



A guide to VAT, tax and Gift Aid for independent hospices



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**Help the Hospices has
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Saffery Champness
CHARTERED ACCOUNTANTS

Help the Hospices is the charity for hospice care. We work with more than 200 local hospices to make sure that hospice care is there for everyone who needs it, helping people who are affected by life-limiting and terminal illnesses to live well.

As the national membership charity, we work with our members, and other organisations, to grow knowledge and expertise, tackle fear and challenge taboos and open up hospice care to more people.

Our work includes providing a wide range of training programmes, practical resources for hospice staff, influencing Government policy, fundraising initiatives and supporting quality care and good practice.

Help the Hospices welcome this guide by Saffery Champness, which will be a helpful resource for hospice staff on VAT, tax and Gift Aid.

VAT and tax is a significant cost to local independent hospices, and has a considerable impact not only on a hospice's strategic and business planning, but also on the day-to-day decisions made by staff across the hospice.

We work on behalf of our member hospices to lobby on VAT and tax issues to enable hospices to use public funds to do what they do best – provide care and support to those in need within the local community.

Craig Duncan
Director of Finance, Help the Hospices

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1 Introduction

It is a general myth that charities do not pay tax. When considering VAT nothing could be further from the truth. Charities seem to suffer the cost of irrecoverable VAT almost as a privilege of being a charity and providing essential services.

The reality is that VAT, being a tax on business transactions, does not sit comfortably with the diverse activities of voluntary organisations, many of which are grant or self-funded activities undertaken to meet charitable objectives.

The evolution of numerous reliefs introduced to ease the burden of VAT faced by charities has led to a complex and cumbersome tax, even for the most straightforward of charities.

Hospices are no different. Income generated by hospices includes standard rate and zero rate sales of bought-in and donated goods, exempt supplies of education and care services and non-business donations, legacies and grants. This diversity of activities results in a complex and challenging structure for VAT purposes, which requires each hospice to individually negotiate its VAT recovery procedure with HM Revenue & Customs.

Equally, it is essential that hospices optimise their ability to claim Gift Aid and to ensure they fulfil the related administrative requirements to substantiate claims. The

emergence of the retail Gift Aid arrangement in recent years has greatly increased the ability of hospices to claim Gift Aid. However, it is essential to ensure the retail scheme has been correctly implemented and all requirements are being met.

Similarly, charities must be aware of circumstances when their income may be taxable. The use of a trading subsidiary company to mitigate exposure to direct tax on trading activities is a common procedure. Again, however, it is vital that this mechanism is correctly adopted and administered.

This guide seeks to assist hospices in optimising the opportunities available in all of these areas to ensure the tax cost to the charity is kept to an absolute minimum. It is not intended for use as a comprehensive technical reference, but rather a user-friendly guide for finance and fundraising staff within the hospice network to ensure opportunities to mitigate VAT and tax costs are considered.



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2 Overview of VAT and charities

Value Added Tax (VAT) is a substantial cost to the majority of charities in the UK. The cost is incurred principally through a supplier charging VAT, which is irrecoverable by the charity. Although many medical supplies can be purchased VAT-free by hospices, the problem of VAT recovery applies to the majority of purchases made.

The charity VAT problem

VAT is a consumer tax levied on business transactions involving the supply of goods or services for a consideration. VAT does not sit comfortably within the voluntary sector, where the majority of income and activities for many organisations is received and undertaken for what are termed 'non-business' purposes. For example, a donation or legacy is not received in exchange for a supply of goods or services, and therefore these incomes are not business income for VAT purposes. Similarly, activities provided free of charge or funded by grant income are also non-business activities.

Whilst it is beneficial that no VAT needs to be declared on, or extracted from, such income, there is the disadvantage that VAT incurred on attributable costs and expenses cannot be recovered. It is a basic fundamental of VAT accounting that VAT incurred on costs and expenses can only be recovered when it is attributable to what is termed a 'taxable' supply. These are supplies made at the standard (20%), reduced (5%) or zero (0%) rate. This places a tremendous financial burden upon the voluntary sector, with an estimated cost of over £1 billion of irrecoverable VAT being suffered per annum.

When VAT is incurred on a supplier's invoice, the charity is required to consider whether the expense can be solely attributed to either a taxable, exempt or non-business activity. If it can, then the VAT will be either:

- Wholly recoverable (if relating to a taxable activity);
- Non-recoverable (if relating to a non-business activity);
- Subject to the partial exemption de minimis regulations (if relating to an exempt activity); or
- Partially recoverable if a general overhead.

Exempt incomes and activities

There are specific reliefs which exempt certain business incomes and activities from VAT. For example, health and welfare activities, educational activities, the staging of a one-off fundraising event, and raffles and lotteries undertaken by hospices are specifically exempt from VAT.

VAT incurred on costs relating to an exempt activity can only be recovered when it falls below two prescribed de minimis limits (this is explained further in section 5). As many activities undertaken by hospices are exempt from VAT or, as outlined above, are non-business for VAT, it is usual for the majority of VAT incurred to be irrecoverable.

Figure 1: The VAT liability of incomes and activities

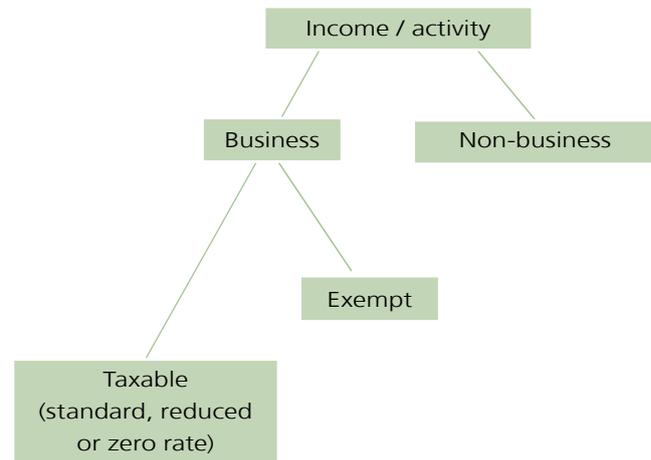


Figure 2: Exempt incomes include:

Health and welfare services
Education
One-off fundraising events
Lotteries
Domestic property rents

3 Overview of direct tax

It is a misconception that charities are without exception exempt from tax on their income. Unincorporated charities are liable to Income Tax and incorporated charities are liable to Corporation Tax unless the income derives from an exempt source and is applied solely to charitable purposes.

The exemptions include:

- Primary purpose trading
- Beneficial workers trading
- Small trades
- Donations
- Lotteries
- Investment income (eg bank interest, dividends, etc)
- Capital gains

Charities may be asked by HMRC to file a tax return, but otherwise they are not obliged to unless they have a taxable source of income. Charities with taxable income must notify HMRC, otherwise penalties may be charged.

Primary purpose trading is the provision of goods or services by a charity for consideration that is undertaken in the course of fulfilling the charity's charitable objects. Hospices providing care services in return for payment are carrying on primary purpose trading.

Trades that are ancillary to a primary purpose also fall within the exemption. A hospice may have a shop or a canteen for patients and their visitors, which may be ancillary to their primary purpose activities. If a shop is open to others, the profits will not be exempt unless it is a small trade (see section 5.5).

Small trades are those that are not otherwise exempt and which generate total annual income (from all the trades combined) of less than either £5,000 or the lower of £50,000 and 25% of the charity's total annual incomings. Charities may therefore be able to sell bought-in merchandise, Christmas cards, etc within the £50,000 de minimis, without having to trade through a subsidiary.

The lotteries exemption applies to those lotteries that are exempt within the meaning of the Gambling Act 2005, and are promoted with an operating licence under that act.

The sale of donated goods is not generally regarded as a trade for direct tax purposes and HMRC will not usually regard the profits as taxable. However, if the goods are materially altered prior to sale, then the charity will be carrying on a trade that will potentially be taxable unless any of the exemptions apply.

Where profits are not covered by any of the exemptions, the charity should consider undertaking the relevant activities through a trading subsidiary. They will remain taxable but, if the subsidiary donates the profit to the charity, no tax will be payable. The donation must be made no later than nine months after the subsidiary's financial year end.

Profits or income derived from exempt activities may still be taxable if they are applied to non-charitable purposes.

Also, where the charity incurs non-charitable expenditure or invests in non-qualifying investments or makes non-qualifying loans, an equivalent proportion of its otherwise exempt or non-taxable income/profits will be charged to tax. In this respect, a charity must take care to ensure that its investments and loans (including those made in or to trading subsidiaries) are qualifying and advice should be sought in advance.

Charities making payments (such as grants to any overseas persons (individuals, corporates, government bodies, etc) must take appropriate actions to ensure that the funds are applied to the intended charitable purposes.

4 Overview of Gift Aid

Gift Aid is a very valuable tax credit for charities as they can make a claim to HMRC for tax paid by the donor. The amount of the claim is equal to the basic rate of Income Tax on the grossed-up donation.

By way of example, assuming a basic tax rate of 20%, the tax credit claim on a donation of £800 would be £200, which is calculated as follows:

Figure 3

	£
Donation received	800
Tax credit at 20% of the gross donation	200
Gross donation	1,000

Gift Aid is also a tax-efficient means of giving to charities for higher rate and additional rate taxpayers, as they are entitled to reduce their tax liabilities or claim tax refunds. Assuming the same example as above, the donor's tax position would be as follows if the higher rate is 40% and the additional rate of 50%:

Figure 4

	Higher rate rate £	Additional rate £
Gross donation	1,000	1,000
Higher rate relief at 40%	400	
Additional rate relief at 50%		500
Basic rate relief paid to charity	200	200
Donor's reduction in tax or refund due	200	300

Figure 5

	£	£
Donation	800	800
Tax recalculation/refund	200	300
Net cost to the donor	600	500

Gift Aid credits are only available on cash donations from individuals (not from corporates or trusts) and only when the donor has given the charity a valid Gift Aid declaration. In order to be valid, the declaration must include the following:

- The name of the charity;
- The full name of the donor;
- The home address of the donor (house number / building name and full postcode are acceptable but it's preferable to have the full address);
- A statement that the donor wishes the charity to claim Gift Aid on the donation(s) and that the donor has paid or will pay sufficient UK Income Tax and/or Capital Gains Tax (CGT) for the tax year of the donation(s) at least equal to the tax that the charity and any other charities and community amateur sports clubs will claim on donations made to them by the donor in that tax year; and
- A note to identify the donation(s) covered by the declaration, which may be a one-off amount, but it is preferable to have one declaration covering all possible (past, present and future) donations.

Gift Aid claims may not be made or may be reduced where benefits are provided to the donor in excess of the permitted limits. For this purpose, charities are allowed to provide small value benefits, as follows:

Figure 6

Donations	Benefits limit
£100 or less	25%
£100 to £1,000	£25
£1,001 or more	5% (up to limit £500)

5 VAT liability of incomes and activities

5.1 General

In order to work out both whether VAT needs to be charged on an income and whether VAT incurred on related costs can be recovered, it is a fundamental requirement to establish the correct VAT liability of all incomes and activities of the charity and its trading subsidiaries.

