



ICAEW TAX REPRESENTATION

REVIEW OF EXISTING VAT LEGISLATION ON PUBLIC BODIES AND TAX EXEMPTIONS IN THE PUBLIC INTEREST

ICAEW welcomes the opportunity to comment on the consultation paper [*Review of existing VAT legislation on public bodies and tax exemptions in the public interest*](#) published by the European Commission on 14 October 2013.

ICAEW is listed in the EU Transparency Register (ID number: 7719382720-34).

This response of 24 April 2014 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

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MAJOR POINTS

1. The main problem with the existing VAT treatment of supplies by public bodies is the distortion of competition and complexity caused by the same supply being subject to different rates of VAT depending upon the nature of the body making the supply.
2. We believe that sectorial reform is appropriate in any case where a supply can be made by more than one type of organisation and the VAT liability differs according to who makes the supply.
3. We are fundamentally opposed to the concept of an option to tax anything. An option to tax inevitably leads to increased complexity, lack of clarity and a distortion of competition between those businesses or countries that have elected to opt and those that have not.
4. Public bodies should continue to be permitted to claim VAT relating to their non-business activities through the normal VAT return, as though it were normal input tax. It would create a considerable administrative burden for such bodies if such VAT had to be separately identified from normal input tax for VAT return declaration purposes.

RESPONSES TO SPECIFIC QUESTIONS

Q1: General evaluation of the current rules

What is your evaluation of the current VAT regime as regards the public sector (including special rules for public bodies, Article 13, and tax exemptions in the public interest, Article 132-134 of the VAT Directive)?

What are in your opinion the main problems of the current rules?

5. The main problem is the distortion of competition and complexity caused by the same supply being subject to different rates of VAT depending upon the nature of the body making the supply.
6. Inconsistency of VAT treatment between Member States can also cause difficulties, particularly when engaging in cross-border activities.

Are there any distortions of competition (output and input side)? If so, how and in which sector do they occur?

7. Yes. We have included examples below.

Is the complexity of the current rules and the lack of harmonisation causing problems?

Please give specific examples.

What is their impact on compliance costs?

8. Existing problems are likely to become considerably worse when the changes to the place of supply rules for B2C electronic services are introduced on 1 January 2015.
9. Where a supply is deemed to be an electronic service, it will become subject to the VAT laws of the Member State of consumption. Businesses will therefore need to become familiar with the local laws if they wish to compete in a particular Member State.
10. It is envisaged that there will be services, particularly in the education sector, where local rules will vary. This could be due to local differences in interpretation of the education exemptions, local decisions regarding the types of organisation that are included within the definition of a

public body, or differences of opinion as to whether a particular supply is electronic or otherwise.

11. The time and cost of obtaining the information necessary to ensure compliance with the VAT laws of other Member States is likely to be considerable.
12. The requirement of some Member States to provide invoices to domestic consumers is expected to cause considerable problems, especially to small businesses. These problems are compounded by the shortage or lack of availability of information relating to some Member States. If computerised systems are to be adapted in time to produce invoices from 1 January 2015, the invoicing requirements need to be known now.

Are the problems identified only of a national nature or do they constitute an obstacle to the smooth functioning of the Internal Market?

13. The requirement for businesses, particularly small businesses, to familiarise themselves with the VAT regulations applying in each Member State will undoubtedly create a barrier to international trade. As such, we expect that the new place of supply rules combined with the local interpretation of exemptions will almost certainly constitute an obstacle to the smooth functioning of the Internal Market.

If you are an entrepreneur how do the current rules affect your business?

14. Not applicable.

Q2: Distortion of competition clause:

Do you think the distortion of competition clause pursuant to the second subparagraph of Article 13 (1) of the VAT Directive and the existing case law from the Court of Justice of the European Union in this respect have been efficient enough in preventing distortions of competition between public and private providers on the output side?

15. No. An obvious example is charges for car parking.
16. This can be illustrated by an example of parking bays alongside main roads in town centres, where some bays are operated by the local authority and others are operated by private operators. The local authority bays are treated as outside the scope of VAT whereas the privately operated bays are standard rated. This results in two identical car parking spaces within a few metres of each other having different VAT liabilities.

Does the national legislation of your country provide for a legal mechanism according to which a private entrepreneur who is experiencing unfair competition from a public sector body could formally raise this issue with the tax authorities or the courts?

17. The Isle of Wight car parking case indicated that the burden of proof lies with HMRC to show that a significant distortion of competition exists. A private entrepreneur would presumably need to persuade HMRC to take appropriate action if he considered that distortion existed.

Q3: Reform measures:

What are your views on the different reform options or reform measures mentioned in this document (including a possible sectorial reform); do you have a preference for any particular option and any particular variant mentioned in relation to the different options and why?

1) Full taxation of public bodies and activities in the public interest (see point 5.1.)

18. It is unlikely that this option would be politically achievable.

2) Full compensation of input VAT ("Refund System") at EU level (see point 5.2.)

19. This option is the closest to that currently operated in the UK. It reduces the costs incurred by local authorities in carrying out their statutory duties, but also arguably gives them an unfair advantage for some services that compete against the private sector.

3) Deletion of special rules relating to public bodies (Article 13 of the VAT Directive), while keeping all or most of the current exemptions in the public interest (see point 5.3.)

