

VAT for hospices

made simple



July 2015

Sayer Vincent LLP

**Chartered accountants
and statutory auditors**

Invicta House

108–114 Golden Lane

London EC1Y 0TL

Offices in London, Bristol and Birmingham

020 7841 6360

svinfo@sayervincent.co.uk

www.sayervincent.co.uk

 [@sayervincent](https://twitter.com/sayervincent)



Published by Sayer Vincent LLP

Chartered accountants and statutory auditors

Limited liability partnership registered in England and Wales
OC390403

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Introduction

A new VAT refund scheme (the 's33c refund scheme') for eligible hospices was introduced on 1 April 2015. The scheme applies to both VAT registered and unregistered hospices. The scheme provides a refund for the VAT incurred on purchases are used in an eligible hospices' non-business activities.

The first section on section 33c explains how to determine if a hospice is eligible for the scheme and how s33c claims are made.

VAT categories for income explains how to distinguish between your non-business, exempt and taxable activities.

How to reclaim VAT on purchases explains how to determine the amount of VAT that can be reclaimed by a hospice. It explains the special VAT rules for apportioning VAT incurred on mixed use costs such as overheads.

Zero-rating and reduced rating reliefs on purchases outlines the main VAT reliefs for hospices. VAT registered and unregistered hospices are eligible for a wide range of VAT reliefs. These work by zero-rating or reduced-rating a purchase that would otherwise bear standard-rated VAT.

Fundraising and VAT explains the key VAT issues involved in fundraising activities commonly undertaken by hospices. These include: charity shops (selling donated goods), fundraising events, challenge events and sponsorship.

The Appendix on how VAT works is for readers who are new to VAT and explains how VAT works including the meanings of output VAT and input VAT.

The s33c refund scheme

A new VAT refund scheme (the *s33c refund scheme*) for charitable hospices has been introduced. It applies to purchases made on or after 1 April 2015. It provides a *palliative care charity* with a refund for the VAT it incurs on purchases that are for use in its *non-business activities*.

A palliative care charity is defined as ‘a charity the main purpose of which is the provision of palliative care at the direction of, or under the supervision of, a medical professional to persons who are in need of such care as a result of having a terminal illness’. Medical professional is defined as a registered medical practitioner or a registered nurse.

In this guide we refer to palliative care charities as hospices. To take advantage of the s33c scheme all hospices will have to be able to distinguish between their business activities and their non-business activities. This is explained in the next section.

Establishing the main purpose of the charity

To establish the main purpose, the charitable purposes or objectives set out in the governing documents must be considered in the light of the actual activities undertaken.

If the only or the main purpose is the provision of palliative care and the charity operates within its objects and powers, then the charity should qualify for the s33c refund scheme. If there are multiple purposes, some of which are not related to or ancillary to the provision of palliative care, the main purpose must be established. The refund scheme is available only if the main purpose is palliative care.

What if palliative care is not the main purpose?

If the main purpose of the charity is not palliative care, but palliative care services are provided, then options for obtaining s33c VAT refunds for non-business activities include:

- Transferring palliative care activities into a separate charity, which has as its main purpose the provision of palliative care.
- Ceasing, reducing or transferring non-palliative services and/or increasing palliative care services so that palliative care becomes the main purpose (including changing the objects as required).

Making s33c claims

There are different claim procedures for hospices that are registered for VAT and for unregistered hospices.

- VAT registered hospices. If the hospice is VAT registered, it includes the amount of VAT claimed under s33c in box 4 of the UK VAT return.
- Unregistered hospices. If the hospice is not registered for VAT, refund claims must be made on HMRC form VAT 126. This is available on the gov.uk website. It must be completed online, printed out and then posted to the address on the form. When your first claim has been approved HMRC will send you a reference number which should be quoted on all future claims. A VAT 126 claim must relate to a period of at least one calendar month, or at least 12 months if it is for less than £100. The period you choose must end on the last day of a calendar month.

Monthly returns

If a hospice is VAT registered, its VAT returns must normally be submitted quarterly. However, a VAT registered entity may request monthly VAT returns. This can be advantageous from a cash-flow perspective but against this must be offset the extra work involved in submitting monthly VAT returns.

Record keeping

For both VAT registered and unregistered hospices, you must keep the purchase invoices and other records to support your claims for at least six years, unless you have applied in writing, and HMRC has agreed to you keeping them for a shorter period. All purchase invoices must normally be bona fide VAT invoices made out to the hospice, though there are a few situations in which HMRC will accept alternative evidence.

Types of VAT that can be claimed

The types of VAT that can be claimed under s33c are:

- UK VAT charged by a UK VAT registered supplier.
- UK import VAT incurred on an import of goods into the UK.

UK VAT registered hospices can also claim for:

- UK reverse charge VAT, incurred on a 'reverse charge' purchase of services from outside the UK.
- UK acquisition VAT payable on an acquisition of goods from a VAT registered EU supplier.

However, only UK VAT can be claimed. Any non-UK VAT (for example French VAT) charged by a non-UK supplier cannot be claimed in the UK VAT return or in a VAT 126 claim.

Deadline for claims

A VAT 126 claim can be made within four years of the end of the month on which the supply was received (*VAT Notice 1001 Section 4.3*). For example, for a supply of goods in July 2015, you must submit your claim by 31 July 2019.

For VAT registered hospices, HMRC say you must make your claim within four years of the due date of your return for the VAT period (VAT quarter/month) in which the VAT became chargeable (*VAT Notice 1001 section 3.4*).

VAT categories for income

Your income streams must be sub-divided into the following types:

- **Non-business income** 'outside the scope of VAT'. No output VAT charged
- **Business income** 'within the scope of VAT'. Output VAT is potentially charged if VAT registered.

If you are registered for VAT, business income must be further differentiated between:

- **Exempt income** within the scope of VAT but no output VAT charged
- **Taxable income** within the scope of VAT and output VAT charged at the relevant rate (standard-rated: 20%, reduced-rate: 5% or zero-rate: 0%).

If the total taxable income in the last 12 calendar months (or next 30 days alone) exceeds the VAT registration threshold (2015/16: £82,000), you must register for VAT.

