

VAT – Why Us? Do I Have to? & What Is It All About?

The issue of VAT is one that raises its head on a regular basis and typically the questions asked are as follows?

- Why are Counsellors and Psychotherapists required to charge VAT whilst Psychologists don't?
- I am not earning very much as a Counsellor/Psychotherapist, do I have to charge VAT?
- When I exceed the exemption threshold do I only charge VAT on the excess income or on all my income?
- Is all of my income taxable or just my Therapy income?

As a result of these issues being brought up by members on an ongoing basis we asked tax expert, Fergal Maher of Byrne Curtin Kelly, auditors to IACP, to prepare an updated guide for IACP Members.

We hope that Fergal's comprehensive summary addresses all of your questions however if not then please don't hesitate to send your queries through to accounts@iacp.ie and we will ask Fergal to comment further.

On the greater issue of why it is necessary for Counsellors and Psychotherapists to charge VAT when their clients are predominantly attending in a personal capacity and therefore cannot reclaim VAT, we have, in the past, raised this with Revenue and with Government representatives and other political parties in the ongoing discussions around the regulation of the profession.

However, recently we have been in discussion with Tony Kelly, our client partner in BCK, and sought his advice around making a further submission to Government to incorporate a compelling business case for changing the VAT status of Counselling and Psychotherapy to that of Exempt, in line with other medical professionals.

We will keep you apprised of our progress with the submission and in relation to any response that we receive from Government or Revenue.

VAT – Implications for Counsellors and Psychotherapists

Value Added Tax

1972 was in many ways a momentous year for Ireland. London imposed direct rule on Northern Ireland, the Republic was (yet again) broke and in May of that year a massive 83% of the electorate voted in favour of Ireland entering the European Economic Community. A condition of entry into the European Community was the introduction of a system of Value Added Tax which was already operating in other EU countries. And so it was that our old Turnover and Wholesale taxes were replaced with a new system of VAT with rates of between 0% to just over 30%.

This new tax, which would quickly grow to become the second largest contributor to the Exchequer (after income tax), was unusual in many ways. The tax was based on turnover rather than profits and designed so that the cost is borne by the end-user rather than suppliers. But perhaps most controversially, VAT was (and continues to be) applied at vastly differing rates to supplies of goods and services on what can often appear to be an arbitrary basis.

The curious nature of this tax was perhaps best summarized by Lord Justice Sedly in the 2001 UK Appeal case of Royal & Sun Alliance, when he said.. "Beyond the everyday world...lies the world of VAT, a kind of fiscal theme park in which factual and legal realities are suspended or inverted".

This fiscal theme park is supported by directives at the EU level, legislation at the national level, and a myriad of revenue precedents and court decisions in between.

VAT and Medical Services

All EU Member States are required to introduce and apply their own VAT legislation which must comply with the relevant EU Directives. Article 13A(1) of the European Communities Sixth Directive lists certain activities which countries are required to exempt from VAT and includes 'The provision of medical care in the exercise of the medical and paramedical professions as defined by the Member State concerned'.

Exemptions from VAT have always been interpreted very narrowly by the EU and member states. In broad terms it is accepted that the exemption for medical services applies to services provided to protect, maintain or support the health of a patient. As the exemption applies to services rather than the service provider, medical professionals may find that while the vast majority of their work is VAT exempt, certain services they provide are taxable as they do not protect, maintain or support the health of a patient (e.g. the provision of expert reports for medical negligence litigation).

Schedule 1 of our 2010 VAT Consolidation Act lists exempt services, the section relating to Medical Services includes the following:

- Professional medical care services recognised as such by the Department of Health and Children.
- Other professional medical care services that, on 1 January 2010, were recognised by the Revenue Commissioners as exempt activities.

In an information leaflet published in 2011, Revenues VAT Interpretation Section lists Medical Professionals they will treat as VAT exempt when providing qualifying medical services. The list includes.

- Persons registered under the Medical Practitioners Act 2007.
- Persons registered under the Nurses Act 1985.
- Persons designated under S4(1) of the Health and Social Care Professionals Act 2005;

Section 4(1) of the Health and Social Care Professionals Act includes health care providers such as Dietitians, Occupational Therapists and Psychologists.

Unfortunately Psychotherapists are not included on the above lists and it is currently the opinion of the Revenue Commissioners that the profession is taxable at the reduced rate of 13.5% in accordance with Schedule 3 paragraph 21 (1) of VAT Consolidation Act , which applies to "Services consisting of the care of the human body,"

What this means for the practising psychotherapist is that where their income from the provision of services exceeds, or is likely to exceed €37,500 in a 12 month period, they are required to register for VAT.

