

Tips For Reducing VAT Costs

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Charities can be very conventional with their VAT accounting, often relying on HM Customs & Excise for advice - perhaps because it is free. Their guidance may be helpful but will always reflect Customs' wisdom. A more proactive approach to VAT could bring financial gain to charities, and this article highlights several areas worthy of review.

Transactions with business supporters

Charge VAT to businesses which can recover tax on their expenses

The amount of VAT recovered on a charity's overheads is influenced by the amount of VATable income received. If it is possible to charge VAT on income coming from VAT registered businesses that can recover the tax, the charity can generate more VATable income without cost and without causing expense to the givers. The charity can thus raise its level of VAT recovery.

Ensure the VAT liability on income is properly identified

Review income on a regular basis to see whether both standard and zero rated VATable income is identified to maximise the recovery of input VAT. Also consider whether corporate givers could change from making donations (which are outside the VAT net) to providing sponsorship (which is VATable). In this way a charity can benefit from an enhanced recovery of input VAT on its expenses. Besides, changing the transaction with the corporate giver from a donation to a business arrangement may be useful to the giver as the money will be sourced differently — in other words, not from a charitable donations budget which may already be strained.

Example: a charity received a significant part of its income from donations by local businesses but could not recover VAT on its overheads. The charity subsequently changed the donations to sponsorship and this enabled it to increase its recovery of VAT on

overheads. There was no VAT impact on those businesses that were giving money to the charity. Therefore, the charity had more money to use without having to increase its income.

Review VAT charged by suppliers

Suppliers may not know when to charge VAT

When this is the case, most suppliers play safe and apply VAT. I therefore suggest that charities take the initiative and regularly review VAT charged by suppliers.

Reducing VAT costs

The cost of making this check may be incidental to the VAT saving that could be made.

Take advantage of zero rated supplies

Make sure that all goods and services that qualify for zero rating are charged appropriately. For example, printed matter can be zero rated when supplied by a printer. Similarly, zero rating is available for advertising in newspapers and on radio.

Combine supplies to take advantage of zero rating

The printing of a booklet or leaflet is zero rated. However, a copywriter or public relations firm advising on the layout or content of, say, an annual report, would have to charge VAT on their services.

In this situation it is worth trying to get these professional services invoiced to the printer and asking him to make a single charge to the charity. This would mean that zero rate VAT can be applied to the whole cost, resulting in a reduced VAT charge. Alternatively, arrange for the adviser to get the printing done so that he or she may zero rate their supply.

Zero rating is not just available on advertising or printing but also on buildings being used for relevant residential or charitable purpose. In these instances, combining the supply can produce real savings through the recovery of input VAT on advisers' fees.

Use a trading company to make the combined supply

Some suppliers may not want to help by combining their services because of possible complications, for instance if something went wrong with the printing or copywriting. Charities can overcome this by using a trading company, if they have one, to purchase the separate elements and then make a single combined supply to the parent charity.

Example: a charity was to produce its annual report and decided to obtain separate design advice. The designer would be required to add VAT to fees charged. The charity entered into an agreement with its trading company for the production of 500 copies of the annual report for the charity. The designer and printer separately invoiced the trading company. The trading company recovered the VAT charged by the designer as it was attributable to the trading company's single zero rated supply to the charity of the finished annual report. Therefore, the charity's VAT cost was reduced.

Supplies made by a charity

Free supplies can enable VAT recovery on related overheads

Although supplies made by a charity may not result in an output VAT charge, they could enable input VAT, which is directly or indirectly attributable to this supply, to be recovered. For example, charities often produce leaflets or booklets to be given away. No VAT is due on these because the supply is zero rated but the charity will certainly incur VAT on some of the related overhead costs such as electricity and telephone bills. Part of this VAT should be recovered against the free supply.

All business activities, whether free or paid for, should be recognised and itemised

If the charity charges for products or services, even though the price may be subsidised through grant or donation income, full VAT recovery on all direct and indirect costs should be agreed with Customs & Excise. Therefore, charities should ensure that all expenditure relating to this income is identified for optimum VAT recovery.

Where charities supply free or subsidised goods or services, the means of recovering input VAT may be usefully reviewed. If a charity is using an income based method, it should ensure that there is scope to include the value of free or subsidised goods or services. Alternatively, consider a cost based method using appropriate cost centres which show the value of VAT attributable to VATable supplies. The method adopted should be agreed with Customs.

Example: a charity carried out research on social issues and published its findings in free and subsidised publications. It received approximately 10 per cent of its income from the publications and the remainder from grants and donations. Customs had stated that only 10 per cent of its input VAT was recoverable.

An analysis of its input VAT showed that approximately 50 per cent of its input VAT directly related to the publications. Customs conceded that this VAT was recoverable in full. Using a non-standard method the rate of input VAT recovery was increased to 78 per cent.

Use of trading company to recover vat on shared expenses

It may be appropriate for a trading subsidiary to purchase equipment used by it and the parent charity organisation. Frequently the trading company's profit is transferred to the parent organisation through a covenant, providing the charity with funds to pay for goods and services some of which may be shared with the trading company. This means that the charity may be incurring irrecoverable VAT costs.

However, if the shared goods and services were purchased by the trading company this VAT may be reclaimed, although it may be necessary to consider making an appropriate charge to the charity for the use of the equipment.

Additional Information

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