special allowance under the flat rate scheme. Include it in your VAT account in your next return.

£57.50 is added to the VAT deductible portion of your VAT account and creates a claim or reduces the VAT payable.

Record-keeping and invoicing requirements

You must keep a record of your flat rate calculation showing:

- your flat rate turnover for the VAT accounting period
- the flat rate percentage you have used
- the tax calculated as due.

This record must be kept with your VAT account.

You must still issue VAT invoices to your VAT registered customers. Your customers will treat these as normal VAT invoices. When you come to calculate the scheme turnover, do not forget to include the VAT inclusive total of any invoices you have issued into the method of working out turnover that you are using. You must keep copies of all sales invoices that you issue to your VAT registered customers.

Reclaim of VAT on capital expenditure goods

If you use the flat rate scheme, you can reclaim the VAT you have been charged on a single purchase of capital expenditure goods where the amount of the purchase, including VAT, is £2,000 or more.

You deal with these capital expenditure goods outside the flat rate scheme. This means that you claim the input tax in box 4 of your VAT return.

If the supply is:

- more than one purchase
- under £2,000 including VAT or
- of services

then no VAT is claimable, as this input tax is already taken into account in the calculation of your flat rate percentage.

Single purchase of capital goods?

The normal VAT rules are used to determine whether any particular supply is one, or more than one, purchase and whether supplies are of goods or services.

Examples of a single purchase are:

- **A computer package** (computer, printer, camera, scanner, speakers etc.) bought as one package is one purchase of capital expenditure goods. If the package costs £2,000 or more (incl. VAT) then input tax can be claimed.

- **Items of kitchen equipment** (a pizza oven, a fridge and a dishwasher) bought for a restaurant. If all the items are from one supplier at one time, then they count as one purchase of capital expenditure goods. If they are from three different suppliers, or at three different times then they will be three purchases and each must be £2,000 or more (inc VAT) to qualify for a reclaim of VAT.

Apportionments for private use

To help simplify the flat rate scheme, where VAT on capital expenditure goods is reclaimable, the intended use of those items is treated as wholly for taxable supplies. This means that you do not apportion input tax to cover any planned private or exempt use of the goods. This is different to the normal VAT rules.

Output tax due on disposal of capital expenditure goods

Where you have reclaimed input tax on capital expenditure goods, then you must account for output tax at the standard VAT rate (not at the flat rate) on the disposal price of those goods when they are eventually sold out of the business.

QUESTION 4

To: Tax Partner
From: VAT Manager
Date: 8 May 2008
Subject: Crosby & CoVAT Reconsideration and Appeal

Pre-assessment letter

It is the normal practice of HM Revenue & Customs to write to the taxpayer prior to issuing an assessment, setting out the basis for the assessment and the calculation. They normally allow three weeks for a response. At this stage Mr Crosby should provide any information he thinks has not been taken into account

Reconsideration

If Mr Crosby disagrees with any subsequent assessment, he can first request HM Revenue & Customs to reconsider the disputed assessment. This is an informal internal procedure carried out an officer independent of the officer who made the assessment

Such a request must be made within 30 days of the date of the assessment and the client should also request HM Revenue & Customs to extend the time limits for appeal to a VAT Tribunal.

It is HM Revenue & Customs practice not to enforce payment of the tax whilst the matter is under local reconsideration.

Time Limits for appeal

If the assessment is upheld following HM Revenue & Customs reconsideration, provided the reconsideration request was made within 30 days of the assessment, the taxpayer has a further 21 days from the date of the letter confirming the assessment in which to appeal to a VAT Tribunal. Alternatively an appeal can be made directly to a Tribunal within 30 days of the date of the assessment. (SI 1986/590 Rule 4)

Making an Appeal

An appeal can be made only in respect of matters listed in VAT Act 1994 s83.

