



**HMT
Policy Paper**

**VAT and the Public Sector:
Reform to VAT Refund Rules**

Submission from ICAS

16 November 2020

Introduction

1. The Institute of Chartered Accountants of Scotland ('ICAS') is the world's oldest professional body of accountants and we represent over 22,000 members working across the UK and internationally. Our members work in all fields, predominantly across the private and not for profit sectors.
2. The ICAS Tax Board, with its five technical Committees, is responsible for putting forward the views of the ICAS tax community, which consists of Chartered Accountants and ICAS Tax Professionals working across the UK and beyond, and it does this with the active input and support of over 60 board and committee members.
3. ICAS has a public interest remit, a duty to act not solely for its members but for the wider good. From a public interest perspective, our role is to share insights from ICAS members into the many complex issues and decisions involved in tax and financial system design, and to point out operational practicalities.

General comments

4. ICAS welcomes the opportunity to respond to this policy paper '[VAT and the Public Sector: Reform to VAT Refund Rules](#)' issued by HM Treasury on 27 August 2020.
5. ICAS welcomes HMT's intention to reform Section 41 of the UK VAT Act (1994) ('Section 41'). Our experience of the current rules is that they are far too complex, and this complexity is exacerbated by frequent change in HMRC's application of these rules. It is not a good use of taxpayers' money for HMRC and bodies providing public services to be devoting time and incurring costs trying to get round problems caused by the fact that the underlying VAT regime for the public sector is currently unfit for purpose.
6. ICAS sees merit in the preferred option of implementing a full refund option on VAT incurred on all goods and services incurred during the course of non-business activities for organisations falling within the scope of Section 41. This brings the VAT treatment for Section 41 more closely into line with the existing VAT treatment for Section 33 which governs local authorities, which accords with the previous representations which ICAS has made on improving the VAT treatment of the public sector.
7. Whilst this change is a move to increase fiscal neutrality within the public sector by greater alignment of treatment of bodies covered by Section 41 and Section 33, it does not arrive at full neutrality. Currently Section 33 bodies benefit from generous partial exemption treatment and it is not covered in 'VAT and the Public Sector: Reform to VAT Refund Rules' whether this is to be extended to Section 41 bodies also. ICAS is aware of how burdensomely complex partial exemption is for NHS bodies and would be glad to see that burden relieved. On a wider level, the sector which delivers public services contains more than merely Section 33 and Section 41 bodies. As it is ultimately desirable that there should be fiscal neutrality for organisations delivering the same services to the same end users, ICAS would like to see any change implemented to take due regard of where distortions could be displaced to other parts of the public sector.
8. The transition of systems required to allow Section 41 bodies to adjust for the implementation of the full refund model will be substantial and significant time must be allowed for changes. In addition, access to very clear guidance and support from HMRC will be essential to a clean delivery of the change. ICAS considers it very important to have a dedicated HMRC team with sufficient specialist resource to deal with public sector issues which is open to discussion with public sector bodies and their external advisers.
9. The comments in 5.11 of 'VAT and the Public Sector: Reform to VAT Refund Rules' show that change will be delayed to give due consideration to the burden of work landing on the NHS and related bodies due to the ongoing COVID-19 crisis. During the period that the current rules continue, ICAS would encourage HMRC to take the most straightforward and consistent approach to their application. This step alone would lighten the time burden of dealing with the rules and reduce confusion.