



ARTICLE NO: 2A

**CORPORATE OVERVIEW
AND SCRUTINY COMMITTEE**

MEMBERS UPDATE 2010/11

Article of:	Council Secretary and Solicitor
Issue 2:	September 2010
Relevant Portfolio Holder:	Councillor D.Westley
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SUBJECT: ANNUAL VAT REPORT

1.0 PURPOSE OF ARTICLE

- 1.1 To inform Members of developments and performance in relation to Value Added Tax (VAT).

2.0 BACKGROUND

- 2.1 The Accountancy Service Plan contains the following objectives for accounting for VAT:
- minimise the Council's VAT liabilities
 - raise the profile of VAT within the Authority
 - develop and improve VAT processes and procedures.
- 2.2 One of the means of achieving these objectives is the production of an Annual VAT Report for Members.

3.0 ACCOUNTING FOR VAT

- 3.1 The Council pays VAT to its suppliers for most of the goods and services procured. The Council also charges VAT for most goods and services provided to its customers for business reasons. Any VAT paid to suppliers is recovered from Her Majesty's Revenue and Customs (HMRC) and any VAT received on the Council's supplies is paid to HMRC. This is done by the completion of a monthly VAT Return.
- 3.2 Responsibility for the Council's VAT function is incorporated within a section of the Accountancy team, Officers aim to continually minimise the Council's VAT liabilities. This includes ensuring fines, interest, and assessments are minimised and VAT recovery is maximised. To achieve this, the team ensure that VAT is accounted for correctly throughout the Authority and that Officers are aware of relevant changes in VAT Regulations.

4.0 VAT MANAGEMENT AND PERFORMANCE

External Inspections

- 4.1 External auditors gave a clean bill of health on their last review of the Council's VAT account and systems. The review being September 2009

VAT Returns

- 4.2 The Council generally expends more on VAT than it collects from its own activities. This is because most of its own activities are not classed as being carried out for business purposes and VAT is, therefore, not applicable. As such, the monthly VAT Returns reclaim the net VAT from HMRC by the Council. During 2009/2010, the Council paid a total of £3,214,700 to suppliers and received a total of £495,820 VAT from its own customers. This resulted in a net total of £2,718,880 being reclaimed from Revenue and Customs. The average VAT return for 2009/2010 was £226,570 comprising, on average, £267,890 due from Revenue and Customs and £41,320 due to them. Table 1 shows how these values compare to the previous financial year of 2008/2009:

Table 1 - VAT Return Comparison: 2009/2010 to 2008/2009		
	2009/2010 £'000	2008/2009 £'000
Total VAT:		
Paid to Suppliers	3,214	3,496
Received from our own Customers	495	601
Reclaimed from Customs and Excise	2,719	2,895
Average Monthly VAT:		
Paid to Suppliers	267	291
Received from our own Customers	41	50
Reclaimed from Customs and Excise	226	241

VAT Penalties

- 4.3 If there are mistakes within the VAT return or if something is missed from it the Council is liable to fines, interest charges, and other financial penalties. A voluntary disclosure is declared when errors are above a threshold of £10,000. This limit has been increased by HMRC from £2,000 as from 1 July 2008. To date we have not been required to register a voluntary disclosure as the Council has not breached this threshold. As from 1 April 2009 a new penalty regime has been implemented by HMRC, this could have an impact on the Council due to the way that fines, interest charges and other penalties are to be calculated, as this could result in a greater percentage of fine being levied to the Council. However, currently this new regime has had no impact on the Council, this is due to no fines etc being imposed.

De Minimis Calculation (Partial Exemption)

- 4.4 Exempt activities for VAT purposes are defined in the VAT Act 1994 and cover 15 categories. Local Authorities can only reclaim VAT paid to their suppliers for its exempt activities providing that this is less than 5% of the total VAT paid to suppliers. For this Council, this is usually in the region of £160,000 per year. If this threshold is exceeded, the Council would be liable to pay the full value of its exempt VAT to Revenue and Customs, i.e. around £160,000.
- 4.5 HMRC had issued a moratorium on this position for the financial years 2007/08 and 2008/09. Representations had been made to HMRC so that they look upon this calculation on a national basis rather than by an individual Council perspective. The findings from HMRC are that the moratorium has ceased, with an amendment of Internal Recharges being removed from the calculation. The partial exemption calculation has been reintroduced from the 2009/10 financial year. Therefore if the limit of 5% was to be breached Vat repayment implications would follow. The Vat team will monitor this expenditure throughout the year to ensure

that the Council does not exceed the 5% margin. In previous years the percentage was not usually greater than 4%.