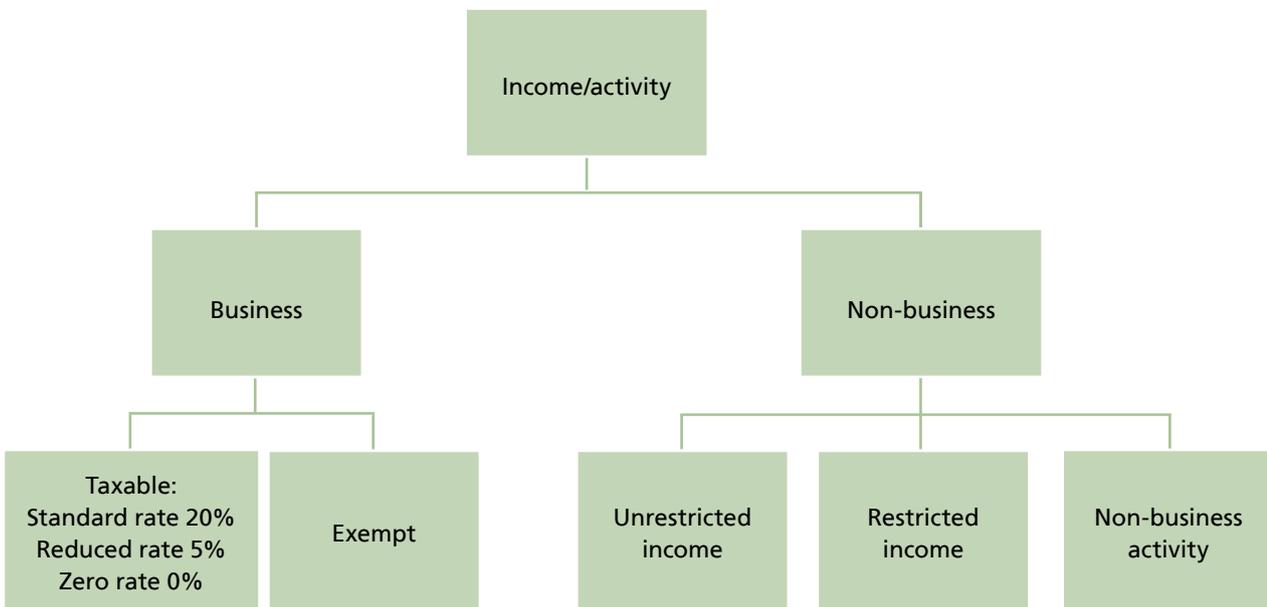
The first question to be asked is: is an activity a business or a non-business activity for VAT purposes? As a general rule, there is a business activity where the hospice or its trading company is supplying goods and/or services in return for a consideration, which is usually by way of money. An example of a business activity is where merchandise is bought in and sold. Similarly, the supply of catering services in the canteen to non-patients is a business activity.

A non-business income or activity exists where either money is given to the hospice with no requirement to make any supply in return (ie a donation, legacy, grant etc) or services are provided and funded by core funds or grant payments.

Where an income or activity is undertaken by way of business, there is a second question to ask: is the activity taxable or exempt from VAT? In this context, taxable means subject to VAT at either the standard (20%), reduced (5%) or zero (0%) rate. As a rule of thumb, all business activity will be subject to standard rate VAT unless it is specifically relieved in the VAT regulations as being reduced rate, zero rate or exempt from VAT.

These principles can be set out as follows:

Figure 7



5.2 Palliative care

There is often a general confusion over whether the core activities of a hospice are exempt from VAT or whether they are a non-business activity.

This may seem only of interest as a technical debate, however the distinction can be extremely important, particularly if capital building works are being undertaken. The reason for this is that certain construction costs can be zero-rated when the premises are used for non-business purposes by a charity. Exactly the same construction costs are liable to 20% VAT when used for exempt purposes. This being so, where capital building works are planned, it is vital that the hospice is confident on the VAT status of its core care activity as this may have a direct impact upon the level of VAT incurred and thus the ultimate cost of the works.

The VAT liability of the care services provided by a hospice will be dependent upon how they are funded and to whom they are provided.

The VAT legislation exempts from VAT, the 'supply' of welfare services by a charity. For these purposes, the definition of welfare includes the provision of care in a hospice. This being so, it would appear that the core care activity provided by a hospice is exempt from VAT when it is supplied under a contract for services to a funder (eg a local authority/the NHS etc).

However, by concession, HMRC accepts that where certain welfare services are provided by a hospice at 'significantly below' cost, these can be treated as being a non-business activity for VAT purposes.

The term 'significantly below cost' is met when the following criteria are met:

- The activities are subsidised by at least 15%;
- The subsidy is available to everyone; and
- The hospice is providing its care services to the individual and not to a funder, ie a local authority or the NHS.

So it can be seen there may be a distinct advantage in having the activities of the hospice categorised as a non-business activity rather than as an exempt activity.

5.3 Overview of typical incomes and activities

Taxable:

- The sale of donated goods (shops, auctions, eBay, etc) – zero rated
- The sale of bought-in goods for resale
- Commission on the sale of donated goods (retail Gift Aid arrangement)
- The sale of rags
- The supply of staff
- The administration/management fee to a subsidiary (unless in the same VAT group)
- Corporate sponsorship
- Catering sales to non-patients

Exempt:

- Raffle and lottery income
- Rental income
- Education and training
- Ticket sales to one-off fundraising events
- Corporate sponsorship for one-off fundraising events
- Palliative care services supplied under contract

Non-business:

- Palliative care (self-funded, grant funded or under welfare concession)
- Donations
- Legacies
- Grant income
- Bank interest and financial investment income (charity)

6 VAT registration

Although the majority of income received and generated by a hospice is likely to be either 'non-business' for VAT purposes (donations, legacies, grants, etc) or exempt from VAT (health and welfare services, fundraising events, lotteries and raffles), it is probable that the annual value of taxable income will still exceed the compulsory VAT registration threshold.

This should not be viewed as merely another regulatory matter to satisfy but, rather, as a financial opportunity to enable the hospice to recover a proportion of the VAT it is charged by its suppliers. Even where the annual value of taxable income is below the compulsory VAT registration threshold, a hospice can voluntarily register for VAT purposes.

6.1 Compulsory VAT registration

The VAT regulations require that at the end of any month, if the taxable income received by the hospice in the previous 12 months is greater than the compulsory VAT registration threshold (currently set at £77,000 per annum as at 1 April 2012), the hospice is required to notify HMRC within the next 30 days of its requirement to register for VAT purposes. Registration will then be effective from the first day of the month following this 30-day period.

For this purpose, taxable income is cash received for any supplies of goods or services which are liable to VAT at the standard (20%), reduced (5%) or zero (0%) rate.

There is a second test for compulsory registration. This requires that HMRC is notified of a requirement to register when, at any time (not just at the end of the month), there is a reasonable expectation that the taxable income of the hospice in the next 30 days will exceed the compulsory registration threshold (currently £77,000 per annum). This situation may arise, for example, if a commission/royalty agreement or similar contract is signed.

6.2 Voluntary VAT registration

Where the taxable income of the hospice does not exceed the compulsory registration limit, a voluntary registration can be sought. Providing some taxable income is generated by the hospice, irrespective of how low this may be, the VAT regulations provide for voluntary registration.

Clearly the principal (and perhaps the only) incentive for this will be a financial benefit where it is projected that



a material level of VAT could be recovered. However, considering the VAT recovery procedures (see section 7), where taxable income is absolutely minimal, it is unlikely that a reasonable level of VAT recovery will be achieved, thus making a voluntary registration unattractive.

6.3 Intending VAT registration

VAT registration can also be sought where no taxable income is currently generated, but it is intended that income will be generated at some point in the future. The benefit of seeking an 'intending registration' is the ability to commence recovery of VAT incurred on related costs, rather than waiting until after taxable income is received.

For example, if a hospice were planning to open its first shop selling donated goods (taxable zero rate income), an intending VAT registration could be sought as soon as expenditure is incurred. This could be several months before the shop actually opens, thus enabling recovery of VAT incurred on fit-out costs, etc.

6.4 Exemption from VAT registration

HMRC has the discretion to permit a hospice to be exempt from the need to register for VAT purposes even where the value of taxable (standard and zero rate supplies) income exceeds the compulsory registration threshold.

The exemption from VAT registration can be sought where the value of a small proportion of the taxable supplies are standard rate, providing that (if VAT registered) input tax to be claimed would normally exceed output tax due year on year.

If exemption from VAT registration is granted, the hospice is required to notify HMRC in any year when the value of output tax that would have been due exceeds the value of input tax that would have been recoverable in any 12-month period.

Although exemption from VAT registration saves the hospice the administration time in not quantifying and submitting VAT returns and also prevents the need to satisfy another regulatory body, it does however mean that the hospice will be financially disadvantaged in that it will not be able to recover any VAT it incurs on costs and expenses.

This being so, and particularly where there is a material value of zero rate income (ie shops), it is invariably a disadvantage not to be registered for VAT purposes and very careful thought should be given before exemption

from VAT registration is sought. It can be very difficult to persuade HMRC to allow a hospice to retrospectively register for VAT for any period when an exemption from registration has previously been granted.

6.5 VAT group registration

Where a hospice is a 'body corporate', ie limited by guarantee, it is able to jointly register for VAT purposes with its subsidiary trading company under what is termed as a VAT group registration.

Although there are some administrative advantages of completing and submitting only one VAT return, the principal benefits of a VAT group registration are:

- a) An ability to join the activities of the two entities together in order to improve the overall level of VAT recovery for the hospice; and
- b) An ability to treat supplies between the hospice and trading subsidiaries as internal (ie VAT free) recharges for VAT purposes, to prevent the charging of irrecoverable VAT between the two entities.

7 VAT recovery

When VAT is incurred on a supplier's invoice, in order to determine whether the VAT can be recovered, the charity is required to consider whether the expense can be solely attributed to either a taxable, exempt or non-business activity. If it can, then the VAT will be either wholly recoverable (if relating to a taxable activity), wholly irrecoverable (if relating to a non-business activity) or subject to the partial exemption de minimis regulations (if relating to an exempt activity).

Any VAT incurred on an expense that does not solely relate to a particular activity can be partially recovered. This is explained at point 7.3 below.

7.1 Exempt incomes and activities

There are specific reliefs which exempt certain business incomes and activities from VAT. For example, certain health and welfare activities, educational activities, or the staging of a one-off fundraising event are specifically exempt from VAT.

VAT incurred on costs relating to an exempt activity can only be recovered when it falls below two prescribed de minimis limits, as follows:

- a) The exempt input tax is no more than £7,500 per annum; and
- b) The exempt input tax is less than 50% of the total business input tax incurred in the year.



7.2 Non-business incomes and activities

Although it is a basic principle of VAT accounting that VAT incurred on costs attributable to non-business incomes and activities cannot be recovered, a distinction needs to be drawn between raising restricted and unrestricted incomes.

Following a ruling by the High Court in 2005, in a case brought by The Church of England Children's Society, VAT incurred on the costs relating to the generation of unrestricted income can be partially recovered, to the extent it is used for taxable business activities. The recoverable element will usually be determined using the overhead recovery calculations (see point 7.3).

7.3 General overhead costs

A sizeable proportion of expenses are general overheads of the charity, which cannot be said to solely relate to one specific activity. The VAT on these costs is therefore termed as being non-attributable or 'POT' costs. This will include central overheads such as building costs, IT, HR, finance, etc.

In order to determine how much of this non-attributable POT can be recovered, the charity is required to undertake two separate and distinct calculations so that this POT can be apportioned between the taxable, exempt and non-business activities and thus determine how much VAT can be recovered. These calculations are as follows:

- a) Business/non-business apportionment

The first stage is to determine how much of this VAT relates to the non-business activities of the charity. Once this has been established, it is known that this non-

business element of the POT is wholly irrecoverable.

b) Partial exemption calculation

The second stage is to apportion the remaining business input tax between the taxable and exempt activities of the charity. All of the taxable input tax will be fully recoverable. The exempt input tax (including the directly attributable exempt input tax) will be recoverable only if it falls below the partial exemption de minimis limits (see point 7.1).