However an assessment of output tax will fall within s83 (b). An appeal against a VAT assessment is a category 3 appeal. The burden of proof lies with the appellant provided the Tribunal is satisfied the assessment is made to the best judgement of HM Revenue & Customs

An appeal is brought by serving a notice of appeal at the appropriate Tribunal Centre.

Form Trib 1 may be used or the appeal can be notified by letter, which must contain the following details as required by SI 1986/590 Rule 3.

- name and address of appellant
- date of VAT registration and nature of business
- address of the HM Revenue & Customs office which issued the assessment
- date of the assessment and address to which it was sent
- grounds of appeal

A copy of the assessment and, if appropriate, a letter from HM Revenue & Customs extending the time limits must be attached. The notice must be signed by the appellant or his representative.

A proper officer at the Tribunal will acknowledge the appeal and notify HM Revenue & Customs

Payment of Tax

An appeal cannot be entertained unless the appellant has made all his VAT returns and paid any tax due. (VATA 1994 s 84(2)). However, HM Revenue & Customs apply this condition only to tax periods in dispute.

The VAT assessment must also be paid or deposited with HM Revenue & Customs unless they agree to the appeal being heard without payment on grounds of hardship. If HM Revenue & Customs oppose a hardship application, the Tribunal may hold a preliminary hearing to determine whether the appeal can be entertained without payment of tax (VATA 94 s84 (3)).

Where tax is paid or deposited and the appeal succeeds, the Tribunal may direct that the amounts are repaid together with interest at a rate that the Tribunal may specify (VATA 94 s 84(8)).

Costs of the Dispute

Costs are not generally recoverable in respect of the reconsideration process.

However, the Tribunal will usually direct that HM Revenue & Customs pay a successful appellant reasonable third party costs incidental to and consequent upon the appeal. There is no award of costs to cover the appellants own time spent on the appeal.

HM Revenue & Customs do not normally seek costs where they are successful except in complex or vexatious cases.

Further Advice

We can act as representative for the partnership in the appeal or provide further advice as necessary.

QUESTION 5

T Adviser
ICTA House
Oxford

1/x/08

Mr Verdoux
Tramp Ltd
Gold Rush Lane
London

Dear Mr Verdoux

INPUT TAX DISPUTES

I am sorry to hear of your problems with HM Revenue & Customs. In answer to your query, I set out below the general principles governing input tax recovery followed by a consideration of the specific points of the assessment.

Input tax recovery – basic principles

Input tax is VAT on goods and services supplied to a trader which are used or to be used for the purposes of his business. The amount to be claimed is the VAT properly chargeable and not the VAT **actually** charged where this is different. The supplies must normally be received in the accounting period in which the claim is to be made and the trader must hold a valid invoice or other satisfactory documentation to support his claim.

Input tax is then recoverable to the extent it is used or to be used in the making of “taxable” supplies by the trader. These would include services chargeable to UK VAT at zero, reduced or the standard rate as well as supplies made outside the UK which would be taxable if they were made inside the UK and certain “specified” financial supplies to non-EU clients. The supplies received must also not be subject to a specific input tax restriction.

Specific scenarios

(a) **Pre-registration VAT**

It is a general rule that the recipient of the supply must be a taxable person (registered or required to be registered under VATA 1994) at the time the VAT was incurred. However HM Revenue & Customs have discretion to treat VAT incurred before this time as input tax. VAT on goods bought up to three years before the date of registration **can** be treated as input tax provided:

- the goods have not been supplied or consumed by the trader before the date of registration;
- the goods were purchased for the purpose of the business carried on or to be carried on by the trader at the time of the purchase;
- a stock account is compiled (and preserved for such a period as HM Revenue & Customs require) showing separately quantities purchased, quantities used in the making of other goods, date of purchase and date and manner of subsequent disposals of both such quantities; **and**
- the VAT would be deductible under general input tax principles.

As HMRC must exercise their discretion reasonably, if you satisfy these conditions, you can rely on them allowing the concessionary treatment.

