

Academies: Accounting for VAT

May 2011

► For guidance

Introduction

1. This document provides information for Academies and Free Schools on the new VAT scheme, and the implications the scheme has for accounting and reporting procedures. Further guidance will be available from HM Revenue and Customs (HMRC) in the coming weeks.

The Current Situation

2. Some Academies have small trading (business) activities, e.g. income from lettings, the sale of educational materials, etc. Such Academies have been able to register for VAT, either voluntarily or by virtue of their level of trading turnover, and thereby to reclaim input VAT from HMRC insofar as it related to these trading (business) activities.
3. However, prior to the anticipated passage into law of the Finance Bill 2011, Academies have been unable to recover input VAT from their mainstream non-business activities, i.e. the provision of free education, which is not 'trading'. To compensate them for this additional cost the YPLA has paid Academies 'VAT grant', which has been a formulaic component of their GAG funding. Because Academies have been required to bear the full, gross cost of these inputs as the end consumer Academies have presented their costs gross in their budgets and accounts, with the VAT grant being treated as a component of income.

The Future

4. The Finance Bill 2011 will change this situation. There will be put in place a special scheme whereby Academies will be able to reclaim input VAT on their non-business activities directly from HMRC and VAT grant will therefore no longer be payable by the YPLA. It is the intention that input VAT on non-business activities will be claimable from HMRC from 1 September 2011, backdated to 1 April 2011. This will effectively place Academies on the same basis as LA maintained schools, where VAT has been recovered via the LA.
5. The YPLA will continue to pay a sum equivalent to VAT grant for the period from April to August 2011 to Academies that have already been notified of a VAT grant funding allocation for academic year 2010/11, and will then reclaim this from Academies by 31 March 2012, in order to avoid any double-funding. Newer Academies, which have not been notified of a VAT grant entitlement for academic year 2010/11, will be able to claim their eligible VAT cost from the HMRC from September 2011 and so will not be subject to any VAT grant clawback by the YPLA.

Accounting for VATable Costs

6. In broad terms, Academies should be neither better off nor worse off as a result of the above changes. However the question has arisen as to whether Academies should continue to show gross costs in their budget returns despite the fact that these costs will no longer need to be borne in full, and also whether the VAT reclaim from HMRC should be shown as income (in the same way as VAT grant was previously).

7. YPLA's position is that, since Academies will no longer need to bear the full costs of VAT (as was the case previously) then costs should be shown net, and the VAT reclaim should not be treated as income.

8. The internal accounting position may be demonstrated in the context of an Academy purchasing some materials at the cost of £100 + £20 VAT:

- The goods are purchased using cash:

DR I&E account (expenses)	£100
DR: Balance sheet (VAT debtor):	£20
CR: Cash	£120

So, the net cost is shown in the income and expenditure account, with the VAT element posted to the balance sheet as a debtor (HMRC being the debtor).

- The VAT reclaim is then made:

DR: Cash	£20
CR: Balance sheet (VAT debtor)	£20

So, the debtor is cleared, the cash position is restored and only the net costs have been taken through the income and expenditure account. Further, since the receipt of the VAT reclaim hits the balance sheet only, it can not be treated as income.

Transitional Arrangements for Academic Year 2010/11

Split In-year Accounting Treatment

9. Assuming that the Finance Bill 2011 passes into law, these new VAT reclaim arrangements will come into effect from 1 April 2011, i.e. part-way through academic year 2010/11, with VAT grant being payable up to 31 March 2011 and the HMRC refund scheme taking effect from April 2011. The result of this is that, for 2010/11, Academies are put in a position whereby:

- they will need to account gross for their non-business costs for the period September 2010 to March 2011, because the costs must be born in full by the Academy during this period, and treat VAT grant as a component of income;
- but they will need to account for their non-business costs net of VAT for the period April to August 2011 (as the costs no longer need to be borne in full) and not treat the VAT reclaim from HMRC as income (as above, it should be recorded as a debtor until such time as the reclaim from HMRC is complete, whereupon it should simply be recorded as the receipt of cash).

Transitional VAT Funding from the YPLA

10. It has been recognised by the YPLA that, for those Academies which have been open for some time and have been receiving VAT grant as a component of income, that the period between April 2011 (when VAT grant will terminate) and September 2011 (when the first VAT reclaim from HMRC should be possible) could be challenging in terms of cashflow. As a concession therefore, the YPLA will continue to pay these Academies a sum equivalent to 5/12ths of the notified VAT grant for the period April to August 2011, but that this sum will be recovered by the YPLA by 31 March 2012.

11. Since these sums are to be recovered, they cannot be treated as income. Rather, they should be treated as a simple receipt of cash, balanced by the creation of a creditor to indicate the liability to repay. The accounting entries would be as follows:

- Recoverable 'VAT funding' paid by the YPLA between April and August 2011:

DR Cash	£20,000
CR Balance sheet (YPLA creditor)	£20,000

- Recoverable 'VAT funding' repaid to the YPLA after September 2011 (by 31 March 2012):

DR Balance sheet (YPLA creditor cleared)	£20,000
CR Cash	£20,000

Once again, the income and expenditure account is unaffected by either the advance or its repayment, with the result that the advance of recoverable VAT grant cannot be treated as income.

Additional Claims

12. In exceptional circumstances, if an Academy considers that it has an unmanageable shortfall or solvency issues as a result of the VAT grant for September 2010 to March 2011 being insufficient to cover VAT costs for this period, YPLA will consider claims on a case-by-case basis.

Arrangements for Academic Year 2011/12 Onwards

13. From September 2011 there will be no VAT funding payable to Academies by the YPLA and all input VAT on non-business activities should be reclaimable from HMRC. As such, all costs for the whole academic year should be shown net of VAT. Accumulated VAT paid out to suppliers and then reclaimed from HMRC will be reflected as balance sheet entries, with no impact at all on the income and expenditure account or budget. The VAT displayed in the accounts should also be split into business and non-business costs, as the new VAT reclaim scheme only applies to non-business costs. Further guidance on what this means will be available from HMRC shortly.

Summary

14. The YPLA does not dictate to Academies on how their internal accounting should be undertaken, nor does it give advice in relation to taxation. These issues are rightly the province of Academy finance directors, their auditors and advisors and HMRC. However the YPLA is obliged to set out how it wants Academy financial information presented to it. Consequently it has been determined that, with effect from April 2011, Academy budgets and income and expenditure accounts should be shown net of recoverable VAT and that any VAT to be reclaimed should not be treated as income. If an Academy is to receive recoverable VAT funding from the YPLA by way of transitional protection for the period April to August 2011 then these sums cannot be treated as income and should instead be shown as a simple cash receipt with an equivalent creditor.

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