Non-business income

Grants, public donations, legacies and similar

Grants, public donations and legacies are normally seen as outside the scope of VAT on the basis they are not consideration for any supply. However, grants calculated per unit of output can be seen as consideration for a business supply of the output.

Passive financial investment income

Bank interest, income and gains from financial investments, dividends etc. are all non-business income for a charity.

Contract income

This can be either business or non-business:

- **Standard NHS service level contract in England** HMRC accept that funding provided under the 2015/16 NHS standard service level contract is non-business (VAT Notice 1001 Section 2.4.2).
- Standard NHS service level agreements in Scotland, Wales or Northern Ireland HMRC accept the standard NHS service level agreement in Scotland, Wales or Northern Ireland is non-business (VAT Notice 1001 Section 2.4.2).
- **Continuing care contracts** HMRC consider income from continuing care contracts for named individuals to be normally VAT exempt business income (VAT Notice 1001 Section 2.4.2).
- **Personal budget contracts** HMRC consider income under personal budget contracts to be VAT exempt business income (VAT Notice 1001 Section 2.4.2). However, we understand they do accept they are eligible for the 15% welfare services concession. See *Subsidised welfare services concession* below.
- **Other contracts** there are two situations that may apply, which are explained below. If the income is business, you must then check to see if it is VAT exempt, zero-rated, reduced rate or standard-rated.

Subsidised welfare services concession

HMRC accept (at VAT Notice 701/1 Section 15.8) that charities that provide welfare services at significantly below cost to distressed persons for the relief of their distress, may treat these supplies as non-business and outside the scope of VAT. *Significantly below cost* means subsidised by at least 15%. The

subsidy must be available to everyone. The charity must also be providing the service to the distressed individual, and not to a local authority. At July 2015 it is understood that HMRC do not accept that NHS continuing care contracts are eligible for this concession, though HMRC do accept contracts under personal health budget agreements are eligible.

The business tests

UK case law has established the 'business tests' to determine if an activity is a business activity (and hence if income generated by that activity is business income):

- 1 Is the activity a serious undertaking earnestly pursued?
- 2 Is the activity pursued with reasonable continuity?
- 3 Is the activity substantial in amount?
- 4 Is the activity conducted in a regular manner and on sound and recognised business principles?
- 5 Is the activity predominantly concerned with the making of supplies to consumers for consideration?
- 6 Is the activity such as consists of supplies of a kind which, subject to differences of detail, are commonly made by those who seek to make profit from them?

The tests are not a checklist but a series of questions to ask about an activity in order to determine its status. The fifth test (predominant concern) does not consider the subjective aim pursued by the supplier but considers whether the activity concerned has sufficient 'economic content'.

Staff secondments

HMRC accept (at VAT Notice 701/1/04 Section 5.17) that if staff from one charity or non-profit voluntary organisation are seconded to another on a cost reimbursement basis the consideration can be treated as non-business and outside the scope of VAT, provided the employee has been engaged only in the non-business activities of the lending charity/organisation and is being seconded to assist in the non-business activities of the borrowing charity/organisation. The payment for the provision of the employee's services must not exceed the employee's normal remuneration, NI, pension contribution etc.

Exempt income

Business supplies of care services

Most business supplies of health and welfare services (and ancillary supplies) by hospices to terminally ill persons are likely be VAT exempt. Exemption covers business supplies of medical care and business supplies of welfare services by charities, and ancillary sales. Welfare services include: services directly connected with the provision of care, treatment or instruction designed to promote the physical or mental welfare of elderly, sick, distressed or disabled persons; and services directly connected with the care or protection of children and young persons.

Business supplies of education or vocational training

A business supply of education or vocational training by an *education eligible body* is VAT exempt:

- Education means a course, class or lesson of instruction or study in any subject, regardless of when and where it takes place.
- Vocational training means training, re-training or the provision of work experience for any trade, profession or employment or for any voluntary work connected with education, health, safety, welfare or the carrying out of activities of a charitable nature

Education eligible bodies include charities and other non-profit distributing bodies provided they ring fence any profits from educational supplies to the continuance or improvement of such supplies. If not an eligible body supplies of education and vocational training are standard-rated.

Business supplies in connection with qualifying fundraising events

Sales of goods or services in connection with a qualifying fundraising event are VAT exempt. See the section on *Fundraising and VAT* below.

Lotteries

Income from the sale of lottery tickets and from other games of chance is VAT exempt. This includes commission on selling other people's lottery tickets, such as the National Lottery. If you run your own lottery or games of chance, the exempt turnover is the full amount of the stakes or takings, less any money paid out in winnings or, if the prizes are goods, their cost (including irrecoverable VAT).

Zero-rated income

Sale of donated goods

The sale or hire by a charity or a 'profits to charity person' of goods donated to it for sale or hire is zero-rated. See *Fundraising and VAT* below.

Sales of printed matter

Supplies of printed-on-paper books, booklets, magazines, journals, newspapers and similar are zero-rated. Zero-rating covers outright sales and the hire or loan of qualifying printed matter. However, zero-rating excludes: printed products with more than 25% areas for completion such as diaries and address books; posters, calendars, postcards, greeting cards and similar. Also excluded are sales of electronic publications and sales of publications on digital carriers such as CDs or DVDs.

Supplies of children's clothing and footwear

The supply of clothing or footwear designed for children under 14 and not suitable for use by older children or adults is zero-rated. HMRC publish tables of accepted children's sizes (*VAT Notice 714 Section 4.2*). The sale of certain protective boots and helmets is also zero-rated.

Reduced rate income

Supplies of welfare advice or information

A business supply of welfare advice or information by a charity is reduced rate, for example a CD or DVD containing welfare advice or information, though reduced rating does not cover dual purpose goods such as a t-shirt with a printed message.

Separately metered supplies of gas and electricity

If you sub-let property to another organisation but make separate charges for metered gas and/or electricity, these separate charges are by default VAT standard-rated but might be eligible for reduced rating.

Standard-rated income

Standard-rating is the default for taxable supplies so a taxable supply is standard-rated unless it falls into one or more of the zero or reduced rating categories. Standard-rated supplies include:

Challenge event commissions

Where a charity or its subsidiary acts as agent of a challenge event organiser in recruiting participants and handling payments, the agency commission is a standard-rated supply for the agent.