(b) **Rogue trader**

If the supplier is not a taxable person but shows VAT on the invoice, the officer is correct that the VAT is not input tax and you have no automatic right of deduction.

In practice however HMRC may allow a claim in these circumstances where they are satisfied that:

- the recipient of the supply is neither involved in nor has close knowledge of the supplier's business;
- it was reasonable for the recipient to consider that he had been lawfully charged VAT; and
- the claim is made in respect of goods and services genuinely supplied at the stated value.

Provided you can evidence the above we may be able to persuade HM Revenue & Customs to allow the concessionary treatment.

(c) **Pension fund costs**

The management of one's own employee pension scheme is seen as a part of a trader's normal business activities. If you are a VAT registered employer, and have set up a pension fund for your employees under a trust deed, the VAT incurred in both setting up the fund and on its day-to-day "management" is input tax. This applies even where responsibility for the general management of the scheme rests (under the trust deed) with the trustee, or the trustees pay for the services supplied.

However, you should ensure that invoices are made out to Tramp Ltd rather than the trustees as otherwise you will fall foul of the rules on evidence and HM Revenue & Customs may deny your VAT deduction.

For VAT purposes a clear distinction is made by HM Revenue & Customs between "management" and "investment" costs [Notice 700/17/02]. The former, which are related to running and administering the scheme itself, are seen as costs of the employer's business. The latter costs, however, related to administering the scheme's underlying investments and assets, are seen as pertinent to the pension scheme itself rather than to the employer and VAT on them will not be available for deduction.

Therefore the officer is correct to disallow the VAT on investment management services to the Scheme but, provided you have appropriate invoices made out in your name, you should be able to recover VAT on the actuarial service.

(d) **6 month consideration/payment reversal**

In relation to a supply made on or after 1 January 2003, where a trader claims deduction of the whole or part of the VAT on a supply as input tax but has not paid the whole or any part of the consideration for the supply within six months of the date of the supply (or if later the date on which the consideration for the supply became payable), then he must make an adjustment to his VAT account to disallow the relevant portion of the VAT. The amount of this negative entry is calculated by multiplying the VAT by the proportion of the total consideration not paid.

In this case Tramp Ltd has purchased goods for £23,500 (£20,000 plus £3,500 VAT) and reclaimed the full amount of VAT. However you have only paid £11,750 (leaving £11,750 unpaid). As you are beyond six months from the relevant date (the supply by Goddard) you must make a repayment of input tax to HMRC of:

£3,500 x 11,750/23,500 = £1,750 negative adjustment.

To the extent that you subsequently pay the remainder of the invoice you will be able to reverse the effect of this negative adjustment and claim the VAT.

Reward scheme

The goods or services on which the VAT was charged must have been supplied to the person seeking to claim the input tax. In the case of the reward scheme, the officer has perhaps taken the view that the cinemas supplied the tickets to your clients (who, after all, chose and attended the films) and that therefore the cinemas cannot also be making a supply to you.

The decisions in Baxi Group Ltd v Revenue and Customs Commissioners

[2006] EWHC 3353 (Ch) and *Revenue and Customs Commissioners v Loyalty Management UK Ltd [2007] EWCA Civ 965* have shown that this view is incorrect. In Loyalty Management UK Ltd, the company operated a reward service scheme for a set of retailers and arranged the redemption of points earned by customers with third party suppliers. The Court Of Appeal held that there was a single supply of redemption services from third party suppliers to LM UK Ltd notwithstanding the supplies direct to customers.

In the second case, Baxi operated a loyalty scheme for its installers whereby the installers earned points per boiler purchased and were able to redeem these against catalogue goods from a third party. Although the goods were supplied by the third party to the installers the court ruled (in accordance with the Court of Appeal in Loyalty Management) that there was also a single supply of services from the catalogue company to Baxi, incurred by the latter in running the reward scheme for the purposes of its business and therefore Baxi were entitled to deduct input tax on this supply.

