



Sue Ryder Briefing

Irrecoverable VAT: The Barrier to the Big Society

Executive Summary

Sue Ryder is a charitable provider of health and social care services. As part of the government's Big Society agenda we expect to see more services transferred from the NHS to charities such as Sue Ryder.

The problem: Charities are faced with a problem of irrecoverable VAT. We are not able to reclaim VAT that we pay on certain supplies. This year we estimate we will be unable to recover £1m in VAT. As more services are transferred to us from the NHS, this figure will rise. In order to stop standards from falling, we will have to inject charitable funds. These will ultimately end up with the Treasury.

The solution: Due to the complex nature of VAT Law, we believe a solution enabling us to reclaim all VAT incurred would require significant legislation change and would involve the Treasury losing out on substantial funds. We understand that in the current climate such a solution is not feasible. However, we believe we have devised a partial solution that will stop the problem from worsening without the Treasury losing funds they already collect. This would only require a minor legislation change or clarification.

The NHS is able to recover VAT on certain supplies that charities are not. The NHS VAT recovery rules are written into Section 41 of the 1994 VAT Act. We believe that there should be a level playing field in this area between charities providing healthcare services and the NHS. In order to achieve this, charitable providers of healthcare services should be included in Section 41.

The Pledge: We would like you to pledge your support to our campaign. The government has committed to make it easier for charities wanting to provide public services. Together we will ensure that the charities and the people in need of our care are receiving the best settlement.

This document will detail how irrecoverable VAT is incurred in this area and how it acts as a barrier to charities wanting to take on the delivery of healthcare



services. We have discovered a simple solution to this problem as detailed below.

1. Overview

Sue Ryder is a charitable provider of health and social care services. We provide care from our hospices, neurological care centres and in people's own homes and communities. We are contracted by PCTs and local authorities to provide our services. Charitable funds contribute towards the delivery of care; particularly our hospice provision where we provide over half of the funding for the services available.

In line with the government's plans for the NHS and the Big Society initiative, more public services will be passed from the NHS to charitable providers. There is evidence of this already; a PCT has chosen Sue Ryder as the preferred provider of all palliative care in their area. As part of the agreement we will take over the management and provision of care from an NHS hospice.

This is an innovative project and is a first for the sector. We estimate that we will be unable to recover roughly £40,000 in VAT per year from non business activities for the hospice alone.

Sue Ryder's strategy outlines our desire to manage health services that are transferred from the NHS to the charity sector in the coming years. We plan to spend a combination of fees received from the NHS and charitable funds raised to provide innovative, efficient and quality services to individuals in need of care.

Current legislation allows the NHS to recover VAT on some non-business activities. The current rules relating to VAT recovery for charities are extremely complex and we are unable to recover VAT in these areas. For example, the NHS would be able to recover around 55% of the £40,000 of irrecoverable VAT we would experience from the hospice detailed above.

2. Current law relating to VAT recovery

Under VAT law, charities do not have the ability to recover VAT incurred in the course of undertaking non business activities. The term non business typically covers goods or services provided for no consideration (where no payment is made by the recipient of the service) or those where donations or grant



income are the principle source of funding. In practical terms this leaves charities with substantial VAT costs.

In contrast, where NHS Trusts and Primary Care Trusts undertake non-business activities, they are able to recover VAT on certain expenses under what is commonly referred to as the 'contracted out services provisions'. The legislation supporting this is contained within Section 41(3) of the 1994 VAT Act. This allows the NHS and Primary Care Trusts to recover any VAT incurred in relation to purchases of services which could have been undertaken in house. A list of the eligible services is published periodically in the London, Edinburgh and Belfast Gazettes. For example, relevant services include catering, laundry, estate management, waste disposal etc. For a more comprehensive list please see appendix one.

Local authorities face even less restrictions. They are able to recover all VAT they incur as a result of non-business activities. The legislation to support this is contained within section 33 of the VAT Act.

3. The VAT problem

As explained above, charities do not have access to the same VAT recovery enjoyed by the NHS despite often providing the same services as them. Consequently, should a hospice or nursing home be transferred from a PCT to a charity, a 'hidden' VAT cost immediately arises for the charity.

If the grant funding offered to the charity for taking over the service is the same as that previously offered to the PCT, it is impossible for the charity to maintain existing service levels without using funds raised through charitable donations. These charitable funds used to pay the VAT will ultimately end up with the Treasury.

When donors give money to Sue Ryder they do so to help us provide care for people with long term or end of life conditions. We are concerned that some of the funds donated will instead be going directly to the Treasury in VAT; this is not what they expect when they donate to the charity. We do not want this situation to further worsen as we take on more care provision from the NHS.

If a VAT recovery mechanism is not introduced it could cause financial inefficiencies within the sector. If non business services are provided 'in house'



there will be little or no VAT cost, but if they are outsourced it will result in paying the providers of these services VAT that is then not recoverable. Section 41 of the VAT Act was partly introduced to help the NHS to outsource some services to the private sector rather than retaining many 'in house'. We believe this should also apply to charities providing the same healthcare services as those available within the NHS so they can spend their money in the most efficient way.

4. Potential solution

We have examined potential solutions to this problem in order to find the most effective one. For example, the discrepancy in funding could be addressed by 'one off' agreements that the level of grant funding allocated to the charity would be adapted to include the cost of irrecoverable VAT.

However, at a time of spending cuts and economic restraint it is unlikely that this flexibility will be built into contracts across the board. Where it is not a part of contracts, financial efficiencies achieved as a result of the transfer will be masked.

