



10 December 2019

To: Manvir Sagoo

By Email: operation.ofPE@hmrc.gsi.gov.uk

Simplification of Partial Exemption and Capital Goods Scheme- Call for Evidence.

About us

1. This response is from the Association of British Dispensing Opticians (ABDO), the Association of Optometrists (AOP) and the Federation of (Ophthalmic & Dispensing) Opticians (FODO). Together we represent the entire range of optical businesses from small family-run opticians to large scale multi-location businesses. We also represent the majority of optometrists and dispensing opticians in the UK.
2. We apologise for the late submission of our response to this first phase of consultation (our email of 26 September 2019 to you refers). However we wanted to be sure we had properly reflected all our members' views before submitting.

Our response

3. Since the 1990s all optical businesses have been affected by Partial Exemption (PE) of VAT with the Capital Goods Scheme (CGS) applying to larger businesses. These are therefore very important issues for our members and we welcome HMRC's openness in seeking to simplify both calculations for the benefit of all parties. Our responses to the grouped questions are below.

Partial Exemption Special Methods (Questions 1- 8)

4. Partial Exemption Special Methods (PESMs) have been problematic in our sector partly because of the complexities in applying them to healthcare operating models. As a consequence, to the best of our knowledge, all eye care providers who have sought to use a PESH have had their proposed methods rejected by HMRC. This is invariably because
 - a. the HMRC officer visiting the provider is usually unable to decide whether a PESH is fair and reasonable i.e. they find healthcare complex

- b. HMRC advice to visiting officers is not very helpful
 - c. visiting officers have to consult HMRC's policy section for advice
 - d. this takes time and, as visiting officers are increasingly overstretched, further confusion can follow
 - e. providers who try to get clarity direct from HMRC about meeting their tax liabilities through PESM experience a lack of HMRC capacity and capability to assist them.
5. As is well-known, there are important differences as well as similarities between healthcare businesses and there one size cannot fit all. It would be unfair for one business to be given the advantage of not agreeing a PESM with HMRC in one healthcare sector whilst another business is challenged for implementing an identical PESM in another.
 6. Given HMRC's own difficulties in applying PESMs to healthcare, it would be unfair to expect any healthcare provider to implement a PESM without prior HMRC agreement. Given HMRC's 0% approval rate to date, this would risk exposing them to avoidable and unexpected VAT bills and penalties in the future. This – and even concerns about managing the potential risk – could easily drive small practices out of business contrary to wider government policy. This is not therefore a solution we could agree to or recommend to our members without significant additional safeguards which are not yet evident.
 7. Moreover this proposal fails, in our view, to address the root cause of the problems within the existing system which are: the complexities of delivering healthcare in a retail setting, confusion at HMRC centrally about this and lack of central clarity, advice and support for field officers and providers.
 8. A more appropriate solution, in our view, would be to require all PESMs to be agreed by HMRC at inception. This would not only bring greater consistency to VAT treatments and PESMs in eye care, it would also get to the heart of the issue and focus both providers and HMRC on resolving unclarities and getting PESMs right first time i.e. striking the balance that generates fair tax revenues for the Exchequer whilst minimising the risk of litigation for both parties.
 9. As the current system does not work effectively and efficiently for anyone, we would welcome an early meeting with the review team to discuss how PESM could be used more effectively and efficiently in the eye care sector and to inform the next stages of the review.

Increasing the de minimis limit (Questions 9-11)

10. SMEs are often unaware of their partial exemption status and, even those that are, often find it difficult to apply the attribution and standard method calculations. They often inadvertently attribute costs between non-attributable and taxable supplies or struggle to determine which sales and purchases should go into the standard method calculation. This is why most small providers choose to undertake annual rather than quarterly de minimis calculations.
11. As we have proposed before, in our view, the de minimis limit should be raised to ensure that smaller businesses fall outside PE requirements. This would have minimal effect on tax revenues but would support small businesses by relieving them of unnecessary and time-consuming work (both key strands of government economic policy).

Removal of de minimis limit (Questions 12-14)

12. It follows that we could not support the abolition of the de minimis test because of the disproportionate effect on the viability of small businesses, especially small businesses which make incidental exempt supplies. This in turn would adversely affect patient access and ultimately the taxpayer who would have to replace lost community capacity with hospital capacity, contrary to wider government health policy c.f. the NHS Long Term Plan.
13. In our view the current de minimis limit of £7500 per annum needs to rise significantly to reflect changes particularly in respect of the recovery of residual VAT on rents. When the de minimis limit was introduced in 1994, the option to tax in respect of commercial property was still in its infancy and a lot of businesses did not incur VAT on commercial rents. Now, however, with the increase in commercial rents, the almost universal application of the 'option to tax' and the rise in the VAT rate (17.5% to 20%), even the smallest optical practices now exceed the de minimis threshold, exacerbated by the disallowance of exempt input VAT.
14. The simplest and fairest solution would, in our view, be to
- a. make the de minimis limit annual rather than monthly
 - b. retain the 50% input tax limit
 - c. simply make an annual adjustment against the increased exempt input tax limit applying the de minimis limit.
15. We would be happy to undertake a benchmarking exercise with our smaller members to help HMRC develop a robust annual de minimis limit.

CGS Thresholds (Questions 15-21)

16. The current £250,000 limit does need to be revisited to reflect the significant increase in construction costs over the years which have not been reflected in the threshold. Larger members provide eye care services from prominent retail positions on the high street or within shopping centres in order to improve patient access and encourage the take-up of sight tests, especially amongst older age groups who are more at risk. The cost of the freehold or of leasing or refurbishing such premises can also now be significant, making larger opticians potentially subject to the CGS on both property transactions and the purchase of IT equipment. In practice however (although there is a cost in terms of time) the operation of the CGS is not particularly onerous. Consequently to have any tangible benefit any increase in the CGS limit would need to be significant.
17. To address these issues and meet the original aims of the CGS, to levy appropriate levels of tax in a more efficient manner, we would propose that the £250,000 limit be raised to £750,000 and the adjustment period reduced to 5 years.
18. This would also address the necessity of making annual CGS adjustments with very limited benefit to the Exchequer when the movement on VAT recovery on the asset or works is minor.
19. As most of our members fall within the definitions of alterations and refurbishments anyway, we believe there should be no distinction between the different types of building works for the reasons set out in our proposals above.

Categories (Questions 22-23)

20. It is extremely unlikely that the majority of optician's business will incur VAT on the purchase of individual items of computer equipment. Most of these will be valued at less than £50,000 and so fall outside CGS. We therefore support the proposal to remove computers from the CGS as a welcome simplification.

Intervals (Questions 24-25)

21. Optical businesses generally retain records for a period of 6 years which is the widely accepted industry norm. A 10-year adjustment period would therefore fall well outside this standard and so be difficult to implement. This would be further complicated by any changes in accounting personnel who may not be aware of pre-existing adjustment periods. It is also unlikely, in our experience, that there would be any material change to the business which would require a significant adjustment outside of a 5-year period.

22. We would therefore propose that the intervals, in respect of land and property transactions falling within the CGS, be extended to 5 years.

Other possible areas to review (Questions 26 – 28)

23. None.

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