

Danish Study on VAT on charities

It is interesting to compare the results from the Ernst & Young study in Ireland with a similar survey carried out for an umbrella body of Danish charities called ISOBRO in March 2002. The survey was undertaken at the request of the Danish Tax Minister to establish the amount of VAT paid by Danish charities.

The ISOBRO survey established that in the year 2000:

- The total expenditure of Danish charities was approx. **€784 million**
- The total VAT paid out on this was **€27 million**
- Danish public voluntary organisations (PVOs) or charities receive just over **34%** of their gross income through private contributions compared to the Irish figure of **52%**

The standard VAT rate in Denmark is 25% with little use made of lower rates compared to the Irish standard rate of 21% and lower rate of 13.5%. Despite the difference in rates the VAT burden on charities is remarkably similar i.e. the proportion of VAT as a % of total expenditure is 3.6% in each case. The Danish study does not categorise the VAT payments by expenditure heading so that a direct comparison on this is not possible.

ISOBRO are in consultation with the Danish Tax Minister about introducing a VAT refund mechanism for Danish charities.

[Source: Redegørelse – Kobsoms og de frivillige organisationer – ISOBRO – March 2002]

Conclusion

The report demonstrates that VAT is a significant burden on Irish Charities costing the sampled charities €18million in 2001

The VAT burden can be relieved by way of a Ministerial Order under Irish VAT law without contravening the EU Sixth VAT Directive

The actual cost to the Exchequer of introducing a refund mechanism is 52% of the total VAT bill since the remainder is paid for from public funding - in the case of the sampled charities a VAT refund would cost the exchequer €9.4m

The advantage of a VAT refund mechanism is that control remains with the Revenue Commissioners as to what organisations qualify for refunds

Acknowledgements

Irish Charities Tax Research Ltd would like to acknowledge the work of Jim Somers, Breen Cassidy (Partners) and Maria Reade (Supervisor) of Ernst & Young on the survey and report and accountants Ann Fitzsimons and Ola Ladenegan, both of whom volunteered to work on the research. Thanks also to Niamh Ni Chonghaile of The Irish Cancer Society and Niamh Cullen of Barnardos for their input on the Research Advisory Committee.

The full report is available for download on www.charitytaxreform.com or www.vatcampaign.com

Report reveals €18m VAT burden on Irish Charities

Summary

Irish charities pay out more than €18m in unreclaimable VAT each year, according to a new report from tax experts Ernst & Young. The comprehensive report was prepared for Irish Charities' Tax Research Ltd and is based on the first detailed survey of the VAT burden imposed on the Irish charitable sector.

- The report demonstrates that VAT is a significant burden on Irish Charities costing the sampled charities €18million in 2001
- The VAT burden can be relieved by way of a Ministerial Order under Irish VAT law without contravening EU law
- The actual cost to the Exchequer of introducing a refund mechanism is 52% of the total VAT bill since the remainder is paid for from public funding - in the case of the sampled charities a VAT refund would cost the exchequer €9.4m
- The advantage of a VAT refund mechanism is that control remains with the Revenue Commissioners as to what organisations qualify for refunds

Last year Concern's VAT bill came to €2m. *"Our entire programme for Ethiopia, which is our biggest, costs us €3m annually. With the money handed over in VAT, we could feed two-thirds more people this winter in Ethiopia "* says Tobin Aldrich, Appeals Director with Concern.

Over the past 12 years Irish charities have repeatedly highlighted the heavy VAT burden that is imposed on them, pointing out that it limits and curtails the amount of assistance they can provide to those in greatest need. Since charities are generally not regarded as being "in business" they are treated as "exempt" from VAT.

In reality, this means that because charities don't charge VAT on the valuable services they provide, they cannot reclaim the VAT they pay on unavoidable costs - building costs, recruitment etc.

Over the years there have been many estimates put forward as to the extent of the VAT burden on the charity sector but most of these have been based on limited information from a small number of charities and/or extrapolated from more general reports on the sector.

For this reason Irish Charities Tax Research Ltd (ICTRL) commissioned an independent study of the issue by tax experts Ernst & Young. Their report, summarised below, is based on the first detailed survey of Irish charities on how much VAT they pay each year.

Essentially Ernst & Young were asked to answer three questions:

- 1 How much do Irish charities pay out in irrecoverable VAT each year?
- 2 How much of the money that pays the VAT bill comes from fundraised income and how much from government or other public bodies?
- 3 What, if anything, can be done about the problem at national level?

Results from a comparable survey on VAT and charities carried out in Denmark (March 2002) reveal a remarkably similar pattern to the Ernst and Young study.

Research Sample

Given the lack of definition of the sector the survey was confined to organisations which meet the requirements for charitable tax exemption as laid down by the Revenue Commissioners.

On the basis that the expenditure of the members of the Irish Charities Tax Reform Group (ICTRG) represent the major proportion of the total spend of the charities sector (a claim borne out by the research findings) they were all invited to take part in the survey together with a random sample drawn from the Revenue database on tax exempt bodies.

