



The Chartered Tax Adviser Examination

November 2010

VAT on Cross-Border Transactions & other Indirect Taxes

Advisory Paper

TIME ALLOWED – 3 HOURS

- You should answer all **SIX** 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.
- Unless otherwise indicated by the provision of additional table information, you may assume that 2009/10 rates and allowances continue to apply for 2010/11 and future years. Candidates referring to actual or pending rates and allowances for 2010/11 and future years will not be penalised.

1. Your client Jack Jones is a private equity investor, who is considering investing in a small UK utility company. The company owns a coal mine, a small wind farm and two power stations, one of which is a combined heat and power station. It produces electricity from coal and methane gas from the mine as well as from the wind farm. It sells waste coal as a solid fuel to wholesalers at £10 per tonne.

The company currently has a dispute with HM Revenue & Customs over a £1 million bad debt relief claim it has made which has recently been denied in writing.

Jack is concerned as to when and to what climate change levy applies and wishes to understand the position in relation to bad debt relief claims. He would also like to understand the mechanism for resolving the dispute with HM Revenue & Customs.

You are required to write a letter to your client addressing his issues. (15)

2. You are the VAT manager in an accountancy firm. Jack Willis, the chief accountant of one of your firm's clients, has written you the following letter:

Chris Turpin
Advisers & Co
Tax Buildings
Town

Reliable Insurance Group plc
Reliable House
Town

1 November 2010

Dear Chris

Our human resources department has just dumped a list of issues on my desk and I need your help. As you know, the group has a policy of moving people around the European operations, and also of supporting good causes in our social responsibility programme. The following people are being seconded in the near future:

- 1) Jacques Xepec, who is employed by our French subsidiary, will be working in the London office for six months. For simplicity, he will remain employed by the French company, and the UK holding company will reimburse the French subsidiary each month for the cost of his salary while he works here. The French subsidiary is registered for VAT in France.
- 2) Tamsin McAllister, who is employed by our London office, will be working for our Italian branch operation for eight months. The Italian branch will reimburse head office (the holding company of the group) for the cost of her salary each month. The Italian branch is registered for VAT in Italy, but it isn't a separate incorporated company.
- 3) Gregory Simpson, who is employed by one of our UK subsidiary companies, will be seconded to a third party German not-for-profit organisation for a year. The organisation is registered for VAT in Germany but is also involved in regulatory activities which are outside the scope of VAT, and it's those non-business activities that Gregory will be working on. In this case, the German organisation will pay a lump sum at the outset of the arrangement which will cover about half Gregory's salary for the year.
- 4) Jane Collins, who works for a different UK subsidiary, will be supplied on a short-term contract to a Polish company for three months. The Polish company is not currently owned by us but we are thinking of buying them. They will pay a fee which exceeds Jane's salary at the end of the three months. I believe that the Polish company is currently only making exempt supplies, so it isn't yet registered for VAT in Poland.

2. *Continuation*

- 5) Lastly, Zac Finesides is being seconded to us from our US associated company. For various reasons which need not concern you, we are not going to have to pay for his services either directly or indirectly. The US company will continue to pay his salary for the four months he is working in London.

As you know, the four UK companies in the Reliable corporate group are all group VAT registered with the holding company as representative member. We make mainly exempt supplies but we do have some recovery of overhead input tax and a few taxable activities.

For each of these secondments I need to know the VAT issues: whether anyone has to pay any VAT, if so who and when, whether it's recoverable, and what reporting requirements we have to watch out for. You can stick to the UK side of things because I've got local firms looking at the other end of each of the transactions.

I look forward to hearing from you.

Yours sincerely,

Jack Willis

You are required to draft a letter responding to Jack Willis. (15)

3. You are the indirect tax specialist at a firm of tax advisers. You have been asked to make a presentation to the group finance director, who is based in Australia, and the European sales director of Kee Products Ltd, a company incorporated in the UK. Kee Products imports into the UK kitchen products and cookware for onward sale to major retailers in the UK and mainland Europe. Currently the firm rents warehouse space and pays Customs Duty (the average rate of duty is 6%) and VAT on importation. There has been a very significant growth in the business and the current warehousing arrangements are unsatisfactory. The company is looking to acquire its own warehouse facilities in the Thames Gateway to house and distribute its product lines for distribution throughout Europe. The value of stock imported into the UK last year was £120 million and, on the average, stock was warehoused for 80 days.

