

# VAT: Possible Solutions

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## Where we are...

- Many EU Member States, including the UK, recognise philanthropic activity by voluntary bodies and give tax relief on donations to support this activity
- BUT, there is no comparable tax relief on the expenditure by charities. This is illogical and can dramatically reduce, if not completely wipe out the benefit of the tax relief on donations

## Current position

- VAT system treats charities harshly
- “Outputs” relating to charitable activity are either non-business or business but exempt (some business activities but VAT input tax recovery allowed)
- Exemption sounds good but, for the charity, is bad news
- No right to input tax credit on almost all expenditure incurred by charities
- Effectively charities are treated as final consumers for VAT purposes

## VAT reliefs

- Some EU Member States give special VAT reliefs for charities.
  - National reliefs, eg:
    - ‘transitional’ reliefs by zero-rating or super reduced rates in some countries, eg UK and Ireland.
    - targeted refunds on particular expenditure (German refund scheme and UK listed places of worship scheme)
  - EU reliefs, eg:
    - Implementation of Article 13A(1)(f) of Sixth Directive
    - Implementation of Point 14 of Annex H of Sixth Directive
    - Only major ‘input’ relief at EU level is for lifeboats used for rescue at sea (Article 15(4)) – effectively a zero rate.

# So What Are the Options?

- (1) Radical reform of the present system – a new VAT deal for charities.
- (2) An EU wide system for refunding VAT to charities on their non-business ESSENTIAL expenditure.
- (3) Refreshing the present reliefs (including all the exemptions and transitional rates) and concentrating on incremental improvements, especially in the application of reduced rates. Using ECJ rulings to help promote a change in law

## Option (1)

- Move charities into VAT system, by abolishing exemptions in Article 13.
- All outputs become taxable, freeing up all input tax on related expenditure (ie cost components needed to fulfil their charitable objectives).
- Non-business activities taxed at reduced rate (to achieve a broadly neutral effect), ie:
  - In UK [17.5% standard rate], but where the tax base is reduced by extensive zero rates (from which charities benefit), would probably equate to a reduced rate of 2%-3%.
  - In a country with a 25% rate, but fewer reliefs, this would be higher, may be 4% - 5%.
- Problem is that foundations or charities that gives grants would have to pay VAT on the value of the grant

## Option (2)

- EU mandatory VAT refund scheme similar to those which apply in a limited number of countries to State and local Government bodies.
- Scheme would depend on calculating and paying a matching grant equivalent to some or all of the VAT incurred on ESSENTIAL expenditure.
- Easy to check and monitor.
- ‘Outside the VAT system’, and therefore not in breach of the Sixth Directive (any more than existing rebate schemes for State bodies, eg UK’s Section 33).

## Option (3)

- The various reliefs – particularly the scope and intention behind each of the social exemptions in Article 13 – need to be better explained and then properly implemented in all Member States.
- The reform of the reduced rates in Annex H should have presented a real opportunity but debate hijacked by Franco-German dispute on VAT on restaurant services. But existing Annex H reliefs should be implemented throughout EU
- Important ECJ cases (eg Kretztechnik) should be used to promote VAT recovery and possibly lead to change in law

# Conclusion

- Most charities can do more to take full advantage of existing reliefs, and by careful but not “abusive” planning, make the existing VAT system work better for them.
- There is still considerable scope for lobbying to secure incremental improvements and better (ie more favourable) interpretations of existing reliefs.
- BUT, we have seen evidence during the conference of the economic and social value of civil society activity – there should be a proper VAT review and, if necessary, a VAT refund scheme.