There are no statutory methods by which these calculations have to be made. The only two requirements are that they are 'fair and reasonable' and, in respect of the partial exemption calculation, that it is approved in advance by HMRC. This being so, it is a fairly subjective exercise and an opportunity to negotiate a favourable arrangement. The most common methods are either based on income, expenditure, salary exclusive expenditure, input tax and staff numbers. It is also possible to use a different method for each calculation.

By way of example the business/non-business apportionment and the partial exemption calculations can be illustrated as follows:

Figure 8

Income	£
Taxable	60,000
Exempt	40,000
Non-business	100,000
Total income	200,000

a) Business/non-business apportionment:

$$\frac{\text{Business income (taxable and exempt) } 100,000}{\text{Business and non-business income } 200,000} \times 100 = 50\%$$

This being so, 50% of the POT VAT is deemed to relate to business activities and is carried forward to the partial exemption calculation. The remaining 50% is deemed to relate to non-business activities and is wholly irrecoverable.

b) Partial exemption calculation

$$\frac{\text{Taxable income } 60,000}{\text{Taxable and exempt income } 100,000} \times 100 = 60\%$$

This being so, 60% of the remaining business POT VAT is deemed to relate to the taxable activities and is therefore fully recoverable. The remaining 40% is deemed to relate to the exempt activities. This can only be recovered if the total value of exempt input tax (ie POT VAT exempt element plus directly attributable exempt VAT) falls below the partial exemption de minimis limits (see point 7.1).

7.4 VAT on rents

Where a hospice incurs VAT on a rent it pays to a landlord, care should be taken that the VAT has been correctly charged.

The letting of commercial land and property is exempt from VAT. However, the landlord has the ability to waive this exemption so he can charge VAT to his tenant. This is commonly termed 'opting to tax'.

The option to tax is disappplied on any land or property which is used solely for non-business purposes by a charity. In order to obtain this relief the charity is required to give a certificate to the landlord confirming its status as a charity and that the relevant land or buildings are to be used for non-business purposes.

The relief can also apply to any identifiable part of a building (or land) which is used for non-business purposes so VAT is only incurred on part of the rent.

7.5 Electricity and gas charges

Charges made by energy companies for electricity, gas, fuel oil etc, can be charged at the 5% VAT rate when it relates to either:

- a) Domestic use; or
- b) Charity 'non-business' use.

The relief for charity non-business use can be applied where the non-business use of the relevant building is at least 60% of the total usage. Where it is more than this, an apportionment can be made so that VAT is charged at 5% on the non-business element.

Where usage is sufficiently low to be below certain de minimis limits, irrespective of non-business use, the supply can be deemed to be 'domestic' and the 5% VAT rate applied. The de minimis limits are as follows:

Electricity	1,000 kilowatt hours per month
Piped gas	150 therms per month or 4,397 kilowatt hours per month
Fuel oil, gas oil or kerosene	2,300 litres per supply

7.6 Solar panels etc

The purchase and installation of energy saving materials by a charity will also be subject to VAT at the reduced rate of 5% when the supply relates to either:

- Domestic use; or
- A charity's non-business use



The reduced rate of VAT applies to installations of:

- Controls for central heating and hot water systems
- Draught stripping
- Insulation
- Solar panels
- Wind turbines
- Water turbines
- Ground source heat pumps
- Air source heat pumps
- Micro combined heat and power units
- Wood fuelled boilers

Please note that the reduced rate of VAT on the supply of energy saving materials to charities is being withdrawn from August 2013.

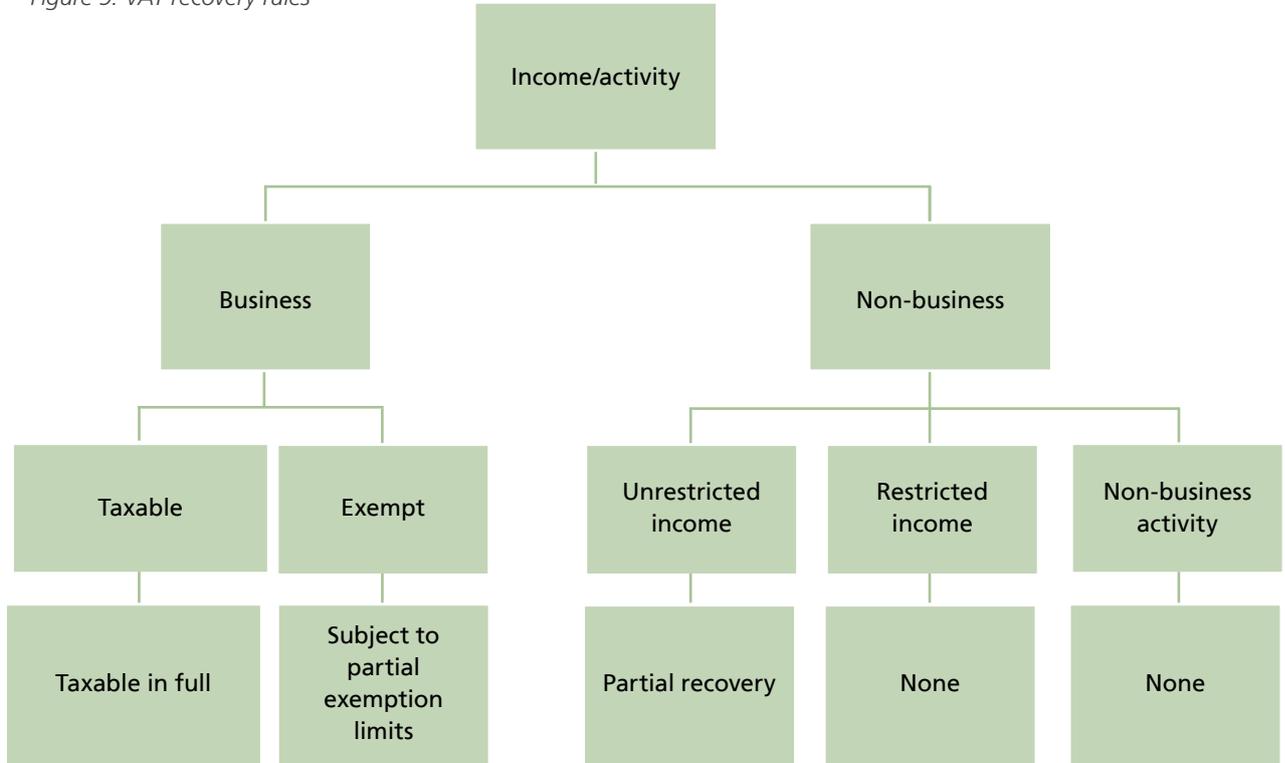
7.7 Summary

As can be seen, the rules for determining how much VAT a charity can recover are relatively straightforward. As set out below, the recovery of VAT incurred on costs and expenses is determined by the activity to which it relates.

Where, however, an activity generates incomes with different VAT liabilities, it is important that this is identified in order to establish the correct VAT recovery position. For example, where an exempt one-off fundraising event generates only exempt income from the sale of admission tickets, the VAT incurred on related costs is likely to be wholly recoverable. However, if the same event also generates zero rate income from the sale of donated goods at an auction, then VAT on related costs is partially recoverable as it cannot be wholly attributed to only the exempt income.

It is therefore vitally important that the VAT liability of every income and activity of the charity is known so that the correct VAT recovery position can be established.

Figure 9: VAT recovery rules



8 Trading companies

Many charities make use of a wholly-owned subsidiary company in which to undertake various trading activities.

The principal benefit of using a trading subsidiary company is to avoid the risk of activity within the hospice being deemed as taxable for direct tax purposes as it is not considered to be a primary purpose activity (see section 3). Additionally, certain trading activity may not fall within the hospice's charitable remit and therefore may not be undertaken by it.

Care does need to be taken to ensure that the use of a trading company does not give rise to VAT disadvantages that would not otherwise exist (ie on suppliers of staff and other cross charges).

Key issues to consider include:

8.1 Supplies of staff

It is usual for the hospice to employ all staff. This being so, where staff employed by the charity are engaged in activities undertaken by the subsidiary trading company, there is a supply of services or staff by the charity. This supply by the charity is liable to VAT at the standard rate (20%).

Where there is a group VAT registration between the charity and the subsidiary, no issue arises as there is no supply for VAT purposes.

Where there is no group VAT registration, this potential problem can be overcome by ensuring the relevant staff are jointly employed by both the charity and its subsidiary. Where joint employment contracts are in place, payment by the subsidiary to the charity is outside the scope of VAT.

8.2 VAT recovery

As it is usual for the subsidiary company to undertake the majority of taxable trading activities, the removal of this taxable activity from the hospice can materially reduce the hospice's ability to recover VAT incurred on costs. This is particularly true for central overhead costs, which will invariably be incurred directly by the hospice itself.

This problem can be overcome by the use of a VAT group registration (see section 6.5). The reason for this is that it should be possible for VAT recovery agreements (business/non-business apportionment and partial exemption calculation) to be negotiated with HMRC to combine the income and activities of the charity and the subsidiary.

Where there is a VAT exempt lottery or raffle, or another VAT-exempt activity is undertaken in the subsidiary, it is likely not to be able to fully recover all the VAT it incurs on costs and expenses (see section 7). Where this is the case, the use of a VAT group registration will also prevent partially irrecoverable VAT being charged on supplies made by the hospice to the subsidiary.



9 VAT-free purchases

9.1 Medical equipment, drugs and consumables

One of the most valuable VAT reliefs available to hospices is the ability to buy a large proportion of medical equipment, drugs and consumable items such as medicines, bandages and plasters free from a VAT charge (see figure 10).

The regulations and HMRC guidance surrounding these reliefs is very detailed. Additionally, many manufacturers and suppliers have contested the VAT liability of their products in an attempt to have them established as being VAT-free. This has resulted in a vast catalogue of detailed commentary available to hospices where there is doubt over whether VAT is required to be paid to suppliers of specific items.

9.2 Advertising

Advertisements covered by the relief

This zero-rating relief covers all types of advertisements on any subject, including staff recruitment and event promotion. The charity name or logo does not need to be included for relief to be allowed. However, charities are expected to only place advertisements which comply with their charitable objectives. This relief does not override charity law or the need to comply with the British Codes of Advertising, or any other relevant regulations.

Scope of the advertising relief

Any charity can benefit provided the supply of the advertisement is made to it by a third party, including its separately VAT registered trading subsidiary. However, the relief is not available for supplies to trading companies.

Types of media covered by the advertising relief

The relief covers any medium which communicates with the public. This includes all the conventional advertising media such as television, cinema, billboards, the sides of vehicles, newspapers and other printed publications. The important factor is whether the advertisement is placed on someone else's time or space, eg a third party television advertisement, a newspaper advert or advertising on the radio. If it is not, there will be no scope for the zero-rating relief to apply.

If space is sold to the charity for advertising on other items, such as beer mats, calendars, or the reverse of till rolls, this will also be covered by the zero rate.

Figure 10: As a broad overview, the following medical items can generally be supplied to a hospice VAT-free:

- Bandages
- Beds (specialised)
- Bedpans
- Drip poles
- First aid kits
- Patient trolleys
- Orthopaedic pillows
- Resuscitation equipment
- Scalpels
- Forceps
- Surgical gloves
- Hypodermic needles
- ID bracelets for patients
- Kidney bowls
- Mattresses (specifically designed)
- Medicine measures
- Sterilising equipment
- Stethoscopes
- Surgical gloves, gowns and masks
- Suture needles
- Swabs
- Clinical thermometers
- Tongue depressors
- Wound dressings
- Refrigeration equipment

However, the sale of the items themselves will not be VAT free unless the item qualifies for other relief in its own right, for example as books or children's clothing.