With this in mind, I believe the officer was wrong to disallow your input tax claim as, per the tests in Loyalty Management UK Ltd:

(i) you made a payment to the supplier;

(ii) that payment was consideration for services supplied to you by the supplier (i.e. of enabling you to meet your obligation under the reward points scheme); and

(iii) those services were used in the course of your business.

There is the further problem of whether this input tax may be blocked due to the rules on client entertainment. As the officer has pointed out, there is a specific restriction on input tax recovery where costs have been used to provide “business entertainment” [SI 1992/3222, Art 5(1)].

The Commissioners view all forms of hospitality including food, drink, theatre and concert tickets as business entertainment. On the face of it the cinema tickets would fall into this category.

However, if the entertainment is not given gratuitously but is provided under a contractual obligation, it does not fall within the scope of the provision per *Celtic Football and Athletic Club Ltd v C & E Commrs, CS [1983] STC 470* and *C & E Commrs v Kilroy Television Company Ltd, QB [1997] STC 901.* Here you have a contractual obligation to provide the rewards which have been redeemed via your scheme and therefore you can recover the VAT as input tax.

Assessment challenge - mechanics

If you disagree with a VAT assessment you have two options which are independent of each other. You can request local reconsideration or you can appeal to the VAT and Duties Tribunal on the form Trib 1.

Local reconsideration

You can request a local reconsideration of the assessment decision within 30 days of the date of the assessment or decision which an officer previously unconnected with the decision will independently review it. He may confirm, overturn or revise the original decision.

You can apply for local reconsideration at any time even if you have **already** appealed to the Tribunal (see below).

VAT Tribunal

A VAT Tribunal is a court hearing and its decisions are binding. If the local reconsideration resulted in confirmation of the **original decision** the confirmation will give a date from which you must lodge your appeal within **21 days**.

If the local reconsideration resulted in a **revised decision** you may appeal within **30 days** of the date of the revised decision.

You may also appeal to a VAT Tribunal without asking for local reconsideration. If you do so you must lodge your appeal within **30 days** of the HMRC decision.

I trust this clarifies the points you were concerned about – please do not hesitate to contact me should you have any further questions

Yours sincerely

T Adviser

QUESTION 6

Smith & Co
11 High Street
Middleton
Surrey M1 2AC

13 May 2008

John Taylor
English Towns plc
City Road
London WC1 2EE

Dear Mr Taylor

VAT Group Registration

Thank you for your letter concerning the possibility of establishing a VAT group registration. I understand that you are aware of the main principles and consequences of VAT group registration and I have set out below the implications of a VAT group for the English Towns group of companies.

General Comments

All the group companies are eligible for inclusion in a VAT group since plc controls all the companies directly or indirectly. The UK companies are established in the UK and it is likely that the Cambridge office of Dortmund has sufficient human and technical resources to amount to a fixed establishment in the UK.

As you know, HM Revenue & Customs can refuse an application for group treatment on the grounds of protection of the revenue. However a refusal is unlikely in your case since any savings would simply follow from the natural consequences of a group registration.

English Towns plc (plc)

Plc's only income is from dividends, which are outside the scope of VAT. It is therefore not entitled to register for VAT on its own and currently cannot recover any VAT it incurs on its costs and expenses.

Plc could apply for a group registration with one or more of the other UK trading companies and you should consider forming a VAT group between, for instance plc and Birmingham. HM Revenue & Customs accept that VAT on holding company expenses can be treated as overhead input tax of the group registration as a whole. This includes VAT incurred on acquisition costs and share issues for raising capital Since Birmingham is a fully taxable company, this should enable plc to recover VAT incurred on its holding company expenses.

Plc would not be able to reclaim VAT on costs related to any VAT exempt activities, such as the sale of shares in subsidiary companies. However this is unlikely to have an impact on group recovery overall.

You should bear in mind however that if a group registration were formed, each of the group members would be jointly and severally liable for any VAT due from the group registration.

