

Client Newsletter – October 2005

Management fee – taxable supply?

It was Benjamin Franklin, the American Statesman, Scientist, Philosopher, Printer, Writer and Inventor who said “In this world nothing is certain but death and taxes”.

Unfortunately – or fortunately, perhaps - for Benjamin, he died in April 1790 and therefore he never had to deal with either VAT or HM Revenue & Customs, otherwise his view might well have been different.

We always look for – and should be entitled to expect – certainty in our dealings with the tax authorities, as it enables us to make plans for changes in our business (and non-business!) activities with some degree of financial certainty and enables decisions to be made as to the most cost-efficient ways of structuring our affairs. But with the tax authorities constantly probing for ways to extract the maximum revenue from taxpayers, they will inevitably resort to pushing interpretative boundaries to the extreme. One example of this is the way that they treat local authority leisure centres which are outsourced to a Trust.

Many local authorities are now considering putting the operation of their leisure centres in a Trust and in establishing the financial viability of such change will have to examine, amongst many other factors, the VAT status of the Trust. Inevitably a Trust will have limited VAT recovery (as it will make mainly exempt supplies) and one of the ways it improves its VAT recovery rate is through making a taxable supply of management charges to the local authority it has a contract with, thus increasing its taxable percentage within its partial exemption calculation. Until recently Customs had rarely questioned this treatment. Until, that is, someone spotted that if the management charge were excluded from the Trust’s partial exemption calculation, VAT recovery would drop significantly.

As a result, Customs changed their position. Note: NO change in law, NO consultation with interested parties, NO Business Brief or other communication, NO advance warning for those authorities part-way through the outsourcing process.....

We understand that Customs have now reverted to their original position that the management charge is a legitimate part of a Trust’s business – *it always was!* – and may be included in the partial exemption numerator. The fact that they have given up on this particular line of attack, however, is no excuse for trying it on in the first place. If taxpayers are expected to pay a fair amount of tax, then they are entitled to expect fair and consistent treatment from the tax authorities.

On a more general note, Customs continue to examine the payments made by local authorities to Trusts – sometimes referred to as deficit funding, or management fee - to ensure that they are payments for services and not grants. Clearly it is in the interests of the Trust that the payment should be in respect of a taxable supply, however we recommend that you should always seek professional advice on the structure of these arrangements to achieve the optimum VAT position.

If you would like to discuss any of the issues above, please write, e-mail or call us. Our contact details are below.

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