Sale of bought in goods

A charity can zero-rate sales of donated goods however there is no general zero-rating for sales of bought in goods, their supply will therefore be standard rated, unless the goods qualify for zero-rating or reduced rating in some other way (for example as supplies of printed matter, children's clothing or welfare advice or information)

Management charges

These are charges made by one entity for providing management services to another, for example administration services, services of managers, IT support, financial support etc. Management charges made by a hospice to its trading subsidiary are standard-rated.

Consultancy services

General business advice is standard-rated.

Advertising services

Supplies of advertising in publications, on websites, on notice boards, bill boards etc. is by default standard-rated, however, supplies of advertising to a charity are zero-rated.

Commission on retail Gift Aid scheme

If you operate the retail Gift Aid scheme then any sales commission charged to donors under the scheme is standard-rated.

Catering sales

Catering includes the provision of hot or cold food or drink for consumption on the premises where they are supplied. By default supplies of catering are standard-rated. For local authority and academy schools, which can also recover non-business VAT via similar schemes to s33c (In s33 and s33b VAT Act 1994), HMRC accept that income from sales of catering from shops, trolleys and vending machines to pupils at or below cost can be treated as non-business. However, there is (as yet) no similar acceptance by HMRC for sales of catering by hospices to patients.

HMRC do accept that catering supplied for a charge as part of an exempt welfare service is also exempt as a supply that is closely related to an exempt supply of care. This includes meals for residents of hospices and care homes, and supplies of food and drink (but not alcohol) from trolleys, canteens and shops to patients (see *VAT Notice 701/1 Section 5.6*). HMRC do not accept that catering provided to non-patients such as staff and family members for a fee is covered by the exemption, unless the supply is to a relative staying with a sick child (see *VAT Notice 701/31 Section 2.12*). If catering is provided for free its provision is a non-business activity.

How to reclaim VAT on purchases

From 1 April 2015 a charitable hospice can claim for the VAT it incurs on purchases as follows:

	Unregistered hospice	VAT registered hospice
Full VAT claim	<p>If you undertake solely non-business activities</p> <p>You can claim all VAT incurred on purchases via s33c</p> <p>You need to record all VAT incurred on purchases and claim via the VAT 126 form</p>	<p>If you undertake solely non-business activities and taxable business activities</p> <p>You can recover all VAT incurred on purchases</p> <p>You need to record all VAT incurred on purchases and enter in box 4 on the VAT return</p>
Partial VAT claim	<p>If you undertake a mix of business and non-business activities</p> <p>You can claim for VAT incurred in non-business activities but not for VAT incurred in business activities</p> <p>You need to record VAT incurred on purchases used in your non-business and mixed/residual activities, apportion the latter and claim via the VAT 126 form</p>	<p>If you undertake non-business activities, exempt and taxable business activities</p> <p>You can recover the VAT incurred in the taxable and non-business activities. You can only recover the VAT incurred in exempt activities if the overall level of exempt activity is de-minimis (see below)</p> <p>Record all VAT on purchases and distinguish between VAT incurred in non-business, exempt, taxable and mixed/residual activities. Apportion the latter and claim and recover in box 4 on the VAT return</p>
No VAT claim	<p>If you undertake solely business activities</p> <p>You cannot claim for any VAT incurred. No need to record VAT incurred on purchases</p>	

Blocked VAT

VAT incurred on certain purchases is 'blocked' and is always irrecoverable. Blocked VAT includes VAT incurred on:

- **Business entertaining** this means the provision, in the course of a business activity, of free entertainment to people who are not employees. Entertainment includes food, drink, accommodation and entrance to events
- **Cars available for private use** Where cars are purchased for employee use and the car will be available for private use then recovery of the VAT incurred on the car is blocked.

Recording VAT on purchases

Most accounting software has a VAT facility which may require activating. Once activated, you then record, at the point of entry, the VAT incurred on each purchase transaction. Manual or spreadsheet ledger based systems could be modified to provide extra analysis columns so the gross (VAT inclusive) purchase cost can be split between net cost and VAT.

VAT pools

Hospices in a partial VAT recovery position will have to assign the VAT incurred on purchases to one of several 'VAT pools' and then carry out periodic calculations on the

balances in those pools to determine how much of that VAT can be claimed:

Hospice not VAT registered

- 1 **Non-business pool claim in full**
- 2 **Business pool no claim**
- 3 **Residual pool part claim**
(business/non-business method)

Hospice VAT registered

- 1 **Non-business and taxable pools claim in full**
- 2 **Exempt pool no claim unless exempt activity is de-minimis**
- 3 **Residual pool part claim** (business/non-business and partial exemption methods)

Assigning purchase VAT to the pools

To determine which pool to assign the VAT incurred on a purchase to you need to decide which type of activity the purchase will be used in. VAT on a hospice purchase is likely to fall within one of the following:

Non-business pool (all hospices)

Business pool (unregistered hospice)

Residual pool (all hospices)

Exempt pool (registered hospice)

Taxable pool (registered hospice)

Wholly grant funded activities

Activities funded wholly from non-business sources – for example grants, non-business NHS contracts, public donations, legacies, reserves, surpluses on fundraising, and financial investment income

Subsidised welfare contracts (that meet the subsidised welfare services concession terms)

Contracts that fail the business tests

Care contracts that do not meet subsidised welfare services concession & ancillary activities
Business supplies of education / training (eligible body only) and ancillary activities
Qualifying fundraising events
Lotteries and games of chance
Property lettings (not opted to tax)

Sale of goods (donated or bought in)
Sale of advertising, use of logos, IPR etc.
Contract education / training (non-eligible body)
Challenge events
Management of a trading subsidiary
Property lettings (opted to tax or special types of property)

Central function costs: CEO's office, HR, admin, finance etc.
Shared premises costs
Trustee costs, audit, statutory filings, AGM, annual report etc.
Assets for mixed use: IT systems, websites, general software etc.
Financial investment management services (but see below)
'Children's Society' costs (but see below)

Accounting systems and VAT pools

There are various ways of assigning the VAT incurred on a purchase to a pool:

- **VAT codes** Many accounting systems have special VAT codes (tax codes, T-codes etc.) for transactions which can be set up to distinguish between the various pools.