Manchester, Leeds and Newcastle

Inclusion of the other UK trading companies, Manchester, Leeds and Newcastle in a VAT group with Birmingham would avoid the need to account for VAT on sales of materials to these companies. This might achieve considerable administrative savings. It would also allow the submission of one consolidated VAT return for the group's trading activities. There may also be fewer visits by HMRC in the future, which will also reduce administration time.

You should however bear in mind the comments made above concerning joint and several liability of companies in a VAT group. This may be a particular issue in the case of Newcastle where there is a minority shareholder.

You would also need to calculate whether the total net VAT payments of the group registration would exceed the limits for monthly payments of VAT on account, currently £2 million per annum. This would accelerate VAT payments for the trading companies.

The partial exemption de minimis limits will apply to the VAT group as a whole. Both Manchester and Leeds currently benefit from these rules. It may be that the combined exempt input tax of Manchester and Leeds together would exceed these limits and result in a restriction on input tax recovery in the group.

Finally, a VAT group registration would require a new VAT number for all the companies. HM Revenue & Customs normally allow companies to exhaust stocks of stationery bearing cancelled numbers subject to a group undertaking to account for tax charged on those invoices.

UK Office of Dortmund

Dortmund is entitled to register for VAT in the UK since it has a business establishment in the UK and makes supplies outside the UK, which would be taxable in the UK.

It could register as part of a group registration. To register as part of a group it is required to have a fixed establishment in the UK. Fixed establishment for group registration purposes is a more stringent test than business establishment for single company registration. However as noted above, the scale of Dortmund's activities in the UK is likely to satisfy both tests.

Group registration would allow it to consolidate its VAT account into the group VAT registration rather than making a separate return and also to use the UK group VAT number.

However since Dortmund makes no taxable supplies, it will be regularly claiming repayments of VAT paid on its costs. In these circumstances it may be worth registering Dortmund under a separate number and submitting monthly repayment claims. Whilst this requires the preparation of a VAT return each month, clearly it will have a positive effect on cash flow. Additionally subject to the satisfaction of HM Revenue & Customs, it may be possible to register from an earlier date with a maximum of three years' retrospection. This would allow recovery of VAT incurred on costs from the date of registration, on goods held at the date of registration and services received in the six months prior to registration.

Summary

Provided you are comfortable with the aspects of joint and several liability I would recommend that you consider a VAT group between plc and Birmingham to allow plc to reclaim VAT on its costs.

As far as the other trading companies are concerned, more information concerning level of VAT payments and partial exemption is necessary to allow a comparison of the administrative benefits with possible VAT costs.

The UK branch of Dortmund should be registered as a single VAT registration to allow it to reclaim VAT on costs and expenses on a monthly basis and possibly make a retrospective claim.

If you need anything further, please contact me. Perhaps you could advise me once you have collated the additional VAT information required for the trading companies.

Yours faithfully

QUESTION 7

T Adviser
Loophole Lane
Dunroamin

1/x/2008

Mr Bone
Dog Ltd
221 Barker Street
London

Dear Mr Bone

IMPORT DUTY AND VAT CASH FLOW PLANNING

Many thanks for your letter asking for advice on imports into the UK and possibilities for managing paperwork and the duty and import VAT cashflow cost. From the information you provided I believe the following options are relevant

Customs warehousing

These arrangements, which you mentioned in your letter, are simply a storage procedure whereby the payment of customs duties and import VAT can be suspended or delayed when non-EU goods are stored in a defined location or under an inventory system authorised as a “customs warehouse”. Goods can be stored in a Customs warehouse for an indefinite period of time. There are two key types of warehouse, public and private, which differ as regards the responsibilities assumed by the different parties.

Responsibilities

If you make a declaration depositing goods in a warehouse you are responsible as “depositor” for ensuring that:

- the goods are sent directly to the warehouse shown on the declaration, **and**
- the customs warehousing procedure is discharged by appropriate declaration of the goods to another customs approved treatment or use.