Internet advertising

Information, whether or not in the form of advertising, placed in, on or through a charity's own website, does not qualify for zero-rating. This is because it is not a supply of someone else's time or space, whether or not the website

is owned, rented or loaned to the charity. Since the information on the website is excluded from the relief, it follows that the associated design costs are also excluded.

However, an advertisement placed on a third party's website does qualify for zero-rating.

Exclusions from the relief

The following are excluded from the advertising relief as they are not considered to be a supply of someone else's advertising time or space, or are a form of general marketing and promotion:

- Direct mail and telesales;
- Anything on a charity's own website;
- Advertisements where there is no supply of time or space to the charity, for example, an advertisement on a charity's own greeting cards;
- Exhibition stands and space;
- Services of distribution; and
- Commemorative items, whether or not they bear the charity's logo, for example pens and adult size clothing.



Figure 11: The zero rate relief applies to the supply to a charity of:

1. A right to make known an advertisement by means of any medium of communication with the public;
2. Making known an advertisement by means of such a medium;
3. Services of design or production of such an advertisement; and
4. Goods closely related to a supply within (3) above (see below for examples).

Design and production of advertisements

Provided it is intended that the advertisement will be placed in purchased or donated advertising time or space, the supply of design or production of the advertisement will qualify for relief. This includes the design of a poster or the filming or recording of an advertisement to be broadcast.

Goods linked to the design or production of advertisements

Goods closely related to the design and production will qualify for relief. For example:

- A finished article like a film or recorded cassette;
- An element to be incorporated in the advertisement such as a photograph, picture or a sound track; or
- All alternative versions of an advertisement produced, to see which works best, even if it is the intention that only one version will be used.

Inserts

HMRC accepts that the supply of an insert into a glossy or similar publication is zero rated as an advertisement, provided that the space is paid for.

The use of advertising agencies

Where a charity uses an advertising agency rather than dealing with the suppliers of the advertising space or time, the VAT liability depends on whether the agency is acting as a principal or an agent.

Principal

Where an advertising agency is the principal, the agency's supplies of qualifying time or space and associated production costs to the charity will be zero-rated. Supplies to the agency are subject to the standard rate.

Agent

Where the advertising agency acts merely as an agent, the agency fees are subject to VAT at the standard rate. The supply of advertising time and space to the charity remains zero-rated.

Charities that create their own advertisements

These adverts do not qualify for the relief. This is because it is not a supply to the charity. Therefore, it is not possible for charities to purchase the equipment and raw materials they use in creating these advertisements VAT free.

Claiming the relief

When a charity claims the zero rate reliefs which are not generally available to all customers, suppliers must be sure that all the relevant conditions for relief are met. It is recommended that a hospice gives its supplier a declaration that the specific conditions for the claimed relief are fulfilled (see appendix A).

An example of where a declaration may not be necessary is when a charity requests repeat orders, has made a declaration for the first one and the information contained in that declaration has not changed.

Retrospective adjustments

Where a supplier has incorrectly charged VAT on an advertisement, or related supply which qualifies for the zero rate relief, you can ask for a VAT-only credit note up to four years after the date of the original supply.

Summary

The advertising relief is an extremely valuable VAT relief available to charities. Ensure that VAT is not charged on advertisements and related goods and services which qualify and if it is request a credit note from your supplier.

9.3 Printed matter

What printed matter is zero rate?

The supply of a complete item of printed matter produced on paper, card and similar materials is zero-rated for

VAT purposes. This includes books, booklets, brochures, pamphlets, leaflets, magazines, journals and other similar items.

Items that qualify for the zero rate relief are shown below:

Figure 12: Zero rate printed matter

- Books and booklets
- Brochures and pamphlets
- Leaflets
- Newspapers
- Journals and periodicals
- Children's picture books and printing books
- Music (printed, duplicated or manuscript)
- Maps, charts and topographical plans
- Covers, cases and other articles supplied with any of the above items and not separately accounted for

Items which are essentially stationery items are not zero-rated. For example, a blank diary is for completion and thus standard rate, whereas a completed diary of historic or literary interest is complete and qualifies for the zero rate. Similarly, a blank sponsorship form is for completion and does not qualify for the zero rate relief.

Looking at the specific items that do qualify for the relief, it is important that they meet the following tests:

Books and booklets

A book or booklet normally consists of the text or illustrations, bound in a cover stiffer than its pages. It can be photocopied, typed or handwritten and includes items published in braille and shorthand.

Brochures and pamphlets

In order to qualify as a zero rate item, HMRC usually requires a brochure to consist of several sheets of reading matter fastened or folded together containing advertising material in the form of text or illustrations.

A pamphlet is similar but usually comprises material of a political, social or intellectual nature.

A single sheet or wallet-type brochure, which is designed with a flap, may be zero rate provided it conveys information, contains a substantial amount of text, is not primarily designed to hold other items and is supplied complete.

Leaflets

A leaflet is zero-rated if it meets the following tests:

- It should convey information by means of text;
- It is printed on limp paper (not laminated paper);
- It is designed to be held in the hand for reading rather than for hanging up or general display;
- It should consist of a single sheet of paper not greater than A4 size. Larger items up to A2 size can be zero-rated provided they are printed on both sides and are folded down to A4 or smaller;
- It should be complete in itself and not part of a larger work; and
- It should be supplied in at least 50 copies to permit general distribution.

Areas for completion and/or return

An item which would normally qualify for the relief may not be zero-rated if it is primarily intended for completion and/or detachment and return. A typical example of this would be a membership joining leaflet with an area for completion and return.

The rule of thumb is that where an item has an area over 25% for completion or return it will not be zero-rated. This is not a statutory limit and it may be possible to get agreement from HMRC where the 25% test is breached.

A publication which is designed to be returned whole after completion is always standard-rated.

Artworks and design costs

Any ancillary services supplied in relation to a zero rate item can also be zero-rated, provided they are supplied by the supplier of the item itself.

Unlike the advertising relief, a sub-contractor can only zero rate his supply if he produces zero rate goods himself.



This being so, in order to ensure zero rating for all services received in relation to a printed item it is necessary for sub-contracted or separate suppliers of ancillary services to make their supply to the provider of the zero rate item.

Electronic supplies

The supply of text in PDF and other electronic transmissions such as audio or video cassette are standard-rated, even where the same document is zero-rated as printed matter.

An example of this is where a membership charity affords members a magazine in printed format; this is a zero rate benefit. Where, however, the same magazine is sent electronically, this is a standard rate benefit.

Posters

The supply of a poster intended for public display to a charity is normally standard-rated.

However, where the poster is intended to be used as an advertisement bought on someone else's medium (eg a billboard) its supply can be zero-rated as an advertisement. Unlike the restriction on printed matter, any ancillary services such as design and artwork for a poster can also be zero-rated where it is intended for use as an advertisement.

Photocopies

Photocopies of zero rate items are always standard-rated, unless the copies can themselves be properly described as a zero rate item, eg leaflet, pamphlet etc.

Mail packs and fundraising material

It is possible to zero rate the majority of printed mail pack and fundraising items: see section 9.4 for more details.

Event programmes

A programme sold separately from an admission or ticket price is zero-rated. Where, however, a programme is included in the value of an admission or ticket price it cannot be separately identified and treated as being zero rate (even though it has been supplied zero rate to the charity).

Membership subscriptions

Where a charity supplies a magazine, newsletter, journal or similar publication as a benefit of membership to its supporters, it is possible to treat all or part of the subscription received as being zero-rated depending upon the other benefits received by the member.

Summary

The zero rate relief for many printed items is a widely used and valuable relief for charities.

The provision of zero rate magazines to supporters (ie via a subscription or membership scheme) is commonly used to enable many charities to increase their 'taxable' income and thus, in turn, increase their ability to recover VAT on costs.

9.4 Mail packs

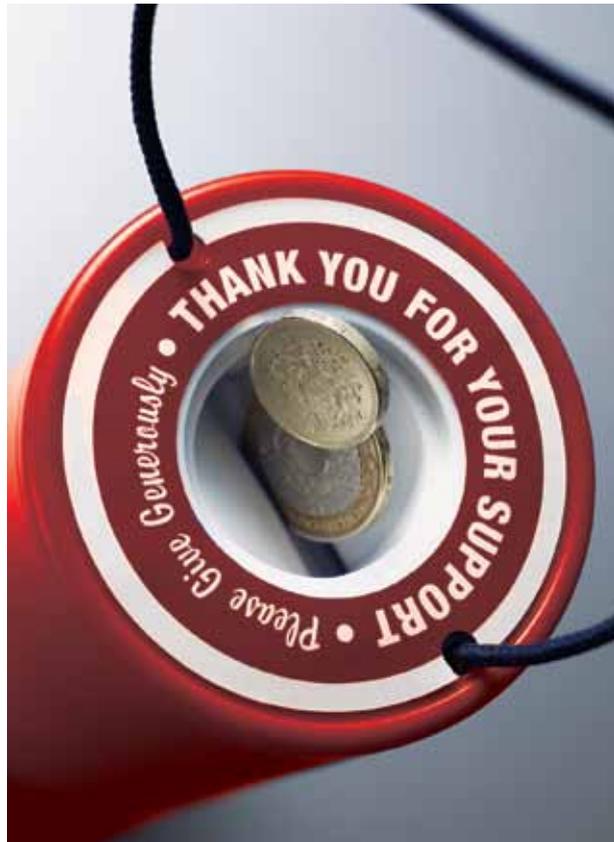
Printed items within a mail pack, which when considered in isolation are themselves zero rate, remain zero rate when supplied in a package of various items. For example, this could apply to leaflets, brochures, pamphlets and other printed items commonly used in mail packs.

A common item is an unnamed letter, ie Dear Householder, which, as it is not individually addressed, can qualify as a leaflet.

Pre-printed fundraising stationery

In addition to the general relief for printed matter set out above, there is a charity-specific relief aimed at mail packs. This enables the following items to be zero rate:

"Pre-printed letters, the primary purpose of which is to appeal for money for the charity, envelopes used in conjunction with such letters for forwarding donations, provided that they are overprinted with an appeal request related to that contained in the letter, and outer envelopes used in conjunction with such letters, again if they are similarly overprinted."



Package test for mail packs

Where a charity buys a package of printed matter, some of which is standard rate and some zero rate, the supplier can apportion his charge between the standard rate and zero rate elements so that VAT is only charged on the standard rate items.

Alternatively, by concession, the supplier can apply what is known as 'the package test'. This is beneficial where the package contains more zero rate items than standard rate items, as in this instance the whole package can be zero rate (clearly this is not beneficial where there are more standard rate items).

Where there are equal numbers of zero rate and standard rate items in the mail pack, the VAT liability of the pack is determined by the cost of the items. If the zero-rated elements of the pack cost more, the whole pack is zero-rated. Again, if the standard rate items cost more the package test should not be adopted and an apportionment applied.

Importantly, the outer envelope in which the pack is enclosed is not taken into account when counting the number of standard rate and zero rate items. A reply-paid envelope does count as a standard rate item unless it is zero rate under the pre-printed fundraising stationery concession outlined above.

Non-printed items

Importantly, if any item in the mail pack is not printed on paper or card, such as a pen, or badge, then strictly speaking the package test cannot be applied to the printed element of the pack.

Consolidation of services

Many suppliers of mail packs offer to consolidate ancillary services such as design or purchase of mailing lists so that these services can also be zero rate.