The company already has in place an integrated accounting and stock control system, and has said warehoused stock sometimes needs to be repackaged to meet the needs of its customers.

You are required to prepare detailed notes for your presentation covering the requirements to be met by Kee Products Ltd to operate a customs warehouse, the type of warehouse appropriate to it, the responsibilities of a warehousekeeper, how movements in and out of the warehouse are dealt with and benefits which might accrue to Kee Products Ltd. (20)

4. The newly appointed finance director of Spexra plc, a very substantial group of companies, has written to you in the following terms:

"Dear Rupert

As part of my Institute's CPD training, I recently attended a conference directed at updating finance directors on current tax issues. One of the speakers was a tax barrister who spoke on abuse of law and its relevance to commercial enterprises. I confess that I found the topic somewhat beyond me, but it caused me to reflect upon the extent to which Spexra plc may be exposed in relation to the following arrangements set up by my predecessor (who, of course, is now the chief executive):

- 1) Our retail website advises purchasers who place an order for home delivery for any product (excluding books) which is priced at £18 or less will have that order fulfilled by Spexra Retail Services Ltd ("SRS"). SRS is incorporated and established in Jersey. Although the website is maintained by Head Office staff here in the UK, SRS processes and despatches the goods directly to consumers (who are mainly resident in the UK, but there are also sizeable despatches to people resident in Ireland, France and Holland) from stock held in Jersey. Payment is made to SRS and it handles all customer enquiries: in short, SRS is a self contained enterprise, with Head Office only providing it with specialist services, and management and financial support.

SRS's annual turnover is £75 million. It is not registered for VAT in the UK, nor elsewhere in the EC. The arrangements were effected in early 2001 to maintain our market share when some of our competitors adopted similar arrangements.

- 2) The Group has a very substantial personal loan brokerage service which is provided by Spexra Financial Services Ltd ("SFS"), a subsidiary company incorporated in Jersey. Through a panel of independent lenders, it arranges for the provision of personal loans to individuals resident in the UK. It has its own premises and staff, and is authorised to conduct such business in the UK. SFS vets and agrees commercial terms with panel lenders and it approves "in principle" loan applications before they are forwarded to lenders. Once the loans are approved by the lenders, it completes the loan documents (as agent for the lenders) and despatches them to Spexra plc for onward transmission to the borrower for signing. It deals with compliance matters relating to its credit licence and has overall control over the placement of advertising in the UK (principally in newspapers, Yellow Pages, etc). The annual advertising spend is £30 million, and the placement of advertising in the UK is handled by an independent advertising agency based in Jersey. SFS is not registered for VAT as its services are regarded as outside the scope of UK VAT.

Under a service agreement between Spexra plc and SFS, the responsibility for processing loan applications rests with Spexra plc. Our call centre staff initially take the personal details of a caller, the loan required, details of income, the estimated value of the applicant's home and other assets, etc - and then send an application pack to the caller. On receipt of a completed application pack, Spexra plc staff summarise the information, identify the most suitable lender for each applicant and undertakes credit and other creditability enquiries into applicants. Once satisfied, an offer form is prepared and transmitted to SFS. SFS then makes all the necessary arrangements to complete the loan. Under the service agreement, Spexra plc receives 60% of all commission receivable by SFS, net of its advertising spend. Spexra plc received commission of £72 million in the financial year to 30 September 2009. Spexra plc's services under the service agreement have been treated as exempt from VAT on the basis that we have acted as an intermediary in the provision of personal loan finance and I do not require you to comment on this treatment.

Continued

4. *Continuation*

These arrangements were put in place to ensure we did not suffer irrecoverable VAT on the very considerable advertising spend.

