FOR PUBLICATION

QUEEN'S PARK SPORTS CENTRE – VAT OPTION TO TAX

MEETING: CABINET

DATE: 24 MARCH 2015

REPORT BY: CHIEF FINANCE OFFICER

KEY DECISION REF: 508

BACKGROUND PAPERS: NONE

FOR PUBLICATION

1.0 PURPOSE OF REPORT

1.1 To consider 'opting to tax' the new Queen's Park Sports Centre

2.0 RECOMMENDATIONS

2.1 That the Cabinet agrees in principle to opt to tax the new Queen's Park Sport Centre with effect from 31 March 2015.

2.2 The Cabinet delegates the final decision of whether to register the option with HMRC to the Chief Finance Officer in consultation with the Leader of the Council.

3.0 BACKGROUND

3.1 Local Authorities, in common with many other commercial organisations, have a range of activities which come within the scope of V.A.T. Some of these activities are 'taxable' and some are 'exempt' for VAT purposes. The amount of V.A.T. payable in respect of exempt activities must not exceed 5% of total tax. If the 5% limit is exceeded then the whole of the exempt VAT becomes irrecoverable, not just the excess amount. The Council's current level of exempt VAT is approximately £200,000 so it is important that all reasonable measures are taken to ensure that the 5% limit is not exceeded.

3.2 With effect from April 1989, suppliers engaged in land and property transaction are given the ability to elect whether or not to charge V.A.T. on the supplies they make i.e. they can 'opt to tax' the premises concerned. Once the decision to 'opt to tax' is taken, it <u>cannot be revoked for a period of twenty years</u>, except on the sale of the property. The Council's policy is to 'opt to tax' all new commercial and industrial schemes and to keep under review other property in order to maximise V.A.T. recovery and prevent the 5% limit being exceeded.

3.3 By 'opting to tax' a property it means that VAT will have to be added to any rent or other associated charges made to occupiers of the building. The affect of the option for each party to the arrangement are:

a) The landlord/owner will be able to treat more of the VAT incurred on providing the premises as a 'standard rate supply' and, therefore, recover the VAT it incurs from the Revenue. This also has the advantage of increasing the standard rated proportion of input tax and thereby reducing the exempt proportion.

b) The occupier will be charged an amount plus VAT for using the premises. If the occupier is VAT registered they will usually be able to recover the VAT from the HMRC. Private individuals, charities, exempt businesses, etc, however, may not be able the recover the VAT element of the rent and instead it becomes a true expense to them.

Once exercised, the option to tax must be notified to the Revenue within 30 days in order to be valid.

4.0 THE NEW QUEEN'S PARK SPORTS CENTRE

4.1 Sports Centres generally create exempt VAT issues because of the level of income they generate from exempt activities such as coaching fees and hiring facilities. In the case of the new QPSC, the joint use arrangement with the College introduces further complications for the Council as:

- We have been advised that the income from the College is exempt from VAT, this is positive because it enables the Council to retain all of the income, however, it provides a risk to the partial exemption position. The option to tax therefore enables us to reduce exempt income in a different area and help with the overall exempt use percentage. We would however only want to do this is absolutely necessary.

- But, by increasing the exempt income at the Centre this increases the amount of expenditure on construction and running costs which must then score against the 5% exempt recovery limit each year.

4.2 The VAT planning work on the project to date has suggested that the Council could treat the College's use as exempt and avoid any penalties under the 5% limit regulation by taking advantage of a special exemption for one-off projects, whereby a seven year average exempt percentage can be used instead of the percentage calculated for each year in isolation. Recent updates to the VAT recovery calculations, however, are suggesting that achieving the seven year average could be tight. One way of helping to relieve some of the pressure on the VAT recovery limits could be to opt to tax the new QPSC. The downside of this approach is that the charges made to customers for room hires etc., particularly "series of lets", would then be subject to VAT. The Council would then have the option of either passing on the additional VAT cost to customers by adding the VAT to current charges or maintaining the current charges and paying over the VAT element from its current income. Coaching fees are unaffected by the option to tax and will remain as exempt income. Given that construction work commenced in this financial year it is important that any decision to opt to tax is taken before the 31st March 2015.

4.3 Further work is currently being undertaken to ensure that the seven year average calculation is robust. Unfortunately this work is still taking place and is not likely to be completed by the date of the Cabinet meeting. It is, therefore, recommended that the Cabinet approve in principle the option to tax but delegate the final decision to the Chief Finance Officer in consultation with the Leader of the Council.

4.4 Opting to tax the new QPSC will bring it into line with the Staveley Healthy Living Centre and allow a common pricing structure to be maintained.

5 CORPORATE ISSUES

5.1 Financial – the financial issues are covered above.

5.2 Legal Issues – the 'option to tax' arrangements are covered by The VAT Act 1994 Schedule 10.

5.3 Risk Management – the major risk relates to not being able to recover routine and exempt VAT and the exempt VAT on the QPSC construction costs in 2014/15 and 2015/16 (£1.0 to £1.5m in each year). The risk analysis is shown in Appendix 1.

5.4 Equalities – there are no equalities implications.

6.0 RECOMMENDATIONS

6.1 That the Cabinet agrees in principle to opt to tax the new Queens Park Sport Centre with effect from 31 March 2015.

6.2 The Cabinet delegates the final decision of whether to register the option with HMRC to the Chief Finance Officer in consultation with the Leader of the Council.

7.0 REASON FOR RECOMMENDATIONS

7.1 To protect the Council's exempt VAT recovery position.

BARRY DAWSON
CHIEF FINANCE OFFICER

Officer recommendation supported.

Signed John Burton

Executive Member

Date 20.3.2015

Consultee Executive Member/Support Member comments (if applicable)/declaration of interests:

APPENDIX 1 - RISK MANAGEMENT

Cause	Effect	Actions undertaken to mitigate the risk	Current Risk Rating – Likelihood / Impact. Rating	Further Action Required	Target Risk Rating – Likelihood / Impact Date by	Risk Lead
The proportion of QPSC income that relates to ‘exempt’ activities causes VAT on construction costs to be allocated to ‘exempt’ and to score against the 5% limit.	Increases the amount of input VAT allocated to ‘exempt’. A risk that the 5% ‘exempt’ limit is exceeded and all exempt input VAT in the year becomes unrecoverable (£0.2m revenue and £0.4m capital in 2014/15 and 2015/16).	Regular monitoring and modelling of options.	Likely / Very High 4 x 5 = 20 Red	External expert VAT planning advice. Modelling seven year average exempt rates. Possibility of exempt activities being reclassified as zero rated or converted to standard rated by opting to tax.	Unlikely / Very High 2 x 5 = 10 Amber By 31/03/15	CFO