- **VAT control accounts** If the system allows multiple VAT control accounts, separate VAT control accounts could be set up for each pool.
- **Nominal / departmental / cost centre / purchase ledger allocations** Another potential option is to link nominal codes, departments, cost centres, suppliers etc. to the pools with VAT incurred by that code/ department/ cost centre/supplier then being assigned to its pool.

Period end routine

At the end of every VAT reporting period (month or quarter) the balance of VAT in each pool is determined:

- The VAT in the non-business pool can be claimed via s33c
- The VAT in the taxable pool can be claimed if the hospice is VAT registered
- The VAT in the exempt pool can be claimed if the hospice is VAT registered and the level of exempt activity is de-minimis (see below)
- The VAT in the residual pool must be apportioned and partly claimed as explained below

A journal is then made to remove the VAT in the pools and record the VAT liability to/from HMRC for the period. Irrecoverable VAT can be either posted to expenditure to go with the associated cost or to a specific expenditure code and apportioned. Another approach is to set custom VAT rates so only recoverable VAT is posted to the VAT control accounts (irrecoverable VAT goes with the net cost).

The business/non-business method

VAT in the residual pool must first be apportioned between non-business and business activities. This apportionment is referred to as the *business/non-business method*. The part of the residual VAT apportioned to non-business activities can be claimed under s33c.

You can use any business/non-business apportionment method you like provided it is *fair and reasonable* and capable of being independently checked by HMRC. Fair and reasonable means it must fairly and reasonably reflect the economic reality of how residual costs are used.

HMRC will enter into agreements regarding business/non-business methods in some situations. If you have entered into such an agreement you may be bound by it. If you have one of the new 'combined' methods agreements (available from 1 January 2011), where no distinction is made between non-business and exempt activities, you will likely have to revise it in order to be able to make claims under s33c. To revise the agreement you should contact the HMRC office that agreed the combined method.

Potential business/non-business apportionment methods

The typical approach is to compare levels of business and non-business activity by use of a suitable and readily quantifiable proxy such as relative levels of income, staff numbers, staff cost, direct expenditure etc. These can normally be taken from the statutory or other annual accounts.

Periodically (annually or quarterly) a s33c recovery percentage is calculated as follows:

$$\text{s33c recovery percentage} = \frac{(\text{non-business level in period})}{(\text{non-business level} + \text{business level in period})} \times 100\%$$

This percentage is multiplied by the amount of VAT in the residual pool for the period. The result is the amount of residual VAT that can be claimed under s33c

Residual VAT to be claimed = Total residual VAT × s33c recovery percentage

Potential proxies for the levels of business and non-business activity include:

- **Income** compare non-business income and business income
- **Expenditure** compare direct costs or direct costs plus apportioned support costs of business and non-business activities
- **Staff** compare staff numbers or the cost of staff working directly in business and non-business activities
- **User visits** compare numbers of user visits for business and non-business activities
- **Floor area** compare floor areas occupied by business and non-business activities
- **Transaction count** compare the number of transactions undertaken by business and non-business activities
- **Activity level** compare other activity statistics

Example – business/non-business method

Hospice A is not registered for VAT. It uses the FTE numbers of staff working in business and non-business activities to apportion residual VAT. The residual VAT for a particular period is £20,000 and the FTE numbers of staff working in different activities (excluding support staff) in that period were:

Working in non-business activities: 12

Working in business activities: 8

$$\text{s33c recovery percentage} = \frac{12}{(8+12)} \times 100\% = 60\%$$

The amount of residual VAT that can be claimed under s33c is:

$$£20,000 \times 60\% = £12,000$$

The annual adjustment

The s33c recovery percentage can be calculated afresh each VAT period or it can be calculated annually via an 'annual adjustment'. An annual adjustment is not obligatory for the business / non-business method however it simplifies the calculation. The general approach is to use last year's recovery percentage on a provisional basis in each VAT period, subject to correction at next year's annual adjustment, with that figure then being used on a provisional basis the next year and so on..

$$\text{S33c annual adjustment} = \frac{\text{VAT claimable at the actual s33c recovery percentage} - \text{VAT actually claimed at the provisional s33c recovery percentage}}$$

If the S33c annual adjustment is positive, the adjustment is added to the next s33c claim, if it is negative it is deducted from the next s33c claim.

Example – annual adjustment

Assume that hospice A used a provisional s33c recovery rate of 50% for VAT in the residual pool and in the whole year the total VAT posted to the residual pool was £100,000. So in the year in question it claimed £100,000 x 50% = £50,000 of the residual VAT on a provisional basis.

The true s33c recovery rate for the year was 60%, resulting in 60% x £100,000 = £60,000 being claimable.

The hospice can claim the difference (£60,000 - £50,000 = £10,000) in its annual adjustment.

If the actual s33c recovery rate for the year is below 50%, the hospice would have to repay some of the residual VAT claimed to HMRC.

The partial exemption method

If a hospice is VAT registered, and if it has VAT exempt activities, it must apportion any remaining residual VAT between exempt and taxable activities. This apportionment is referred to as the *partial exemption method*. By default you must use the *standard partial exemption method* (income based) however you can apply to HMRC to use an alternative *special partial exemption method*, for example an apportionment method based on the numbers of staff.

As with the business/non-business annual adjustment, the general approach is to calculate a year end *business recovery percentage* which is used provisionally next year subject to an annual adjustment. If you use the standard partial exemption method the business recovery percentage can be rounded up to the nearest whole percent (provided total business residual VAT is at most £4.8 million per year), however if you use a special partial exemption method, the business recovery percentage must (normally) be rounded to two decimal places.