5. The proposed solution

We believe there is a more effective solution. Our proposal is to widen the scope of the contracted out service rules by amending Section 41(7) VAT Act 1994 which presently specifies that NHS Trusts and PCTs are included.

We propose that charities should also be included within Section 41(7), but only to the extent that they manage healthcare services which:

- Have historically been managed by the NHS or PCTs
- Are ultimately financed from Government resources.

This could just be applied to NHS services transferred or financed by the government from the date Section 41 is amended. In this event the solution would not alter the amount the Treasury currently pays out in recoverable VAT as it is simply designed to reflect the existing VAT position enjoyed by NHS Trusts and PCTs.

This change would ensure that the impact of irrecoverable VAT does not affect service levels and would not act as a barrier to efficiencies being achieved. An



unintended consequence of the current arrangement is that the Treasury receives more VAT payments that are not reclaimable when services are transferred from PCTs or NHS Trusts to charities. This means they raise more money as a result of the transfer. A move towards mitigating for this would show that the government is committed to both the Big Society and NHS Reform agendas.

We would welcome application of this principle to include all services currently provided for or funded by the NHS, but we recognise this would remove funds that are currently received by the Treasury from the charity sector. However, we hope the solution we have proposed would act as a step-change towards this wider reform as we do not believe the government would want to gain financially from charitable providers of care in the long term.

5. Wider considerations

It is expected there will be no material impact on private sector providers of similar care facilities, as any change in law will only maintain the existing position. In fact by limiting the proposed relief to charities only, it would mean that any efficiencies or cost savings achieved would be directed back into care as opposed to removed as profits.

The VAT relief detailed in Section 41 covers only non business activities and therefore will not be available to providers of care which receive payment from patients. The different VAT regimes have existed side by side for sometime in the healthcare sector and we see no reason this cannot continue.

6. Precedent for change

Precedent has been set for this change by both the present and previous governments.

The recent creation of Section 33B of the VAT Act 1994 gives VAT relief to Academy Schools. This amendment in law was required to maintain the existing VAT recovery position in relation to schools which have been transferred out of local authority control.

Local authorities enjoy full VAT recovery on expenditure related to non-business activities. Again, this is included in the 1994 VAT Act. The previous government legislated to include museums in this clause.



In fact, we believe the change that we are seeking is less complex to implement than either of these changes as minimal changes to legislation are required.

7. The pledge

We aim to work with MPs, Lords and other charitable providers working in healthcare to build momentum around this issue. We believe we can encourage the government to change existing policy in this area as it currently acts as a barrier to the success of both the Big Society and NHS reform agendas.

MPs have already tabled an EDM (1261) on this subject that we would encourage you to sign. We would also like to ask you to consider writing to the Chancellor about this matter, calling for him to examine our proposal.

Please pledge your support to our campaign by contacting Blanche Jones, Public Affairs and Policy Manager on blanche.jones@sue Ryder.org or calling 0207 400 0445



Appendix One

Below is a table that looks at the effect of irrecoverable VAT on Sue Ryder's neurological care centres. If you would like to see the same information for our hospices, or to see the breakdown of the figures by centre, please contact us on the details provided above. This table has been produced for Sue Ryder by the accountancy firm BDO.

RUNNING EXPENSES		£	VAT incurred	VAT recoverable by local authority	VAT recoverable by NHS Trust/PCT	VAT recoverable by charity
Nurses	Registered (On Rota)	2,693,557				
	Registered (Off Rota Bank)	75,243				
	Registered (Off Rota Agency)	27,500				
	Unregistered (On Rota)	4,016,705				
	Unregistered (Off Rota Bank)	133,408				
	Unregistered (Off Rota Agency)	57,500	11,500	11,500	11,500	
Salaries & Wages		2,656,808				
Other Costs						
	Energy Costs & Water	447,176	89,435	89,435		
	Catering Supplies	298,656	59,731	59,731	59,731	
	Laundry & Cleaning Supplies	111,340	22,268	22,268	22,268	
	Staff Training	43,997	8,799	8,799	8,799	
	Staff Uniforms	13,769	2,754	2,754		
	Consumables					
	Medical Supplies	114,479				
	Med. Supplies					
	Equipment	36,135				
	Therapy Supplies	22,004				
	Vehicle Costs	26,758	5,352	5,352	5,352	
	Travel Expenses	36,395	7,279	7,279		
	Telephones &	25,674	5,135	5,135		

Sue Ryder

Postage					
Printing Stationery & IT	35,212	7,042	7,042		
Waste disposal clinical	30,570	6,114	6,114	6,114	
Waste disposal general	31,520	6,304	6,304	6,304	
Property Expenses					
Salaries	226,518				
Repairs & Maintenance	138,236	27,647	27,647	27,647	
Maintenance Contracts	110,259	22,052	22,052	22,052	
Furnishings & Equipment	31,121	6,224	6,224		
Rent & Rates	23,333				
Insurance	59,876				
Other Expenditure					
Legal & Professional Care Standards	13,270	2,654	2,654	2,654	
Registration	24,508				
Advertising Costs	13,662	2,732	2,732		
Sundry Expenses	3,527	705	705		
Restricted Expense	29,443	5,889	5,889		
TOTAL RESOURCES EXPENDED	11,608,159	299,617	299,617	172,421	0
VAT cost to local authority (£)		0			
VAT cost to NHS Trust/PCT (£)		127,196			
VAT cost to charity (£)		299,617			