Providing the consolidated services are ancillary to the principal item being supplied, ie the zero rate mail pack, then it may be possible to use this technique to extend the scope of the zero rate in this way.

New rules with effect from 19 July 2011 have uprooted this valuable relief to the sector. HMRC has yet to provide firm advice, but services which do appear as ancillary, such as mailing lists and fulfilment services, will now be subject to VAT.



Contracts with suppliers

It is important to ensure, wherever possible, that the incentive to ensure the correct VAT liability of the mail pack or services provided lies with the supplier.

It is common practice for contracts to stipulate that it is the supplier's responsibility to design a mail pack which is wholly zero-rated. Should HMRC later deem the pack to be wholly or partially liable to VAT, then the cost is the responsibility of the supplier.

We would recommend a clause in contracts with mail pack providers to stipulate it is the supplier's responsibility at the time he raises his invoice to establish the correct VAT position and any error is his financial cost.

Recovery of VAT incurred

If VAT is incurred on part or the whole of a mail pack or related services its recovery will be determined under the usual rules.

If the pack relates to appealing for unrestricted donations then any VAT incurred can be partially recovered using the charity's normal partial recovery rate.

If the pack relates to appealing for restricted donations then any VAT incurred will be wholly irrecoverable (unless in the unlikely event that the funds are restricted for use on a business, taxable activity).

If the pack relates to a taxable business activity (eg a zero rate/standard rate membership subscription), then any VAT incurred can be recovered in full.

9.5 Postage charges

With effect from 2 April 2012, The Royal Mail has started to charge VAT at the standard rate of 20% on a number of additional services, including direct bulk mail services. The impact of this change in treatment on charities is that the VAT they will incur is unlikely to be fully recoverable.

VAT incurred on mail shots relating to raising unrestricted income will be partially recoverable, but VAT incurred on raising restricted income or raffle-type lottery income is likely to be wholly irrecoverable.

Following sector consultation with HMRC, the following arrangements seek to mitigate the impact of this additional VAT cost:

Under the arrangement, charities will use commercial 'downstream access' (DSA) providers such as TNT, UK Mail, City Link, Secured Mail, etc. Charities will contract with these DSA providers for them to collect and sort bulk mail, with only the 'final mile' delivery being actioned by Royal Mail. As part of the supply, the final mile element of the postage (which DSA providers are required to purchase from the Royal Mail, in order to be able to make their supply to charities) will be treated as a disbursement.

The final mile element of the overall supply usually works out to be more than 88% of the total price of the supply. This arrangement is made possible as a result of the fact that DSA providers enjoy an existing agreement with the Royal Mail, whereby they are able to treat their supply of the final mile delivery services to their customers as exempt from VAT and therefore they are not required to charge VAT on the recharge of that supply to the charities. However, as the recharge is to be treated as a disbursement, the DSA providers must ensure that the VAT disbursement rules are satisfied.

9.6 Collecting tins, lapel badges, etc

Certain goods which are supplied to a charity for the purposes of collecting monetary donations can be zero-rated. The relief is not statutory but rather a concession and relates to collection boxes and receptacles, lapel stickers and similar tokens.



Collection boxes and receptacles

Only particular types of collection boxes and receptacles qualify for zero-rating. In order to do so, all of the following conditions must be met:

- The collection boxes must be secure, ie capable of being sealed by, for example, tape or lock;
- They must be charity collection boxes for a named charity; and
- They must bear the name of the charity, for example by permanent printing, embossing or having raised letters, or allow for the charity name to be added later.

Typical examples include:

- Pre-printed card collecting boxes;
- Moulded plastic collecting boxes; and
- Models in any material, including hollow plaster, wood, base metal or glass.

These boxes could be handheld, floor standing, wall mounted or for placing on a tabletop or shop counter.

Receptacles made with a simple balancing mechanism by which the money moves from one level to another or the weight of a coin causes it to roll helter-skelter fashion into the collecting area would be included in the relief.

The relief does not apply to those boxes of a higher value (ie those made of some sort of precious metal) and would include boxes with elaborate mechanisms such as gaming or quiz machines, coin slot machines or some other

form of mechanical entertainment. However, if a simple collection box was to be attached to these or other forms of receptacles which collect money for another purpose such as wishing wells and fonts etc, then these particular boxes would also qualify.

Buckets

General purpose buckets which can be bought from hardware stores are not covered by the concession, irrespective of their intended use.

However, the following do qualify for relief:

- Specially designed tamper-proof bucket lids with tamper evident stickers making them suitable for a charity donation;
- Bucket-shaped receptacles which cannot be used for anything except collecting donations of money; and
- Bucket packs for assembly, consisting of bucket, money collecting top and tamper evident seals and labels.

Lapel stickers and similar tokens

Another zero-rating relief is for lapel stickers, emblems and badges which are to be given away for free as an acknowledgement of a monetary donation.

In order to qualify for zero-rating, the relief is restricted to small items which are designed to be worn on clothing and which are of a kind that are traditionally attached to the lapel. Included in these items are paper stickers, ribbons, artificial flowers (ie poppies worn for Remembrance Sunday) and metal pins and badges. Other items not designed to be worn on the lapel, such as wristbands and dog tags, do not qualify.

Examples of qualifying items that are considered to be of no real value and are of low cost to the charity, would be emblems or badges given in return for any non-specified donation, or a suggested donation of up to £1. In practice this would mean that the cost to the charity would be considerably less than £1 per item. Items above this value would therefore not qualify for the relief.

Although the zero-rating applies if a charity suggests a donation of £1, if lapel emblems or attachments are offered for sale for a fixed price, (even if the cost was £1 or less) they would not qualify for relief as these items would not be given away freely.

If a charity buys identifiable constituent parts which are then assembled into badges in-house, these are covered by the relief.

The relief does not cover containers which are used to hold the lapel badges. If the container is considered to be merely normal packaging for the lapel attachments, then these and their container would be seen as a single zero-rated supply of lapel attachments. The more considerable containers, such as those with a strap to hang around the neck, are items in their own right and would not be included in the relief. The supply of an empty container is standard-rated.

Where a cardboard collecting vessel is incorporated into a cardboard tray that holds the lapel attachments, and is supplied as a single item (often as a flat pack), there is a single supply for VAT purposes and normal VAT rules would apply. Providing the main purpose of the goods is to act as a collecting receptacle, then the whole supply can be zero-rated.

For both of these reliefs, a certificate must be produced to the supplier as evidence for the supply to the charity to be zero-rated. A sample certificate is included at appendix A.

VAT recovery

Where VAT is incurred on the purchase of such items this can normally be recovered at the charity's normal POT rate, providing the donations sought are unrestricted.

Where the donations are restricted no VAT recovery is usually possible.

Where VAT is incurred on the purchase of badges because they are intended for sale rather than be given away in recognition of a gift, then on the grounds the income from the sale of the item is standard rate, the VAT incurred on purchase can be fully recovered.

10 Dealings with corporates

Perhaps one of the most frequent questions our Charity Team is asked is whether or not a payment from a corporate sponsor is liable to VAT and to direct tax?

What is corporate sponsorship?

Sponsorship is a generic term which is widely used in the voluntary sector and can mean different things to different people.

When used in the context of dealing with a corporate body the question is whether or not the charity or its trading company is making a supply of goods or services, eg advertising or the use of a logo in return for the payment it receives. Or, put another way, are the funds provided by the corporate a donation for which nothing is required in return? Or is this payment, either in full or part, for the supply of goods and/or services?

Recognition or advertising?

In order to answer this question, the issue of the tax position can frequently depend upon whether or not the exposure given to the corporate is merely recognition of its support of the charity or advertising.

This can sometimes be a difficult distinction to make. As a general rule, however, wherever the use of the corporate's logo is made, it is likely that HMRC will consider there to be a supply of advertising and seek VAT on the payment made and seek tax on the profit generated.

Conversely, if the corporate's name is merely listed in an annual report or in a programme with other supporters of the charity, then this can be treated as merely providing recognition and not advertising, so neither VAT nor tax is due on monies received.

Contractual obligation

In order for there to be a supply of goods or services by the charity or its trading company, there has to be an agreement or understanding between the parties that the benefit will be provided in return for the sponsorship payment.

This would normally be stated in a contract or memorandum of understanding (MOU), or be included within correspondence outlining the arrangements.

If there is no contractual obligation for a charity to provide goods or services to the sponsor but it chooses to do so of its own free will, then strictly speaking there is no supply for VAT purposes and the sponsorship payment can be treated as an unconnected donation. HMRC will be sceptical if such a situation arises and we would strongly recommend that correspondence with the sponsor is retained stating that there was no obligation for the charity to provide goods or services as a condition of the sponsorship payment being made.

Contracts/agreements

It is important that where a contract/agreement/MOU is in place, the VAT treatment of the payment made reflects the responsibilities and obligations required of each party.

This is particularly important where only an element of the sponsorship monies is to be treated as a payment for a supply by the charity, with the remainder being treated as a donation. The danger is that where no distinction is made between the payment and donational elements, HMRC will seek to treat the whole of the sponsorship monies as being subject to VAT and to direct tax.

It is therefore essential that where such a split is agreed with the corporate sponsor (ie part donation, part payment for advertising) there are two agreements: a contract for the payment for services/goods which invariably will be with the trading company for direct tax purposes, and an agreement with the charity for the donational element. The value of each element must be clearly quantified and set out in the agreements.

Similarly, the arrangements can be set out in a tripartite agreement between the corporate entity, charity and trading company.

VAT position of the corporate sponsor

Where the corporate sponsor's trading activity is exempt from VAT (eg finance, insurance, property sectors) it is likely that it will be unable to recover, either wholly or partly, VAT charged to it by the charity.

Figure 13: Contractual obligation

Many charities receive money, goods or services from sponsors:

- If the charity is obliged to provide the sponsor with a significant benefit in return for the sponsorship (eg free tickets, free advertising, space in a charity event programme), this is a business activity and is taxable at the standard rate.
- If the sponsor receives no significant benefit in return for its contribution, the charity may be able to treat the income as non-business. HMRC accepts that giving a flag or sticker to a donor, or naming a donor in a list of supporters, is insignificant.

HMRC advises that where a charity is obliged to provide any of the following benefits in return for the sponsorship monies, they will consider the sponsorship to be liable to VAT:

- Naming an event after the sponsor;
- Displaying the sponsor's company logo or trading name;
- Participating in the sponsor's promotional or advertising activities;
- Allowing the sponsor to use the charity's name or logo;
- Giving free or reduced tickets to an event;
- Allowing access to special events such as premieres or gala evenings;
- Providing entertainment or hospitality facilities; or
- Giving the sponsor exclusive or priority booking rights.

This list is not exhaustive.

This being so, it is important to ensure that agreements reached for sponsorship monies are exclusive of VAT. For example, where a finance company agrees to pay £10 to the charity for every new customer it achieves from the campaign, it should be stated that the £10 is exclusive of VAT. If this is not done, the VAT cost will fall on the charity, which will only receive £8.33 per new customer, with £1.66 being paid in VAT as output tax by the charity to HMRC.

It may be possible to mitigate such a loss by agreeing with the corporate to treat an element of each payment as a donation. However, any such arrangement must be agreed between the parties and be fully documented in the contract and agreements between the hospice, its trading company, and the corporate.

The tax position of the corporate sponsor

Generally a sponsor will obtain a tax deduction against taxable profits for the costs of advertising, sponsorship etc and for donations to charities.

Royalties and licence fees

Income from royalties and licence fees for the use of the charity's name and logo are subject to VAT at the standard rate unless the payment is made from an entity which belongs outside the UK.