- 3) Spexra Leasing Ltd ("SLS") is incorporated in the UK, and is part of the Spexra plc VAT group. It acquires MRI scanners and other radiology equipment which is leased to another group company, Spexra Medical Services Ltd ("SMS") which is not VAT registered (nor is it part of the Spexra plc VAT group) since it provides VAT exempt specialist medical services. This arrangement was entered into to defer over an extended period the VAT cost on equipment acquired by SMS. I believe that the leasing charges are based on prevailing market rates.

Could you provide me with an explanation of the principle of abuse of law, the extent to which it may apply to the arrangements outlined and advise if there is anything else that we should do to pre-empt enquiries from HM Revenue & Customs.

Kind regards
Jonathan Client."

You are required to write a letter to your client in response to the matters that he has raised. (20)

5. You are an indirect tax specialist in a firm of accountants. Your firm has a number of Lloyds' syndicates as clients, and you have been asked to advise on the extent to which the following risks are chargeable to Insurance Premium Tax in the UK:

- 1) damage to or destruction of gas and oil installations in the North Sea;
- 2) travel insurance policies covering personal injury, illness, loss of personal effects and repatriation expenses incurred outside the UK;
- 3) professional indemnity insurance taken out by an international partnership of accountants which has offices in the UK, the Middle East, Europe (France, Germany, Switzerland and Luxembourg), Hong Kong, China and India. The international partnership's directorate is based in London and all international partners participate in the partnership worldwide profits. Local offices have separate partnership management committees responsible for the operation of their offices. The premium is initially payable by the London practice and is recharged to offices on the basis of their fees as a proportion of worldwide fees.

You are required to write a memo to your tax partner setting out your advice. (10)

6. You are a VAT consultant with a firm of accountants. You have been approached by an Australian businessman, Archie Cochrane, who is an international expert on satellite technology. He has approached European government agencies with a view to making supplies of consultancy services to them concerning their space programmes. He has been told that he must form a company within the EU in order to make these supplies and he has incorporated a company in the UK called Spacetech Ltd in order to meet this requirement.

His plan is for Spacetech Ltd to invoice the government agencies (who are all registered for VAT in their respective countries) for consultancy services. None of the customers will be based in the UK. Mr Cochrane himself will manage the company from Australia, corresponding with your firm about the administration of business by means of e-mail and telephone. There will be two other directors and they will hold regular board meetings at the offices of an Australian company owned by Mr Cochrane.

He will use independent consultants to do the work. Most of them will be based in Australia, and they will invoice Spacetech Ltd in respect of their services rendered. Spacetech Ltd has asked to use the address of your firm as its registered office, and intends to pay a fee for your firm to provide administration services (answering and forwarding mail and telephone queries, raising invoices, filing statutory returns, preparing accounts for statutory and management purposes). The company will not employ anyone in the UK.

Mr Cochrane expects that his consultants will incur accommodation and transport costs (including car hire as well as air transport) as they travel around Europe. The company will supply them with mobile telephones for use in the EU, under contracts with a UK supplier. They will also be able to use these contracts to connect to the internet. It is unlikely that the consultants will visit the UK, but they will use the phones all around the EU.

Some of the customers have expressed an interest in receiving training as well as consultancy. They envisage the consultants visiting their premises in different EU states and using their facilities to present courses to groups of employees, and where this occurs it will probably be a minor part of a larger project.

Mr Cochrane is concerned about whether his company will be allowed or required to register for VAT in the UK or elsewhere in the EU. He is also concerned to know what VAT the company may incur in the UK or elsewhere, and whether and how he can recover that VAT. He wonders if it will make any difference if, after the business has expanded, it begins to operate from its own office located in the UK with UK-hired administrative employees (but still using Australian consultants).

You are not required to consider any direct tax issues.

You are not required to give details of specific VAT treatments in other EU member states, but you should outline the likely issues that will arise in any member state based on the EU VAT Directive provisions.

You are required to explain the VAT issues that arise for Spacetech Ltd. (20)