The overall recovery rate

The *overall recovery percentage* is the proportion of all residual VAT (including any apportioned to non-business) that can be claimed. This can be calculated as an overall recovery percentage of all VAT posted to the residual pool as:

Overall recovery percentage

$$= \text{s33c\%} + \text{BR\%} \times (100\% - \text{s33c\%})$$

S33c%

= s33c recovery percentage (rounded to two decimal places)

BR%

= business recovery percentage (rounded as appropriate)

Example – standard partial exemption method

Hospice B is VAT registered and has a mix of non-business, taxable and exempt activities. It incurs residual VAT of £100,000 in a VAT year. It uses income based methods. In the year in question, its (net of VAT) income was:

Non-business	£1,400,000
Taxable	£200,000
Exempt	£400,000
Total	£2,000,000

The s33c recovery percentage is:

$$\text{NB\%} = \frac{£1,400,000}{£2,000,000} \times 100\% = 70.00\% \text{ (to 2dp)}$$

The business recovery percentage is:

$$\text{BR\%} = \frac{£200,000}{(£200,000 + £400,000)} \times 100\% = 33.33\%$$

As this is the standard partial exemption method, the business recovery percentage is rounded up to the nearest whole percent:

$$\text{BR\%} = 34.00\%$$

The overall recovery percentage is:

$$70\% + 34\% \times (100\% - 70\%) = 80.20\%$$

This is calculated to two decimal places.

The actual residual VAT that can be claimed in the year is:

$$80.20\% \times £100,000 = £80,200$$

In the above example the overall recovery percentage could be obtained by dividing taxable plus non-business income by total income. However, the ability to round up the standard partial exemption percentage would be missed by this approach.

De-minimis test

The de-minimis test is normally an annual test, carried out in the annual adjustment. If the hospice is de-minimis for the year it is assumed to be de-minimis on a provisional basis in each period of the next VAT year. If not de-minimis it is assumed not to be de-minimis in each period of the next VAT year. These assumptions are then corrected in the annual adjustment.

There are three de-minimis conditions. If one or more of them is met, a hospice is de-minimis and if none of them is met it is not. In the de-minimis conditions: 'Input VAT' means VAT on purchases directly attributed and apportioned to business activities and 'exempt input VAT' means VAT on purchases directly attributed and apportioned to exempt activities.

De-minimis condition 1

- Total input VAT is less than or equal to £7,500 and
- The turnover on exempt supplies is less than or equal to the turnover on taxable supplies

De-minimis condition 2

- Total input VAT less input VAT directly attributable to taxable activities is less than or equal to £7,500 and
- The turnover on exempt supplies is less than or equal to the turnover on taxable supplies

De-minimis condition 3

- Exempt input VAT is less than or equal to £7,500 and
- Exempt input VAT is less than or equal to 50% of total input VAT.

If not carried out on an annual basis, for a VAT quarter the figure of £7,500 above is replaced with £1,875 and for a VAT month it is replaced with £625.

The Children's Society case

The 2005 High Court Children's Society case established that, for a charity, VAT recovery on the costs of raising unrestricted donations depends on how the donations are used:

- If the donations are used to support all of the activities of the charity then the VAT is treated as residual VAT
- If the donations are used wholly to support a hospice's non-business activities, then the VAT can be recovered in full via s33c

This treatment applies to the costs of raising

unrestricted public donations, legacies, and unrestricted public grants. The Upper Tier Tax Tribunal has recently decided that VAT incurred in managing Cambridge University's endowment fund is residual on this basis though at the time of writing it is not known if HMRC will accept or appeal this decision. The business/non-business apportionment may require adjustment to deal with such 'Children's Society costs'.

Zero-rating and reduced rating reliefs on purchases

Charitable hospices can obtain a wide range of VAT reliefs on the purchases they make. A hospice does not have to be registered for VAT or eligible to make s33c claims to obtain these reliefs. The reliefs work by the supplier zero-rating or reduced rating a purchase that would otherwise bear standard-rated VAT.

Even though eligible hospices can now reclaim non-business VAT via s33c, purchases should still be zero-rated or reduced-rated where applicable. HMRC may argue that if a purchase is correctly zero-rated or reduced-rate, there is no standard-rated VAT to be recovered so any s33c claim for the VAT is invalid.

You may have to tell a supplier to treat their supply as zero or reduced rate. For some of the property reliefs a certificate must be provided. For the rest suppliers may ask for a written declaration.

In the reliefs below *disabled person* includes a person who is chronically sick (including terminally ill) and detailed relief specific conditions apply in most situations:

- 1 Medical equipment** Zero-rating applies to the purchase or hire of medical, scientific, computer, video, sterilising, laboratory or refrigeration equipment which is for use in medical research, training, diagnosis or treatment. Zero-rating also includes accessories for such equipment, repairs and spare parts. Zero-rating also applies where the goods are paid for by a third party with voluntary contributions and donated to a hospice.
- 2 Computer software** HMRC accept that computer software is zero-rated when purchased by a charity solely for use in medical research, diagnosis or treatment

but not when purchased for donation to a charity (*VAT Notice 701/6 Section 4.2.5*).

3 Medicines and other medicinal products

are zero-rated when they are for use solely in the provision of care, treatment or research. Medicinal product means:

- any substance or combination of substances presented as having properties of preventing or treating disease in human beings; or
- any substance or combination of substances that may be used by or administered to human beings with a view to (i) restoring, correcting or modifying a physiological function by exerting a pharmacological, immunological or metabolic action, or (ii) making a medical diagnosis.

4 Vehicles

Zero-rating applies to ambulances, adapted motor vehicles, and vehicles for use by a charity providing care for terminally sick persons mainly to transport such persons. Zero-rating includes repairs and spare parts.