A frequently asked question is; what is the market rate value for the provision of the use of our logo under a licence agreement? Providing the licensee is an unconnected third party, the value of the licence is not a matter for HMRC. It is common for a charity to license its logo use at different rates to reflect different commercial arrangements and benefits arising.

One-off fundraising events

Sponsorship received in direct relation to an exempt one-off fundraising event is also exempt from VAT.

However, in order for the exemption to apply, the sponsorship payment must be wholly and directly connected with an event and not also relate to more general sponsorship of the charity.

Where this VAT exemption applies to the income of the charity, the income is also exempt from direct tax.



Cause-related marketing

The placing of a charity name on a corporate's product in return for a payment is a supply for VAT purposes and subject to VAT at the standard rate. This income is also subject to direct tax. This treatment applies even where the corporate advises its customer that it will make a donation of a specific amount to the charity for each item sold.

In these circumstances, it is common for the payment to be treated as part consideration for the use of the charity's logo and part donation. Clearly, the contracts between the parties need to correctly reflect the position agreed. Where, however, the corporate is able to fully recover VAT charged to it by the charity there appears little incentive to split the contract in this way.

Charitable foundations

Where a corporate provides funding through its charitable foundation, HMRC is willing to accept that there is no supply of advertising to the corporate entity, even where the logo of the foundation is very similar to that of the corporate. Where, however, there is any doubt on this issue, we recommend an approach is made to HMRC.

Similarly, where a grant-making trust provides funds and the recognition given by the charity includes the use of the funder's logo, it is accepted that there is no supply taking place by the charity and no VAT need be declared.

Such receipts are also generally not liable to direct tax.

11 Fundraising activities

11.1 Fundraising events

One of the most valuable, and widely used, VAT reliefs is the exemption from VAT for income generated by a one-off fundraising event. Although widely used, there remains doubt over certain elements of the relief.

What is a fundraising event?

For the purposes of the VAT exemption relief, a one-off fundraising event is an event which is organised and promoted primarily to raise money for charity.

It is therefore key that people attending or participating in the event are wholly aware that it is a fundraising event. With this in mind, tickets, leaflets, posters and other promotional material must make it clear that the event is being staged to raise funds for charity.

Events, such as a social or awareness occasion, which may or may not make a profit, do not qualify for the relief. However, an event which is clearly a fundraising event, but makes a loss merely through lack of success, would still qualify.

The relief is intended solely to cover specific fundraising events, so activities which are regular or continuous, such as a charity shop, do not qualify.

Figure 14 lists examples of events HMRC agrees qualify for the relief.



Figure 14: Qualifying fundraising events

- A ball, dinner dance, disco or barn dance
- A performance, eg concert, stage production and any other event which has a paying audience, eg a film
- A fete, fair or festival
- A horticultural show
- An exhibition – such as art, history or science
- A bazaar, jumble sale, car boot sale
- Sporting participation, eg sponsored walk or swim
- A sporting performance
- A game of skill, a contest, or a quiz
- Participation in an endurance event
- A fireworks display

An event which is repeated on successive days, such as a pop concert, is seen as one event, each day (see below for maximum number of events permitted). A single event which takes place for more than one day, such as a show, or golf tournament, is seen as one event.

HMRC accepts that an event can be held over the internet.

A limit on the number of local events

The relief is restricted to 15 events of the same kind at any one location per financial year. If more than 15 are held, then none of the events qualify for the VAT exemption.

For this purpose, one location means “held in the same place”. Similar events held in different locations still qualify. For example, 30 sponsored walks held in different locations around the country would all qualify for the VAT exemption.

The 15 events limit on local events does not apply where the gross weekly takings are no more than £1,000. If this limit is breached then none of the events in that week would qualify.

How does the VAT relief work?

The relief enables all income generated from the supply of goods or services at, or in connection with, a fundraising event to be exempt from VAT. This will include ticket sales, admission charges, advertising space in programmes/brochures (except to other charities, which is zero rate), merchandise, non-donated auctioned goods, auctioned services, bar and catering supplies and sponsorship.

Zero rate supplies at an event remain zero rate. This will include sales of programmes/brochures, sales of donated goods at auction or otherwise, children's clothing (including T-shirts and baseball caps) and advertising sold to other charities.

Donations received at an event remain outside the scope of VAT altogether.

By way of example, the following diagram shows an income account for a typical event to show the VAT treatment of common income types.

Figure 15: VAT liability of common income types generated at one-off fundraising events

	£	VAT liability
Ticket sales	1,500	Exempt
Sponsorship from a corporate	750	Exempt
Programme sales	300	Zero rate
Auction income		
- Sale of donated goods	3,000	Zero rate
- Sale of donated services	2,500	Exempt
- Sale of bought-in goods	1,000	Exempt
Merchandise sales on night	800	Exempt
Donations collected on the night	1,000	Non-business
Bar sales commission	700	Exempt
Sale of commemorative DVDs post-event	450	Taxable
Total	12,000	

It is important to note that the application of the VAT exemption is not optional. If an event qualifies for the relief then the exemption is applied mandatorily.

Who can apply the relief?

The fundraising event exemption is unusual as it is one of the few VAT reliefs that is not restricted to the charity itself.

A hospice's trading subsidiary company can also apply the relief to fundraising events it stages on behalf of the charity, providing it:

- Is wholly owned by a charity; and
- Donates all profits made, from whatever source, to a charity.

However, care needs to be taken: though an event may be organised for the benefit of a charity, or charities, it will not qualify for the exemption unless it is organised by a charity or other qualifying body. For example, where an individual, corporate or other independent group autonomous to the charity holds an event, the exemption does not apply.

Where, however, a charity appoints an agent or promoter to organise the event on its behalf, then the exemption still applies. HMRC may wish to see the agency agreement. If the agent charges or retains any element of the event's gross receipts, this is an agency fee and subject to VAT at the standard rate.

Events organised jointly with another charity also qualify for the relief.

VAT recovery on event-related costs

The VAT exemption relief only applies to income generated by the fundraising event. It does not apply to any goods or services purchased in relation to the event.

This being so, VAT will be incurred on the majority of event-related costs. The recovery of this VAT is dependent upon the income generated by the event. If the only income generated is exempt from VAT (eg ticket sales/admissions) then the VAT incurred is either wholly recoverable or irrecoverable, depending upon whether the entity staging the event has managed to stay below the partial exemption de minimis limits (see section 7).

If, however, the event generates both exempt income and zero rate income – perhaps from the sale of a programme/brochure, or the sale of donated goods via an auction – certain amounts of VAT incurred can be partially recovered

under the charity's partial recovery agreement with HMRC (effectively as a general overhead). In such circumstances, HMRC accepts that VAT incurred on venue/marquee hire can be partially recovered, but any cost relating to admission, catering or entertainment remains wholly attributable to the exempt event.

Accordingly, it can be extremely advantageous to ensure an event produces zero rate income in order to enable a partial recovery of VAT on certain costs.

Care does need to be taken on a couple of issues:

Sponsorship

Corporate sponsorship of an event (where the sponsor receives advertising/exposure in return for his payment), is also covered by the exemption. This is only the case, however, where the sponsorship payment relates solely to a fundraising event. In all other circumstances, the sponsorship payment is liable to VAT at the standard rate in the normal way.

Unsold merchandise

Event-specific merchandise and commemorative items such as adult T-shirts, mugs, posters, etc, which are sold after the day of the event, will be liable to VAT at the standard rate (unless zero rate in their own right).



Video and audio recordings of the fundraising event sold after the event are also standard rate.

VAT summary

This exemption for one-off fundraising events is an extremely valuable VAT relief for the sector.

Where VAT recovery is anticipated to be restricted, the use of zero rate income to enable a partial VAT recovery is very straightforward, yet very effective. Similarly, if it is considered that it would be more beneficial to charge VAT on tickets/admissions to enable a full VAT recovery on event costs, the use of a subsidiary which either is not wholly owned or does not pass all of its profits to the charity, can prevent the need to apply the exemption when desired.

Finally, where supplies of zero rate items at events have not previously been identified, it may be beneficial to consider the retrospective opportunities for claiming additional VAT recovery on previous event costs.

Direct tax summary

Any income of the charity that is exempt from VAT under this exemption is also exempt from direct tax. However, a trading subsidiary will be taxable despite the VAT exemption. Other event income not covered by the VAT exemptions will be taxable unless one of the other direct tax exemptions applies.

11.2 Participatory events

Background

It is common for charities to organise sponsored events for both individuals and groups in order to generate income and raise funds. This method of raising funds, which participants often enjoy and undertake with great fervour, is attractive to charities as it serves the dual purpose of raising income whilst increasing the charity's brand awareness.

The events are often wide-ranging and can include walks, runs, swimming, treks and other sporting activities. Where a hospice is organising and promoting the event, it may be able to take advantage of the fundraising exemption.

There are many commercially organised events, however, where an individual or a team partake in order to raise money for a charity, that does not qualify as an exempt fundraising event.

VAT liability of participatory events - general rules

It is common for charities to pay for places within a commercially organised event such as the London Marathon and subsequently offer those places to individuals or groups. Where a hospice allows individuals to take part in an event, regardless of an entry fee or the amount of sponsorship they raise, and the individuals do not receive any benefits in return for the monies raised, sponsorship income can be treated as a donation and outside the scope of VAT.

HMRC has published guidance confirming that it does not consider the following to be benefits:

- Provision of free training and health advice;
- A free T-shirt, running vest or similar that clearly portrays the charity the individual is taking part on behalf of;
- Free massages and support for physical wellbeing during the event;
- Free pre-event meeting, which may include free professional advice or support, a simple meal, energy drinks and encouragement from the charity and other participants; and
- Free post-event meeting, which may include medical treatment or advice, changing facilities, light refreshments and gives the charity the opportunity to thank participants.

HMRC does, however, consider the provision of free travel or accommodation and other gifts, such as bikes or watches, as benefits. Therefore, where a charity provides such benefits the amount raised by the participant will be subject to VAT at the standard rate. Conversely, any VAT incurred on the cost of providing the benefit would be recoverable in full as it is a cost component of making a taxable supply.

Registration fees and minimum sponsorship

Some charities require individuals to pay a registration fee and/or insist that a minimum amount of sponsorship is raised as a condition for partaking in the event. HMRC regards this as an entry fee and the income is subject to VAT at the standard rate. Where, however, a participant raises sponsorship over and above the registration fee or minimum amount, the excess sponsorship over the registration fee is treated as a donation and outside the scope of VAT. In such circumstances, the charity is entitled to recover a proportion of the VAT incurred on expenses in accordance with the normal rules on VAT recovery.

Where output VAT is paid on the registration fee income, the hospice can recover, in full, the VAT it has incurred on any cost of buying the place from the event organiser, eg gold bond places.

Registration fees will potentially also be subject to direct tax and Gift Aid cannot be claimed on the fees.

Pledges and commitments

In some circumstances, the hospice may request that individuals pledge or commit to raise a certain amount of sponsorship, but the charity does not insist on any payment before allowing the individual to take part in the event. Where this occurs, the total amounts raised can be treated as donations and outside the scope of VAT. In order for the income to be treated as a donation, and outside the scope of VAT, a charity can encourage individuals to pass on sponsorship money as they receive it, but cannot insist on receiving a certain amount before allowing the individual to take part.

Prizes

Hospices may offer prizes to the most successful fundraisers. HMRC does not regard the prizes as benefits for VAT purposes and the prizes do not affect the VAT treatment of income from participants.

Such prizes may be benefits for Gift Aid and may prevent or reduce Gift Aid claims on donations from the participant and/or sponsorship from the participant's family and other connected persons.