If, as a “warehouse keeper”, you operate a warehouse, you are responsible for:

- the security and proper control of the warehoused goods, including maintaining stock records for those goods throughout the customs warehousing procedure and accounting for any shortage
- ensuring that the conditions of the customs warehouse authorisation are met
- fully co-operating with HM Revenue & Customs in their supervision of the warehouse authorisation, and

- allowing HM Revenue & Customs access to the warehouse premises, records and goods at all reasonable times.

Private warehouses (known as Types C, D and E) are for the storage of goods deposited by an individual trader, authorised as the warehouse keeper. He/she need not own the goods but must take on the responsibilities of the "depositor" as outlined above.

By contrast, a public warehouse (Type A) is authorised for use by a warehouse keeper whose main business is the storage of **other** traders' goods. A Type A warehouse keeper does **not** take on the responsibilities of the depositor.

Compliance burden

Public Warehouse

If you wish to use a Public Warehouse you must check with the warehouse keeper that it is authorised to store the type of goods you wish to deposit. As depositor you are then responsible for providing all the necessary details on the form entering the goods into the warehouse to enable the warehouse stock records to be updated (such as the quantity and a description of the goods).

Running a warehouse can represent a heavy compliance burden which will be reflected in the prices charged for depositing goods in a Public Warehouse.

Private Warehouse

If you wish to operate your own warehouse, you will first require UK authorisation,

which can be obtained on submission of a C1410 form to HM Revenue & Customs. You must:

- be established in the European Union;
- intend to use the warehouse primarily for storing goods;
- demonstrate that there is sufficient duty involved such that there is a genuine economic benefit in running the warehouse; and
- satisfy HM Revenue & Customs that you will meet any other conditions imposed

HM Revenue & Customs will then arrange to visit you to check your application. Provided they are satisfied that the conditions are met and that they have sufficient resources available to police the operation of your warehouse, they will issue your Authorisation Number which must be quoted on all customs warehousing entries, to your premises.

Types C, D and E

Type C is the basic private warehouse model. A premises or place is authorised as a warehouse and goods are subject to duty calculated at the rates applicable when the goods are **removed** from the warehouse into free circulation.
Type D differs only in that the duty and VAT on goods are calculated on the values, tariff and exchange rates applicable when the goods enter the warehouse.

Type E warehouses offer more flexibility by allowing traders to use their stock control system rather than any specific premises as the warehouse. Type E warehouses also offer you the choice of which values are used to calculate the duty and VAT on the goods (i.e. on removal or on entry). In return for this flexibility there are further conditions HM Revenue & Customs impose:

- the administration and organisation of your business must be sound and strictly managed;
- the company's accounts and stock controls must be robust and managed to ensure that all commercial transactions are properly handled and recorded;
- the system must be capable of identifying the location and quantity of a given item held under duty suspension at any stage under a controlled inventory system;
- the company must have a compliant revenue record (for example VAT returns and payments must be up-to-date);

- payment of duties must be secured by the deferment arrangements where simplified removal procedures are used
- your accounting system must be authorised by HM Revenue & Customs; and
- any changes to those parts of the business such as the structure, administration or accounting systems which directly affect the warehousing arrangements must be notified to HM Revenue & Customs in advance.

Record Keeping & Stocktaking

It is a condition of your customs warehousing authorisation that you maintain sufficiently detailed stock records to identify:

- receipt
- stockholding
- handling and
- removal

of warehoused goods held under the customs warehousing procedure using your authorisation number. The records must provide a complete history of the goods from the time of their entry to the warehouse to the time of their exit.

You must keep your stock records and any associated documentation for **at least 4 years** after the date of removal of the goods from the customs warehousing arrangements.

If you are a depositor in a public warehouse you must still maintain records that provide evidence of the details of entry to the customs warehousing procedure and removal from the customs warehousing procedure.

Although there is no obligation to conduct regular stocktakes, HM Revenue & Customs can require this periodically under their supervision.