5 Equipment for use by disabled persons

Assorted specialist equipment for use by disabled or chronically sick persons qualifies for zero-rating: (a) medical or surgical appliances; (b) electrically or mechanically adjustable beds; (c) devices for sitting over or rising from a sanitary appliance; (d) chair lifts or stair lifts; (e) hoists and lifters; (f) certain adapted motor vehicles; and (g) other equipment and appliances designed solely for use by a disabled person. For (g), the equipment or appliance must be so designed at the point of supply. Zero-rating includes repairs and spare parts

- 6 **Adaptation of goods** The supply to a charity of services of adapting any goods to suit the condition of a disabled person is zero-rated, for example the adaptation of kitchen fittings. The adapted goods must be made available to a disabled person, by sale or otherwise, by the charity.
- 7 **Advertising** Supplies of advertising to a charity in third party media are zero-rated. However this excludes advertising targeted at specific individuals such as direct mail, though the production of direct mail items may be able to be zero-rated (see goods for collecting donations below)
- 8 **Goods for collecting donations** Various goods connected with collecting donations can be zero-rated, including collecting envelopes, pre-printed appeal letters and envelopes, boxes and receptacles used for collecting money, collecting buckets, lapel stickers, emblems and badges. See VAT Notice 701/58
- 9 **Fuel or power** Supplies of gas, electricity, fuel oil, heating, kerosene, coal, solid fuels etc. are reduced rate when:
 - For use by a charity for its non-business activities, or
 - For use in a residential hospice building, or
 - Below certain de-minimis levels – 4,497 kwh per month for gas and 1,000 kwh per month for electricity

VAT reliefs for property

- 1 **Ramps** The construction of a ramp or ramps for the purpose of facilitating a disabled person's entry to or movement within any building is zero-rated
- 2 **Widening doorways** The widening of doorways or passages for the purpose of facilitating a disabled person's entry to or movement within any building is zero-rated
- 3 **Washrooms and lavatories** Providing, extending or adapting a washroom or lavatory for use by disabled persons in a building, or any part of a building, used principally by a charity for charitable purposes is zero-rated where such provision, extension or adaptation is necessary to facilitate the use of the washroom or lavatory by disabled persons. Washroom means a room containing a lavatory or washbasin (or both) but not containing a bath or shower or cooking, sleeping or laundry facilities. A lavatory is a room containing a toilet and possibly, but not always, a washbasin.
- 4 **Bathrooms** Providing, extending or adapting a bathroom for use by disabled persons in residential accommodation, or in a day-centre where at least 20% of the individuals using the centre are disabled persons, is zero-rated where such provision, extension or adaptation is necessary by reason of the condition of the disabled persons. Bathroom includes a shower room.
- 5 **Lifts** The supply to a charity providing a permanent or temporary residence or day-centre for disabled persons of services necessarily performed in the installation of a lift for the purpose of

facilitating the movement of disabled persons between floors within that building is zero-rated.

- 6 **Alarm systems** The supply to a charity of an alarm system is zero-rated if it is for making available to disabled persons (by sale or otherwise) for domestic or their personal use. The alarm system must be designed to be capable of operation by a disabled person, and it must be designed to enable a disabled person to alert directly a specified person or a control centre. Also zero-rated is the supply of services necessarily performed by a control centre in receiving and responding to the calls from the alarm system.
- 7 **Construction of a new building** Supplies in the course of construction of a new 'qualifying building' are zero-rated. Supplies in the course of construction include demolition, site clearance, construction services, building materials and some landscaping costs. A new building is one that is constructed from the ground up, though existing structures such as walls can be retained in some situations. A qualifying building is a building that is:
 - **Relevant charitable purpose** intended for charity non-business use, and/or
 - **Relevant residential purpose** intended for hospice residential use (including ancillary buildings such as kitchens or laundries constructed at the same time as a residential building), and/or
 - **Dwellings** designed as a dwelling or dwellings

If only a part of a building is qualifying, a corresponding portion of the supply can be zero-rated.

The current HMRC guidance says that a hospice only falls within the meaning of *relevant residential purpose* to the extent that it contains residential accommodation. However, it is understood that HMRC have recently accepted that where a hospice constructs a new building and a part of it is intended for relevant residential use, then the while construction can qualify for zero-rating on the basis of relevant residential use, though this has not yet been announced by HMRC.

- 8 **Purchase of a new building from its developer** The first sale by its developer of the freehold or of a long lease in a new qualifying building is zero-rated. See point 7. above for the meaning of new qualifying building. If only a part of a new building is qualifying, a corresponding portion of the contract price can be zero-rated. A long lease is a lease for a term of more than 21 years (not less than 20 years in Scotland).
- 9 **Construction of a relevant charitable purpose annexe** Supplies in the course of construction of a new annexe to an existing building or buildings are zero-rated if and to the extent the new annexe is relevant charitable purpose. Note that relevant residential purpose annexes do not qualify.
- 10 **Residential conversions** The conversion of a non-residential building into a residential building is zero-rated. Residential buildings include residential

hospice buildings. A non-residential building includes a building that was residential but has not been lived in for at least 10 years. The change of use rules also apply (see point 7. above).

- 11 **Renovations and alterations of residential buildings** Certain building works and builder supplied materials qualify for reduced rating when renovating or altering residential property, including residential hospice buildings.
- 12 **Energy saving materials** The installation of certain energy saving materials in residential accommodation qualifies for reduced rating. However the Court of Justice of the EU has recently decided that the UK's reduced rating for energy saving materials is too broad and must be limited to residential accommodation that meets a defined social policy. It is not yet clear if the UK will limit this relief or abolish it altogether.

Fundraising and VAT

Shops

The sale or hire by a charity or a *profits to charity person* (see below) of goods donated to it for sale or hire is zero-rated. The goods can be cleaned or repaired as long as this does not alter their structure or original use. The goods must be available for purchase or hire by the general public or by two or more *specified persons*. Specified person means a person who is chronically sick or disabled or a person who is entitled to any one or more of certain specified social security benefits. By concession (*Extra Statutory Concession 3.21*) HMRC also allow zero rating of the sale of goods in a poor condition and unwanted goods to scrap merchants and similar.

A profits to charity person is a person who has agreed to transfer to a charity the profits from supplies of the goods or a person for whom the profits are otherwise payable to a charity. So sales by a trading subsidiary with an agreement in place to transfer profits in place also qualify for zero-rating.

Sales of bought in goods

Sales of goods that are purchased for sale are by default VAT standard-rated, unless the goods qualify for some other VAT relief, for example, as zero-rated sales of bought in printed matter. Sales of bought in goods at a qualifying fundraising event are VAT exempt unless they also qualify for zero-rating, in which case they are zero-rated.