Charity challenge events

It is common for hospices to organise treks, bike rides and other sponsored events (treks and challenges) in order to raise funds. These are usually arranged to include travel and accommodation. Income from treks and challenges consists of: (i) registration fees; (ii) minimum sponsorship amounts; and (iii) sponsorship income, ie that received by way of donation in excess of the minimum amount of the sponsorship or registration fee.

The sponsorship income under (iii) above is always outside the scope of VAT on the basis that this represents unrestricted donations from individuals to the charity. The VAT liability of the income under (i) and (ii) above, however, depends on the nature of the trek/challenge and where it takes place, ie in the EU or outside the EU.

The registration fees are taxable income for direct tax and are not eligible for Gift Aid. Where family members of other connected persons of the participant give sponsorship payments, Gift Aid is not available where pledged sponsorship levels are set, as HMRC regards these as payments to secure benefits.

A charity carrying out an activity outside the UK must seek advice on the tax exposure in the other country.

Sponsorship of a charity

Many events organised by charities are sponsored, with charities receiving money, goods or services from their sponsors. Where the charity is obliged to provide the sponsor with a significant benefit in return for the sponsorship, the sponsorship received is treated as business income and taxable at the standard rate.

HMRC has given the following examples of what they regard as "significant benefits":

- Naming an event after the sponsor;
- Displaying the sponsor's company logo or trading name;
- Participating in the sponsor's promotional or advertising activities;
- Allowing the sponsor to use the charity's name or logo;
- Giving free or reduced price tickets;
- Allowing access to special events such as premieres or gala evenings;
- Providing entertainment or hospitality facilities; or
- Giving the sponsor exclusive or priority booking rights.

This list is not exhaustive and there are many other situations in which the charity's sponsor may be receiving tangible benefits in return for sponsorship income. Where a hospice is obliged to do something in return for the income, it is likely that the income will be taxable at the standard rate.

Where no significant benefits are provided, the hospice may be able to treat the income as non-business. HMRC accepts that giving a flag or sticker to a donor, or naming a donor in a list of supporters, is insignificant and does not constitute a taxable benefit for VAT purposes.

Conclusion

The above illustrates that the VAT liability of the income received from participants of events is dependent on a number of factors. It is important to be able to distinguish, from the outset, income that is taxable and subject to VAT and income that is a donation and outside the scope of VAT.

Where income is identified as taxable, the charity may choose to pass the VAT cost on to the participant. Where, however, money is received and the income is only identified as taxable at a later stage, the income will be seen as VAT-inclusive. In such an event, the charity will have to account for VAT from the amount received, thus reducing the quantum of the total income raised.

Finally, where income is a mixture of sponsorship and donation it must be clear that any benefits the sponsor receives are not conditional on the making of the donation. In such cases, VAT will only be due on the sponsorship and not the donation.



11.3 Overseas treks

In addition to the practical and logistical difficulties of organising a successful event, charities often have to contend with the subsequent VAT issues arising. Even where a charity is relieved from the burden of organising an event by entering into a contract with a third party, it is still faced with unravelling the VAT issues.

HMRC acknowledges that the VAT issues surrounding participatory events are far from straightforward. For many years the charity sector has been in discussions with HMRC, with a view to producing accurate guidance to assist fundraisers overcome the VAT obstacle and accurately determine the VAT liability of each event.

General

Fundraising events that include: a package of both travel and accommodation; or bought-in accommodation; or more than two nights' accommodation from a charity's own resources, do not qualify for the fundraising VAT exemption.

Please note, if a hospice is providing up to two nights' accommodation from its own resources, and is not providing a package of travel and accommodation, the income from the event will be exempt under the fundraising exemption.

Is a supply being made?

As previously stated, many hospices offer or encourage participation in "challenge" events as a way of raising funds. If the hospice insists that the participant makes a payment before allowing them to take part in the challenge event, the hospice will be making a supply for VAT purposes.

That supply may be of a package to the participant (if the hospice acts as a principal or undisclosed agent) or of agency services in selling the package/holiday for a specialist company that has put the event together (if the hospice acts as an agent).

There are different VAT implications depending on whether the hospice is acting as (1) a disclosed agent or (2) an undisclosed agent or principal.

(1) Hospice acting as disclosed agent

If the hospice uses a specialist company to organise challenge events, they will normally have a contract setting

out exactly who is responsible for what. A hospice will be acting as a disclosed agent if:

- Both the hospice and the specialist company have agreed that the hospice will act as the company's agent; and
- The hospice discloses the name of the principal (the specialist company), for example in the event terms and conditions and on all tickets issued; and
- The hospice is not taking any significant commercial risk in relation to the event, for example the hospice does not have any financial liability should something go wrong.

If the hospice is acting as a disclosed agent, any commission which the hospice receives will be subject to VAT at the standard rate, regardless of where the event takes place.

In HMRC guidance, the example of a charity promoting a challenge event in China is given with the charity using the services of a specialist company that is VAT-registered in the UK and acting as its disclosed agent, as explained above. The participants pay the charity £1,750 (£250 booking fee plus £1,500 sponsorship) before the charity allows them to take part in the challenge event. This is the cost of the event and constitutes a supply for VAT purposes made by the specialist company. The charity, acting as disclosed agent, has agreed with the specialist company that it will receive a commission of £550, and it invoices the specialist company for this amount plus £91.66 VAT, as the commission is taxable at the standard rate. This VAT of £91.66 is due from the charity as output tax (and can be reclaimed by the specialist company as input tax).

As the charity has made a taxable supply it can reclaim any UK input tax it has incurred in promoting the event (subject to normal VAT reclaim rules). Any further money raised by the participant and passed on to the charity is a donation and is outside the scope of VAT provided it is not consideration for other goods or services.

(2) Charity acting as a principal or undisclosed agent

If the charity is acting as a principal or undisclosed agent it will need to follow the Tour Operators Margin Scheme (TOMS) to calculate any VAT due. VAT will be due on the margin between what the cost (excluding overheads) is to the charity to provide a place on the event and what the charity insists on receiving as payment before allowing



the participant to take part. For events/packages that take place within the EU, the margin will be taxable at the standard rate. For events/packages which take place outside the EU, the margin will be taxable at the zero rate. The following examples, illustrated in HMRC guidance, demonstrate the basic principles:

An event outside the EU

A hospice arranges a challenge event where participants will cycle across part of the Sahara. The hospice organises flights, accommodation, food, equipment and the services of expert guides and a small medical team. The participants pay the hospice £1,450 (£200 booking fee plus £1,250 sponsorship) before the hospice allows them to take part in the challenge event.

The hospice receives £1,450 and a place on the event costs the hospice £900 to provide. The margin the hospice has made is £550. The event is taking place outside the EU, so the margin is taxable at the zero rate and no VAT is due. The hospice cannot reclaim any VAT it has incurred on the tour elements but it can reclaim, outside the TOMS, VAT on overhead costs incurred in the UK in putting the event package together (subject to normal VAT reclaim rules). Any further money raised by the participant and passed on to the charity is a donation and is outside the scope of VAT, provided it is not consideration for other goods or services.

An event inside the EU

A hospice arranges a challenge event where participants will cycle from London to Paris. The hospice organises train travel, accommodation, food, equipment and the services of expert guides and a small medical team. The cost of these to the hospice is £900. The hospice promotes the event to its supporters. The participants pay the hospice £1,450 (£200 booking fee plus £1,250 sponsorship) before the hospice allows them to take part in the challenge event.

The hospice receives £1,450. A place on the event cost the charity £900 to provide. The margin the hospice has made is £550. The event is taking place inside the EU so the margin is taxable at the standard rate and VAT is due at 1/6 of the margin (ie £91.66).

Once again, the hospice cannot reclaim any VAT it has incurred on the tour elements, but it can reclaim, outside the TOMS, VAT on overhead costs incurred in the UK in putting the event package together (subject to normal VAT reclaim rules); it cannot claim any VAT incurred on overhead costs outside the UK via the UK VAT return. Any further money raised by the participant and passed on to the hospice is a donation and is outside the scope of VAT, provided it is not consideration for other goods or services.

Conclusion

The VAT liability surrounding this area has traditionally been riddled with complexity and uncertainty. What the guidance does achieve is certainty for the hospice and this

should be welcomed. Fundraisers are advised to consider the new guidance when organising participatory events and to consider where VAT may now be due on certain events.

11.4 Sale of donated goods

The sale of donated goods by a hospice or its trading subsidiary is a zero rate activity. It does not matter where there goods are sold, ie in a charity shop, at an event or auction on eBay etc, the zero-rating still applies (see also section 12.1).

In order to qualify for the zero rate relief, the donated goods must be made available to the general public and must not be subject to any pre-sale arrangements between any of the parties involved. Similarly, the goods must not be used for any purpose other than being made available for public sale.

HMRC does not generally consider the sale of donated goods to be trading or an otherwise taxable activity for direct tax purposes.

11.5 Sale of bought-in goods

The sale of goods bought in by a hospice, or its trading company, will always be liable to VAT at the standard rate of 20% unless it falls into one of the following exceptions:

- Goods which are normally zero rate in their own right, such as certain printed matter, children's clothing, certain food stuffs;
- Goods sold at a one-off charity fundraising event which qualifies for the fundraising exemption, for example goods sold at an auction mid-way through a dinner;
- Goods exported outside the EU; and
- Goods sold to a person in 'business' in another EU member state.

Unless the sale is carried out in the performance of the charity's primary purpose objects, the profits generated from the sale will be liable to direct tax, unless the hospice is within the small trading exemption limit of £50,000. This being so, it is usually preferable to undertake such activity in a trading company.

12 Charity shops

It is a common practice for hospices to have charity shops on the high street. Whether this is one or two shops, or a more substantial retail operation, the use of charity shops is very efficient for tax, Gift Aid and VAT purposes. This is even more the case following the ability to operate retail sales using the retail Gift Aid scheme.

12.1 Sale of donated goods

The sale of donated goods by a hospice or its trading subsidiary is a zero rate activity.

In order to qualify for this relief, the goods must generally be made available to the general public and must not be subject to any pre-sale arrangements between any of the parties involved. Similarly, the goods must not be used for any purpose other than being made available for sale.

The only exception to this rule is where the donated goods are, by reason of their poor quality, not fit for sale to the general public. An example of where the concession can be used is for the sale of substandard clothing to rag merchants or the sale of electrical items, toys etc, where their sale to the public is prevented under safety legislation.

12.2 Sale of bought-in goods

The sale of goods bought-in for re-sale is a standard rate activity and accordingly, unless the goods are zero rate in their own right (eg books, children's clothing etc), 20% VAT is due to be declared as output tax (see also section 11.5).

The sale of bought-in goods is trading, and hence potentially liable to direct tax on the profits generated.

12.3 Retail Gift Aid scheme

Over the past couple of years it has become commonplace for the majority of charities that operate charity shops to restructure their retail activity to benefit from the Gift Aid arrangements. This is because the Gift Aid rules only permit Gift Aid to be claimed on cash donations, and not gifts in kind, such as donated goods. Accordingly, rather than simply donate goods, the charity will sell the goods as agents and donors will be requested to donate the cash value realised from the sale of their goods so that



this income can be donated to charity under the Gift Aid arrangements, assuming all other requirements are met.

A commission is charged to the donor for the agent's services in selling the goods.

We strongly recommend that any hospice seeking to implement the retail Gift Aid arrangements take professional advice to ensure the correct procedures are put into place.

12.4 VAT recovery on shop costs

Historically, charity shops have always enjoyed the status of being a fully taxable activity and, as such, VAT incurred on the attributable costs has been able to be fully recovered.

