VAT Alert
VAT Cost Sharing exemption

The Government today published draft legislation intended to give effect to the VAT Cost Sharing exemption contained in Article 132(1)(f) of the EU VAT Directive. It also published some guidance in which it summarised the responses to a consultation exercise regarding this exemption which was held earlier this year.

Who will be affected?

The exemption has potential to benefit all organisations who are unable to reclaim all the VAT they incur on their expenditure. As such, it is likely to be advantageous to bodies such as universities, charities, housing associations and medical bodies, as well as commercial organisations in the financial services and insurance sectors.

What does the exemption apply to?

The draft legislation mirrors EU legislation and exempts services supplied where:

1) Services are supplied by an independent group of persons to members of that group;
2) The group members are unable to reclaim all the VAT they incur;
3) The services provided are directly necessary for a non VAT-able activity;
4) The services are supplied at cost; and
5) The exemption is unlikely to cause distortion of competition.

Potentially, the exemption applies to services which are provided to members of a cost sharing group, provided certain conditions are met. In practice, this could cover services provided to unconnected bodies who come together to share infrastructure resources and costs as well as to groups of companies who centralise common costs and resources.

What limitations will be applied?

Guidance published today suggests that the Government plans to limit the application of the exemption in certain cases. In particular, it will require the supplier of exempt services to be a separate legal entity from the recipients of the services (thus preventing contractual cost sharing alliances). Whilst it will allow connected parties to reply upon the exemption, it will not allow the supplier of the services to be controlled by a third party. This in particular seems to be directed against outsource providers.

A number of other restrictions are proposed (some of which do not seem to be supported by EU legislation) concerning the level of non VAT-able activity a recipient of services must have before being able to use the exemption.
When will the exemption be introduced?

The Government intends that the exemption will be included in the Finance Act 2012. However, it accepts that taxpayers can already rely upon the fact that the provision already exists in EU law and has direct effect. Anyone whose circumstances already meet the tests in the law may be able to claim exemption with retrospective effect.

Further information

To discuss the Cost Sharing exemption, please contact your usual Deloitte adviser or Richard Gilroy, ph 020 7303 2864.