Security

Security is not normally required on warehoused goods although HM Revenue & Customs may ask for financial security if they consider that the duty and VAT is at special risk. Should security be required it will need to be provided in the form of a cash deposit or banker's guarantee.

Customs Freight Simplified Procedures (CFSP)

Normally when you import goods, you need to complete a C88 import declaration and also attach supporting documentation, such as an invoice and a valuation declaration, when the goods arrive into the EC.

As an alternative to using these normal procedures; for entering goods to and removing goods from a customs warehouse you can apply for authorisation to use Customs Freight Simplified Procedures (CFSP). Under CFSP, formalities at the frontier are kept to a minimum with the bulk of fiscal and statistical data being supplied electronically to HM Revenue & Customs at a later date.

There are two types of procedure:

Local Clearance Procedure (LCP)

In warehousing, CFSP LCP can be used in two different ways:

(a) **Use of CFSP LCP at the frontier.** Goods can be removed from the frontier under transit and moved inland to a designated LCP premises (for example - your authorised warehouse). On arrival the transit will be discharged and the goods must be entered in your records. A full electronic CFSP supplementary declaration should then be submitted by the fourth working day of the month following entry into the records.

(b) **Use of CFSP LCP to remove goods from warehouse.** Goods can be removed via an entry into your customs warehouse stock records and Local Clearance records (which may be one and the same) followed by an electronic CFSP supplementary declaration.

Simplified Declaration Procedure

This allows the speedy release of goods from the frontier to the warehouse on acceptance of a Simplified Frontier Declaration (SFD). The frontier declaration must be followed by a supplementary declaration that must be transmitted to the authorities electronically.

SDP **cannot** be used to remove goods from a customs warehouse; you must use either LCP with CFSP or the standard C88 form.

Further possibilities or alternative – Duty deferment & SIVA

Once you have removed/imported the goods and calculated the duty due you can mitigate cashflow effects further by the use of the duty deferment scheme. This allows you to delay payment of the duty and import VAT until the 15th (or next nearest working day) of the calendar month following the date of removal. This is available to depositors in both types of warehouse and to importers who do not use warehousing and so could be considered as an alternative should the cost of warehousing prove unattractive.

HM Revenue & Customs require security in the form of a guarantee from an independent approved third party guarantor. Upon authorisation you are granted a Deferral Approval Number (DAN) which can be entered on removal/import documentation. The advantages are that you defer payment of the duty for 30 days on average, charges are taken with a convenient monthly direct debit and goods are cleared more quickly by HM Revenue & Customs as they do not have to wait for payment each time.

Simplified Import VAT Accounting (SIVA) can reduce the level of the deferment guarantee required as regards the import VAT on the goods. To obtain approval to use SIVA you must:

- have been VAT registered for 3 years;
- have a good compliance history for VAT;
- have a good payment history with HM Revenue & Customs;
- have sufficient financial means to meet any amount deferred under SIVA;
- have a 12 month record of international trade operations;
- have a good compliance record for International Trade.

[Notice 101 para 5.10]

Where reduced security applies, you must provide a schedule (form SIVA 2) of your anticipated deferred charges per calendar month in order to determine your level of guarantee and set a Deferment Account Limit.

Input VAT deduction

If you are registered for VAT and are the consignee on removal of the goods, you can deduct as input tax, subject to the normal rules, the VAT payable on imported goods removed from warehouse, for the purposes of your business. To reclaim this tax on your next VAT return you must hold official evidence that the VAT shown has been paid or deferred.

Evidence is normally in the form of a monthly VAT certificate on Form C 79. HM Revenue & Customs send this direct to your VAT registered address on or about the 12th day of the month covering transactions for the previous calendar month.

I trust this makes clear the different options available for mitigating paperwork and cashflow in relation to your planned imports.

Please do not hesitate to contact me should you require further clarification on any point.

Yours sincerely

T Adviser