- 4.6 The Council will take specialist advice, if appropriate, when projects that may affect its vat position substantially are undertaken, for example in previous years, the new Office accommodation development. In addition such issues are raised with HMRC to inform them of the project and the proposed vat approach the Council is undertaking.

VAT Manual and Training

- 4.7 The Council has a VAT manual, which is available on the Council's intranet, updated as at September 2010. VAT training for some key officers has been undertaken on a one to one basis. Details on vat issues are also included in the Finance Budget Manual which is published on the Intranet.

Change in VAT rate

- 4.8 The Government changed the VAT rate back to 17.5% from 15% effective from 1st January 2010. The budget speech in June 2010 announced that the VAT rate will increase to 20% as from 4th January 2011. From a fiscal point of view, the timing maybe the intention to contribute to the flurry of activity in the Christmas period and in the sales period that follows. The 4th January is the back to work Tuesday after the bank holiday at the start of the year. As a result of this measure it meant that some of the financial systems had to be altered to accommodate this rate change back to 17.5%. This system alteration was achieved with no operational issues being encountered. The same system procedures will be followed in order to implement the rate change to 20% in January, and no problems are envisaged at this stage.

Overall Performance

- 4.9 Management of the VAT function within the Authority is a well established process. The monthly vat return to HMRC is always completed on time. HMRC inspections in previous years have been undertaken with the result that the Council's processes and procedures have been given a clean bill of health. The Authority is part of a Lancashire wide Council networking group. Whereby, Vat topics and issues of a common interest can be raised. This promotes good practice across the Councils and the latest Vat topics are discussed in order to maximise performance.

5.0 RECENT VAT DEVELOPMENTS

- 5.1 The Vat Team continually review developments in the sector in order to identify any implications for the Council. Some of the topics are highlighted below.

VAT on Off-Street Car Parking

- 5.2 The local authority can provide off-street parking where for the purpose of relieving or preventing congestion of traffic it appears to be necessary to provide within their area suitable parking places for vehicles. The output Vat levied for this function has been subject to legal proceedings by a group of Councils, commonly referred to as the Isle of Wight case. It is a complex and technical issue, which may result in the Council not levying output Vat for this service area. This may mean that the amount of Vat levied to date by the Council may be repaid to the Authority at some future date. However, developments are indicating that this is becoming a more unlikely outcome. A protective claim has been submitted to HMRC to safeguard the Council's Vat position, the Vat sum involved to date is £1,011,481.
- 5.3 This case is still ongoing and we are waiting for High Court and the European Courts of Justice rulings. Once the High Court issue a ruling, this will be analysed and any financial implications will then be taken into account.

Leisure Claim – January 1990 to March 1994

- 5.4 The Council made a VAT claim to HMRC for a sum in the region of £600,000 plus interest. This claim is in respect of Leisure Services and has been able to be made as a result of a legal case referred to as the 'Fleming Case.' This allows all organisations to submit VAT claims to HMRC back to when Vat was introduced to the U.K. This is as a result of a court ruling that deemed that HMRC did not implement changes into Vat rules in the correct manner. The Council has received this claim from HMRC in September 2009, the amount being £886,000 for the claim and interest.
- 5.5 The details of the actual claim are a little technical and complex however, it had allowed us to submit the claim, as detailed above with a favourable outcome for the Council.

Sports Tuition Claim

- 5.6 The Council has submitted a further VAT claim to HMRC under the 'Fleming Case' for the sum in the region of £50,000 plus interest. The Council are awaiting the outcome of this claim, we will provide an update on this in next year's report.

6.0 SUSTAINABILITY IMPLICATIONS/COMMUNITY STRATEGY

- 6.1 There are no significant sustainability impacts nor Crime and Disorder or Community Strategy implications associated with this Update.

7.0 RISK ASSESSMENT

7.1 The formal reporting of performance on VAT is part of the overall management and control framework that is designed to minimise the financial risks facing the Council. Furthermore, the monitoring of performance during the year minimises the chance of breaching the de minimis 5% threshold.

8.0 SUMMARY

8.1 Value Added Tax is a technical and complex area and mistakes can be costly to the Council. The VAT Team strive to achieve the continuous aim of ensuring that the Council's VAT liabilities are minimised and VAT recovery is maximised by developing and improving VAT processes and procedures.

8.2 The possibility of recovering VAT in relation to car parking and sport tuition claims, would, if successful, provide a significant benefit for the Council in these difficult financial times.

Background Documents:

There are no background documents (as defined in Section 100D(5) of the Local Government Act 1972) to this Article.

Equality Impact Assessment

There is no evidence from an initial assessment of an adverse impact on equality in relation to the equality target groups.

Appendices:

None