

2 June 2011

**Item 3**

**Possible EU proposals on VAT and public authorities**

**Purpose of report**

For discussion / direction.

**Summary**

The report highlights the need for early LGA action ahead of any EU proposals in 2012 to reform the VAT treatment of public bodies.

**Recommendations**

Members are asked to discuss the issue, consider the key messages (paragraph 9) and to agree next steps (paragraphs 11-12).

**Action**

Officers to progress as appropriate.

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## **Possible EU proposals on VAT and public authorities**

### **Background**

1. The European Commission has launched a major review of the current VAT system as applied across the EU. From an EU perspective, the system was developed over 40 years ago and many complexities have built up over the years including a patchwork of exemptions and different VAT rates.
2. The EU's aim is to simplify the VAT rules by more closely aligning national VAT regimes with each other.
3. As part of the review the Commission has announced it may bring forward specific proposals in 2012 on the VAT treatment of public bodies. This is the aspect of the review which has the potential to impact upon local authorities.
4. Different EU countries currently treat VAT costs incurred by public bodies in different ways. In the UK for example local authorities can normally reclaim from government (HMRC) each month the VAT they pay when *purchasing* goods and services: anything from office supplies to major construction contracts.
5. The *provision* of certain public services by local authorities is subject to different VAT rules in different EU countries. For example the provision of car parks by local authorities has different VAT treatment across the EU. Where VAT is charged this raises the cost of the service for the customer.
6. Local authorities are also increasingly providing public services in the same market as the private sector e.g. crèche services, adult education and training, sports facilities, car parks, letting of business units. This creates additional VAT complexities and, from an EU perspective, the possible distortions of competition. (The provision of statutory public service functions such as education or social services are outside the scope of VAT by virtue of them not being considered economic activities).
7. The EU has not yet developed the details of what might be proposed in 2012 as regards public bodies and VAT. The impact on local authorities is therefore currently unknown. Any proposals have the potential, however, to diminish local authorities' ability to reclaim VAT, perhaps particularly in relation to their services in the same market as private sector providers.

### **Key messages**

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8. Given the potential importance of the issue, the LGA would propose making some early representations to the EU.
9. The UK Local Authority VAT group brings together VAT managers from local authorities. They have submitted a response to the EU which makes a strong case for maintaining the status quo as regards the VAT treatment of public authorities. Their paper contains the following messages which members are asked to consider:
  - 9.1 VAT should not be a financial burden on public bodies undertaking their public service functions. Any future EU proposals affecting public bodies should not diminish local authorities' ability to reclaim VAT.
  - 9.2 The ability for local authorities to reclaim VAT stops it falling as a cost passed onto the tax payer in the form of increased council tax.
  - 9.3 Any moves towards a common VAT regime for public bodies must meet the LGA's objectives to reduce administrative burdens on local authorities; promote efficient use of public resources; and provide financial flexibilities at the local level.
  - 9.4 Key public service activities must remain free from VAT at the point of delivery. The state should not levy VAT on public services as they are already funded through taxation.
10. The full response of the UK Local Authority VAT group will be made available at the Board meeting.

**Next steps**

11. Consideration of the above key messages will provide LGA with a mandate to engage with Whitehall and the European Institutions on this topic to set down some early markers ahead of any potential proposals in 2012.
12. This is a potentially complex and technical topic. A full report can be brought to the board in future as and when the EU begins to define the scope of its proposals, and more is known about their potential impact on local authorities.