The sample period was 1 January 2001 to 31 December 2001 (or for some charities the financial year closest to the sample period).

The total number of charities surveyed was 219 (93 member charities of ICTRG and 126 randomly selected charities).

Key Research Findings

The sampled charities paid out a total of over **€18 million** in VAT on total expenditure of **€500 million** during the period

Less than **€300,000** of this was eligible for a VAT refund

83.5% of the total expenditure of **€500 million** and **76.2%** of the total VAT bill of **€18m** was accounted for by members of ICTRG, supporting their claim to represent the major proportion of the total spend of the charities sector

52% or **€9.4million** of the total VAT incurred was funded by private means e.g. fundraising, donations, sponsorship, commercial activities etc.

47% or **€8.5million** of the total VAT incurred was funded by the government either directly or indirectly via other public bodies such as FAS and local authorities

The source of funding of the remaining **1%** is unknown

Figure 1 Total Expenditure of sampled charities - 2001



Figure 2 Total VAT Expenditure of sampled charities - 2001



Figure 3 VAT expenditure by source of funding

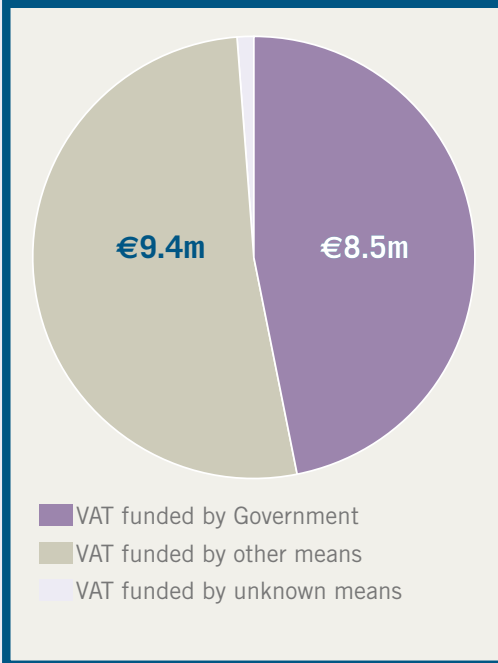
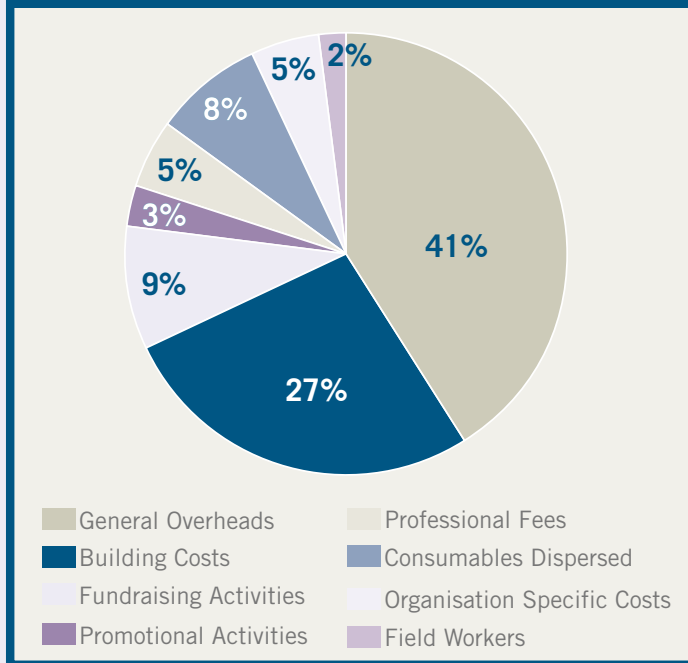


Figure 4 Breakdown of VAT by expenditure heading



Of the total VAT bill of **€18m**.

- more than **€7m** was incurred on general overheads,
- almost **€5m** on capital expenditure
- **€2m** on fundraising and promotional costs,
- **€1.5m** on consumables,
- **€1m** on professional fees and
- the remaining **€1.5m** on other organisation specific costs.

The report was quite unambiguous on the power of the Minister for Finance to relieve charities of their VAT burden:

“Although the Minister is obliged to collect VAT (since it forms part of our resources which fund the budget of the European Union) once collected the VAT can be disbursed as the Minister deems appropriate, without EU clearance. This has been confirmed by Commissioner Frits Bolkestein (Directorate-General for Taxation and the Customs Union).

The Minister has, by way of section 20 VAT Act 1972, the necessary power to make available to charities, the various reliefs which are outlined in this report.

It is therefore recommended that VAT continues to be charged to charities with a relief from VAT effected by way of Ministerial Order.

The granting of relief via a Ministerial Order ensures that the benefit of the relief goes, in its entirety, to a specific charity or individual. None of the relief is dissipated by way of the retailer increasing his price which might be the case if relief was granted by another method. Furthermore, by using a Ministerial Order control remains with the Revenue Commissioners.”