Retail Gift Aid scheme (RGAS)

This scheme aims to make gifts of goods to a charity shop eligible for Gift Aid, the Gift Aid scheme being limited to monetary donations. Under RGAS, the charity or its trading subsidiary enters into an agency agreement under which the charity or subsidiary sells

the goods as agent of the donor. If the goods are sold the proceeds, less any seller's commission, belong to the donor. The donor can then choose to Gift Aid their monetary proceeds.

There are three HMRC approved methods for operating the scheme (the *standard method*, method A and method B). HMRC provide detailed guidance in its *Chapter 3 Gift Aid guide* (available online).

The scheme is only suitable for personal goods donated by individuals. If goods belonging to businesses are sold, VAT may have to be charged on the sale.

Before the advent of s33c, the general approach was for the donor to be charged a seller's commission in order to make the agency sales activities a taxable business activity so as to obtain VAT recovery on associated costs. This seller's commission is standard-rated for VAT. However, now that a charitable hospice can reclaim its non-business VAT under s33c, not charging a donor commission may be a possibility, though it is not yet clear that HMRC would accept this. However, it would only be effective if the charity operates the scheme as opposed to a trading subsidiary.

Fundraising events

Supplies of all types of goods or services in connection with a qualifying fundraising event are VAT exempt, unless also zero-rated (for example printed programmes), in which case zero-rating takes priority. Exemption covers supplies at the event, for example admission or catering, and supplies in connection with the event, such as sponsorship and advertising in a programme. To be a qualifying fundraising event the event

must meet all five of the following conditions:

- The event must be organised by a charity, a wholly owned subsidiary of a charity whose profits from the event are payable to a charity, or a combination of charities and wholly owned charity subsidiaries
- Its primary purpose must be the raising of money
- It must be promoted as being primarily for the raising of money
- There must not be more than 15 events of the same kind in the same location in the body's financial year. However kinds of events whose aggregate gross takings at any location do not exceed £1,000 per week can be ignored when assessing the 15 limit.
- It must not include provision of:
 - A package of both travel and accommodation; or
 - bought-in accommodation; or
 - more than two nights' accommodation from a charity's own resources.

See challenge events below for where these conditions are not met

Challenge events

Where a sponsored event includes accommodation or is organised by a commercial event organiser, it does not qualify for the fundraising exemption. The options for such events (*challenge events*) are then:

- if you have no pre-existing agreement with either the donor or event organiser, and simply receive a donation from the participant or event organiser – this is an outside the scope of VAT donation in the charity's hands.

- If you market the event to your supporters and sell places as disclosed agent of an event organiser (disclosed agent means that participants know who the event organiser is and who they are ultimately contracting with), with the event organiser taking responsibility and liability for the event itself, you are seen as receiving a standard-rated commission of the difference between what the participant must pay before departure and what you pay to the event organiser. Any funds raised on top of this are outside the scope of VAT.
- If the charity or its subsidiary organises its own challenge event as principal, taking responsibility for the event and participants, or if it acts as undisclosed agent (so participants do not know who the organiser is), the event is likely to fall under the special VAT Tour Operators' Margin Scheme ('TOMS').

Renting property

By default supplies of leases and licences to occupy property are VAT exempt. However, a supplier can opt to tax a property, in which case that supplier's supplies of that property become VAT standard rated. But in some situations the supplier's option to tax is disapplied so it has no effect.

Disapplication If a hospice is renting property a landlord's option to tax can be *disapplied* on the basis of use for a charity's non-business activities and/or use as a residential hospice. However, it is not always advisable to disapply an option to tax, especially for a s33c eligible hospice that can claim for the VAT charged. You should check the rental agreement as in some situations it will be better not to disapply. If a hospice

has been disapplying an option to tax on rented property it may be better to cease to disapply.

Special types of property Supplies of certain types of property are always standard-rated, irrespective of any option to tax. These include the letting of car parks, catering facilities, lets for weddings and parties, goods storage facilities, sports facilities, hotel and holiday accommodation, caravan sites and camping facilities, though in each case there are exceptions and special situations.

Letting out conference facilities If the facility has not been opted to tax, HMRC accept the basic hire fee can be VAT exempt whilst any separate charges for catering are standard-rated (see *VAT Notice 709/3 Section 4.3*)

Sponsorship

Sponsorship is a term that covers a wide variety of situations. It is necessary to consider what if any benefits the sponsor obtains in return for their sponsorship payment:

Trivial benefits can be ignored HMRC accept trivial benefits include: giving a flag or sticker; naming the donor in a list of supporters in a programme or on a notice naming a building after the donor; and putting the donor's name on the back of a seat in a theatre

Advertising and promotion If the main benefit for the sponsor is advertising and promotion then by default the supply is standard-rated. However if the sponsor is a charity it is zero-rated, and if the sponsorship is of a qualifying fundraising event, it is VAT exempt.

Barter supplies If you supply goods or services to a sponsor and in return they provide 'free' goods or services, then this is seen as being two separate supplies with the consideration for each set off.

Split payment/donation HMRC accept that provided it is entirely separate from your sponsorship agreement, you are not required to account for VAT on any donation you might also receive from a sponsor. However, it must be clear that any benefits your sponsor receives are not conditional on the making of the donation or gift (*VAT Notice 701/41 Section 2.3*).