20. This option has a distinct advantage, in that the same supplies would have the same VAT treatment regardless of the supplier. Coupled with consistent input VAT recovery rules, this would achieve the consistent and fair treatment.

21. As suggested in the consultation paper, the list of supplies that can currently be treated as exempt would need to be reviewed and common treatment applied to all providers of the affected supplies.

4) Sectorial reform (see point 5.4.)

22. Reform is required in some sectors to eliminate as far as possible the distortion of competition that currently occurs.

5) Possible (additional) selective amendments of the current rules as described under point 5.5.

23. We support the suggestion that the VAT liability of a supply should be determined by the nature of the supply and not the nature of the organisation that makes the supply.

Is there any option which should be excluded and why?

24. Option 1, the full taxation model, should be excluded, as there would be little, if any, chance of achieving political agreement to such a radical change.

Do you have any additional ideas or proposals?

25. In practice, the most likely outcome would appear to be a mixture of the suggested models. Any final version should aim to make compliance as simple as possible and minimise distortion of competition.

Q4: Sectorial reform:

In case a sectorial reform would be the way forward, Copenhagen Economics has modelled the sectors postal services, broadcasting, waste management and sewage. Other sectors such as air traffic control, access to roads and parking areas could be potential candidates as well.

Do you agree with this list?

26. We believe that sectorial reform is appropriate in any case where a supply can be made by more than one type of organisation and the VAT liability differs according to who makes the supply. We therefore agree with this list, but think that there are other sectors that should be added.

Which other sectors should in your view be selected for such a review? Why?

- 27.** Another sector that we believe should be selected for review is the higher education and vocational training sector, where a number of inconsistencies have been identified.
- 28.** We are concerned that similar courses leading to similar qualifications can be treated differently for VAT purposes, depending upon the organisation that is making the supply and, in some cases, the status of the person receiving the training.
- 29.** For example, we are concerned that restricting the exemption for higher education to degree courses would create a distortion of competition with similar professional and vocational qualifications that provide greater access to the professions and that are becoming increasingly available to school leavers as an alternative to a degree.
- 30.** We are therefore of the opinion that the exemption should include services provided by all providers of higher education that lead to a degree, professional qualification and vocational qualification.
- 31.** A provider of higher education could be defined as an institution that provides education, training or examinations leading to one or more professional qualifications or vocational qualifications. A list of the qualifications for this purpose could be separately defined and updated in secondary or tertiary legislation.
- 32.** However, we suggest that VAT liability should be determined by the qualification being sought, regardless of the status of the body that was providing the training. The exemption should cover all charges for higher education services including training and examinations.
- 33.** Consequently, there would be no need for the concept of an eligible body. This would provide simplification and remove the distortion of competition, so that all suppliers of education and vocational training would be treated equally.
- 34.** Similarly, we see no requirement for all supplies by a particular body to be treated as exempt or otherwise.
- 35.** UK VAT legislation currently requires supplies made to an eligible body to be treated as exempt. This could be amended by applying the exemption to supplies made in relation to an eligible qualification, such as marking fees for examinations.
- 36.** The UK imposes a restriction that all supplies by a recognised organisation have to be treated as exempt. Articles 133 and 134 of The Principal VAT Directive provide the restrictions under which a Member State may allow organisations to treat their supplies as exempt. Those restrictions do not include a requirement that all supplies by a recognised organisation have to be treated as exempt. Consequently, we see no legal reason why such a restriction should be imposed.
- 37.** Under the current legislation, a good example of variation according to the status of the person receiving the training is where two students sit the same examination to obtain the same professional qualification. A student receiving vocational training from his employer can benefit from the vocational training exemption. However, a student sitting the same examination independently, and possibly unemployed, does not benefit from this exemption and so has to pay VAT on the examination fee.
- 38.** A training course may be jointly run by two organisations, only one of which is an eligible body for the purposes of VAT exemption. In this example, the VAT liability of the training fee will vary, as a student registering with the eligible body will receive his training exempt from VAT, but a student registering with the other body will have to pay VAT.

Q5: Option to tax:

Do you think that an option to tax as regards tax exempt activities either by taxable persons or Member States should be considered?

- 39.** We are fundamentally opposed to the concept of an option to tax anything. An option to tax inevitably leads to increased complexity, lack of clarity and a distortion of competition between those businesses or countries that have elected to opt and those that have not.
- 40.** In many cases, it would be unclear to recipients of supplies whether or not the supplier, or country, had opted to tax the supply in question and to the validity of the VAT that they were being charged and asked to pay.
- 41.** It is an administrative burden for both the businesses making an option to tax and their tax authorities to maintain records of the options that have been made. This is particularly burdensome and problematic where the option extends for a significantly longer period than the normal time limits for retention of records.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx)

APPENDIX 2

IDENTIFICATION OF THE STAKEHOLDER

☐ **You are included in one of the following groups:**

Others: Professional accountancy body

☐ **Name of your organisation/ entity/ company**

The Institute of Chartered Accountants in England and Wales

☐ **Country of domicile**

United Kingdom

☐ **Brief description of your activity or your sector**

Professional accountancy body – see page 2 above

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☐ **Do you confirm your agreement to have your response to the consultation published along with other responses?**

Yes

☐ **Do you agree to the publication of your personal data?**

Yes