Additionally, it is possible to use this taxable activity to good effect for the purpose of increasing the hospice's overhead POT recovery rate by its inclusion within the business/non-business apportionment and partial exemption calculations. With this in mind, great care should be taken to use a methodology which maximises the influence of the retail activity. For example, the use of a headcount or full-time equivalent method may be advantageous as it is generally accepted by HMRC that each shop may require up to four or five full-time equivalent staff to operate.

Any suggestion from HMRC that the inclusion of the retail activity within these calculations is distortive should be fiercely defended.

Where the retail Gift Aid arrangements are in place, a full VAT recovery on shop costs can still be enjoyed, providing the VAT-able donor commission is being applied.

13 New buildings, extensions and refurbishment projects



13.1 New buildings

In principle, the construction of a new hospice is zero rate. This is because the VAT legislation specifically includes a hospice within the meaning of a building used for a "relevant residential purpose". Additionally, a new hospice may qualify as a building used by a charity for non-business purposes. This will be dependent upon the funding of the care activity (exempt or non-business) and possibly the precise use of the building, which cannot be more than 5% business use.

Where, however, a new standalone building is constructed in the grounds of an existing hospice, achieving a zero rate construction can be far more problematic; HMRC views this as the provision of additional facilities at an existing hospice and not the provision of a new hospice.

13.2 Extensions/annexes

There is no VAT relief available for the construction of an extension or enlargement to an existing hospice. This rule applies equally to either an extension or enlargement of an existing building, or a new standalone building (a new standalone building may qualify for non-business use by a charity, depending upon the funding of the care activity within the hospice).

There is, however, a zero rate relief for the construction of an annexe used by a charity solely for non-business purposes (in this context, 'solely' means at least 95%). The distinction between an extension/enlargement and an annexe for VAT purposes appears particularly officious and trite and achieving the status of a building being an annexe is notoriously difficult.

HMRC gives the following criteria to be met in order for a building/extension to be treated as an annexe:

- The works amount to the construction of an annexe, rather than merely being the alteration, enlargement or extension of an existing building; and the annexe is capable of functioning independently of the existing building; and
- The only access or (if there is more than one means of access) the main access to the annexe is not via the existing building; and
- The only access or (if there is more than one means of access) the main access to the existing building is not via the annexe.

Generally speaking, if the new build area merely provides additional space for the existing activities undertaken at the hospice, it will not be seen by HMRC as an annexe and will thus be subject to VAT at the standard rate of 20%.

13.3 Refurbishments/restorations

The refurbishment or restoration of an existing building will generally be subject to VAT at the standard rate of 20%.

The only exceptions to this are where either the works are:

- The conversion of a non-residential building solely for use by the hospice (5% rate applies); or
- The restoration of a residential building that has been empty for two years or more (5% rate applies).

13.4 Listed buildings

Perversely, it is not the maintenance and restoration of a listed building which attracts VAT relief but rather oddly, the alteration.

Alterations which require, and have received, the approval of the local listed building authority to a grade two (or above) listed building intended for use as a hospice are zero-rated. Works of repair and maintenance are subject to VAT at the standard rate of 20%, unless they qualify as reduced rate works.

This relief was withdrawn on 21 March 2012. However, under a transitional relief, zero-rating can still apply up to 30 September 2015 if either listed building approval or a written contract was in place by 21 March 2012.

13.5 VAT recovery on building projects

As outlined above, there is only limited opportunity to prevent VAT being incurred on the majority of building works undertaken by a hospice. This being so, thought needs to be given to how the maximum recovery of VAT incurred on such works can be achieved.

Works costing £250,000 or more

Any major works undertaken, which are treated as capital expenditure in the hospice's accounts, and with a value of £250,000 or more (excluding VAT), are subject to a special VAT arrangement termed the Capital Goods Scheme (CGS).

Under the CGS, the VAT incurred on these works is originally recovered in the year in which it is incurred, at the hospice's agreed rate of VAT recovery, using the business/non-business apportionment and partial exemption calculation (see section 5.3). Following this, the actual use of the relevant property must be considered year-on-year for a period of 10 years. This is so that the original level of VAT recovered can be annually adjusted to reflect any change in the taxable, exempt and non-business use of the property.

The CGS should be viewed as an opportunity as much as an administrative burden. This is because if the property is used for taxable purposes to a greater extent than the general overhead POT recovery methods estimate, a greater level of VAT can be recorded on the works. Of



course, the opposite is also true. For example, HMRC may consider that new accommodation is all but wholly used for care purposes and accordingly argue that very little, if any, VAT should be recovered.

It is usually possible to agree with HMRC that the general overhead POT recovery rate can be applied to such expenditure, but this is not always the case.

Works costing less than £250,000

Any works costing less than £250,000 (excluding VAT) are not subject to the CGS. The recovery of VAT incurred on such works is determined in accordance with the normal VAT recovery rules (see section 5).

It is usual for major building works to fall within the general overhead POT recovery procedure as outlined at section 5.3. Where, however, works relate wholly to a taxable activity, such as a charity shop refit, the VAT incurred can be recovered in full under the normal rules.

Summary

The recovery of VAT on building works is a matter where a hospice should seek professional advice to ensure the optimum level of recovery is achieved, particularly where the cost of the works exceed £250,000 and falls within the CGS.

14 Expenses, subsistence and motor costs

14.1 General costs

Subsistence expenses

Where an employee is paid a flat rate for subsistence expenses, no VAT can be claimed as input tax. If the hospice pays the actual cost of the supplies, input tax incurred can be reclaimed as below. If the hospice pays a proportion of the actual costs, it can reclaim as input tax the VAT fraction of the amount it pays, subject to the normal recovery rules.

Meals

Any VAT incurred on meals for employees can be treated as input tax, provided it is not business entertainment.

Hotel accommodation

All VAT incurred on accommodation for employers and employees, when away from the normal place of work, can be treated as input tax subject to the normal requirements.

Where, occasionally, an employee uses overnight accommodation near the normal workplace, VAT incurred is input tax and deductible if the employer requires the employee to stay in the accommodation and the expense is fully borne by the hospice and recorded as such in the accounting records.

Trustee expenses

VAT incurred on expenses by trustees of the hospice is recoverable as input tax, subject to the normal requirements. The basis of this is that the trustees are effectively treated as employees for this purpose.

Volunteer expenses

VAT incurred on expenses by volunteers is also recoverable as input tax, subject to the normal requirements.

Business entertainment

VAT charged on business entertainment cannot be recovered as input tax.

'Business entertainment' means entertainment (including hospitality of any kind, given free of charge) provided by the hospice in connection with an activity carried on by it, but does not include the provision of any such entertainment for employees only of the hospice.

HMRC regards "business entertainment" as the following, provided to persons other than employees:

- The provision of free food and drink.
- The provision of free accommodation (such as hotels)
- The provision of free theatre and concert tickets.
- Free entry to sporting events and facilities.

With effect from 1 May 2011, entertainment provided to overseas clients can be recovered provided it is of a scale and kind of which is reasonable.

Travelling expenses

Taxi fares

Zero-rating of domestic passenger transport does not apply if the vehicle is designed to carry less than 10 passengers. Taxi and hire car fares are, therefore, standard-rated and if the business provider is registered for VAT, it must charge VAT to its customers. Extra charges for baggage, waiting time, etc are also standard-rated, as are referral fees from other taxi businesses. Tips and gratuities given voluntarily are not payments for supplies and are outside the scope of VAT.

In order to recover VAT on taxi fares, you must obtain a VAT receipt as evidence for input tax. It should be noted that the majority of taxi drivers are not VAT registered and it is therefore unlikely that much VAT will be incurred on such expenses.

Rail travel

Passenger transport by rail is zero-rated.

Air travel

Passenger transport by air is also zero-rated.

Evidence for input tax claims on expense items

At the time of claiming input tax, a document must be held to support the claim for input tax. This would normally be the supplier's invoice.

If the value of the expenditure is less than £25 (including VAT) no VAT invoice is required. This expenditure must relate to:

- Telephone calls from public payphones.

- Purchases through coin operated machines.
- Car park charges (except on the street meters).
- A single or return standard-rated toll charge paid at a toll booth.

A less detailed tax invoice can be accepted for expenditure where the value is less than £250.

The VAT invoice need only contain particulars of:

- The name, address and registration number of the retailer;
- The time of supply;
- A description sufficient to identify the goods or services supplied;
- The total amount payable, including VAT; and
- For each rate of VAT chargeable, the gross amount payable including VAT, and the VAT rate applicable.

Credit card receipts cannot be accepted unless they have been adapted to serve as a less detailed tax invoice.

14.2 Motor car costs

Purchase / hire

VAT can be recovered in full on the cost of any car bought solely for use in relation to a taxable activity (eg retail) and not for any other purpose, including private use. Similarly, VAT can be recovered at the partial recovery rate on the cost of a pool car providing it is:

- Normally kept at the hospice;
- Not allocated to an individual; and
- Not kept at an employee's home.

If you lease hire a car then the hospice can normally treat 50% of VAT incurred on the hire charges, and any other charges under the terms of the lease, as POT VAT and make a partial recovery in line with general overhead costs.



Repairs and maintenance

If a motor car is used by the hospice wholly for its taxable activity (eg retail), VAT incurred on repairs and maintenance costs can be recovered in full, providing the hospice (or the trading subsidiary) pays for the services. It does not matter whether the motor car is also used by the employee for private motoring.

If a motor car is used for taxable, exempt and non-business activities, VAT incurred on repairs and maintenance costs can be partially recovered.

Fuel costs

The treatment of VAT incurred on fuel costs depends on whether or not there is any private use of the vehicle.

No private use:

1. Claim all VAT incurred because the motor car is wholly used for a taxable activity; or
2. Claim the POT rate partial VAT because the motor car is used by all departments of the hospice.

Some private use of vehicle, including home to work driving:

3. Claim all VAT incurred and apply a fuel scale charge; or
4. Use detailed mileage records to distinguish between hospice business and private mileage; or
5. Claim no VAT incurred.



The choice would depend on the value of the VAT reclaimable as compared to the administrative burden of monitoring the level of private usage.

The fuel scale charge is a value of output tax payable by the hospice on its quarterly VAT returns, based upon the carbon dioxide emission rating of the car. This effectively accounts for private mileage and enables the hospice to recover all VAT incurred on fuel costs.

If you pay a mileage allowance to employees, the hospice can treat VAT incurred on the fuel element of the allowance as input tax subject to the normal rules. The allowance must be based on actual miles travelled and be supported by detailed mileage records and the tax invoice for the purchase of the fuel by the employee.

Appendix A:

Charity advertising request for zero-rating

PART 1 - to be completed by the charity

(tick boxes as appropriate) (*delete as appropriate)

I.....(full name)
(status in organisation)
 of.....

(name and address of organisation)

declare that the above named charity is *buying from / importing from:

.....

(name and address of supplier)

the following which *is / are eligible for the relief from VAT under item

8 or 8a 8b or 8c of zero rate Group 15:

OR qualify as

- Printed appeals letters
- Printed envelopes for use with appeals letters
- Printed monetary donation collection envelopes
- Monetary donation collecting boxes
- Lapel stickers or badges or component parts

.....(signature and date)

NOTE: It is the supplier's responsibility to ensure that the goods or services supplied are eligible before zero-rating them

PART 2 - for use by the supplier

I have read the guidance in HMRC VAT Notice 701/58 and agree that the goods/services described come within the category indicated.

.....(signature and date)

This certificate should be retained by the supplier for production to his VAT officer.

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