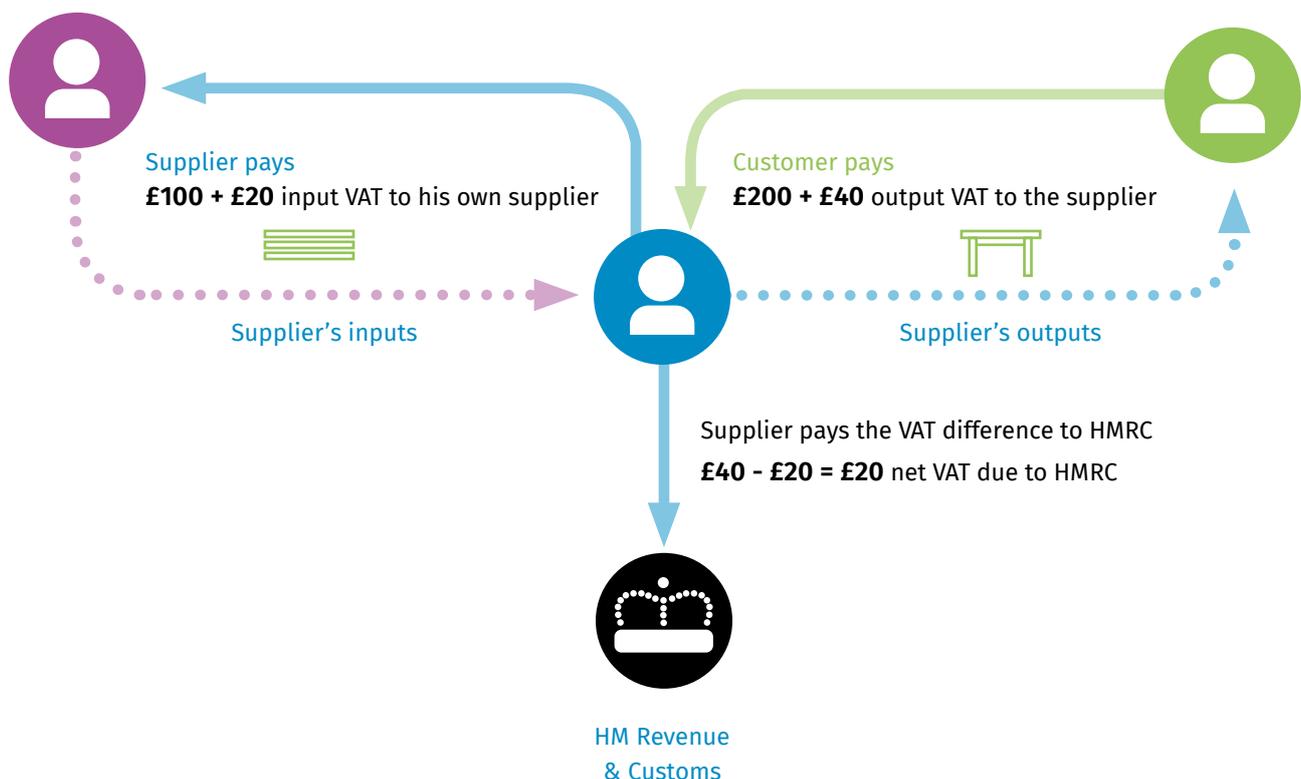
Appendix How VAT works

VAT is a type of sales tax that applies at a transaction level. When a transaction is subject to VAT (a *taxable supply*), the supplier adds VAT (at the appropriate percentage rate) to the selling price and charges this VAT to the customer. This is referred to as the supplier's *output VAT*. The supplier collects this output VAT from the customer and pays it over to HMRC.

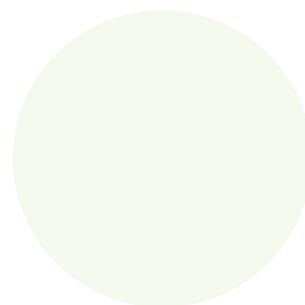
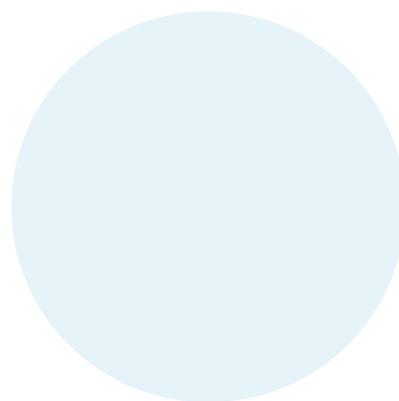
The supplier can recover from HMRC the VAT charged by its own suppliers on the purchases that it uses to make its taxable supplies. The VAT charged on purchases ('inputs') is referred to as the supplier's *input VAT*. The supplier has to pay HMRC the net amount, output VAT less input VAT. If input VAT exceeds output VAT, the supplier receives a VAT refund from HMRC.

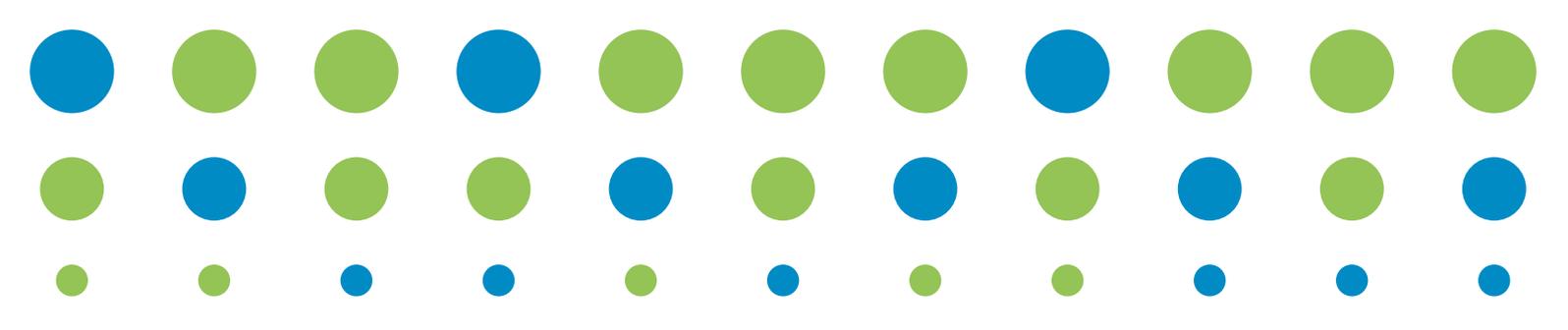
Example

A table manufacturer sells a table for £200+VAT but incurs costs of £100+VAT in creating the table:



A business must register for VAT and start charging VAT on its sales if the level of its taxable supplies goes over the VAT registration threshold (2015/16: £82,000). The business must register if total taxable supplies in the last 12 calendar months has exceeded the threshold or total taxable supplies in the next 30 days alone will do so. A business can also register voluntarily if it makes or intends to make any level of taxable supplies. However, some supplies are exempt from VAT (in particular public interest activities such as care, education, cultural services and sports) and some income (non-business income) is not subject to VAT, for example most grants and donations.





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