In the case of services consisting of the care of the human body (including presumably the mind), VAT should be accounted for at 13.5%. Where other services are provided (e.g. fitness certificates, lifestyle counselling, expert witness etc), VAT should be accounted for at the standard rate of 23%.

This can have a very significant effect on the cash flow of a practising Psychotherapist. Patients are typically not vat registered and therefore cannot reclaim VAT on fees, and while therapists are entitled to claim a VAT deduction for tax incurred on any practice expenses (electricity, phone, rent etc), this 'input VAT' will not usually be significant. The net effect is that for every €100 in fees a therapist earns he or she will first have to pay VAT of €11.90 ($100 \times 13.5\% / 113.5\%$), leaving just €88.10 to pay other expenses such as wages, employers taxes, rent, utilities, and lastly him or herself.

In addition to being a cash flow burden, VAT can also be an administrative burden, though with appropriate systems in place the burden should not be overly cumbersome.

Registering for VAT

A practitioner is required to register for VAT as soon as it becomes apparent that annual turnover will exceed the €37,500 threshold. Where a number of practitioners are trading together via a partnership or company, the €37.5k turnover threshold applies to the partnership/company as a whole and not the individual practitioners. Therapists (or their agents) should register for VAT via Revenues Online Services (ROS).

VAT returns are usually filed bi-monthly via ROS, with a return for the Jan/Feb VAT period due for submission and payment by 19th March etc. Traders whose annual liability is less than €14k have the option of filing quarterly returns.

Alternatively practitioners can elect to avail of Revenues Direct Debit on Line payment system.

Traders availing of this scheme will pay their VAT monthly by direct debit and submit an annual VAT return, at which point an overpayment, or additional liability might arise.

When registering for VAT the therapist will be requested to provide details of the bank account to be used for the purpose of making payments or receiving refunds.

Accounting for VAT

VAT is usually accounted for on an *invoice basis*, i.e. the service provider must account for VAT in the period in which an invoice is raised, regardless of when payment is actually received. Traders can avail of the *cash receipts basis* if sales are less than €2m per annum, or 90% or more of supplies are to unregistered entities. The majority of practitioners / practices should qualify for the cash receipts basis and when registering for VAT it is important to notify Revenue that you wish to avail of this basis.

Where services are provided to VAT registered businesses the usual practice would be to quote a net-of-vat fee and issue an invoice including the appropriate VAT which the client should then be able to reclaim. A valid VAT invoice must include all of the following information:

- the date of issue of the invoice,
- a sequential number which uniquely identifies the invoice,
- the full name, address and the registration number of the therapist (or practice),
- the full name and address of the person to whom services were provided,
- the nature of the services provided,
- the date on which the services were provided,
- the net of VAT fee and the appropriate VAT at 13.5% and / or 23%

In calculating their bi-monthly or annual VAT liability a practitioner / practice is entitled to deduct any VAT incurred on the purchase of goods and services in so far as:

- the goods / services are used for the purposes of making taxable supplies and.
- the practitioner has a valid VAT invoice in respect of the expense (see above).

A deduction may not be taken for expenditure on food, drink, entertainment or personal services. VAT on accommodation is allowable only where it relates to attending conferences, subject to certain conditions. VAT on petrol or on the purchase or hire of cars is also specifically excluded, however VAT on diesel is deductible in so far as it is used for the business purposes, other than travel to or from work.

Practitioners are required to retain VAT invoices for a period of 6 years after the relevant transaction and while it is not necessary to provide invoices when filing a VAT return, this information will be requested in the event of a routine VAT return compliance check, or a revenue audit.

Conclusion

While VAT rules and regulations seem relatively straightforward at first glance, their interpretation and application can produce some very strange results.

A 'fiscal theme park in which factual and legal realities are suspended or inverted' seems a very apt description of a world in which ballet dancing classes are VAT exempt as a cultural activity, but Irish dancing classes are taxable at 23%. Unfortunately practicing psychotherapists currently find themselves front row and centre in this fiscal theme park.

While it is to be hoped that Revenue will change their view in the not too distant future, at the moment psychotherapists are pretty much alone amongst conventional health care providers in having to charge VAT on their services. As these services are predominantly provided to unregistered individuals, the VAT cannot be reclaimed and therefore the cost invariably falls on the practitioner.

A further consequence of providing taxable services to unregistered individuals is that failure to operate the tax properly can lead to an expensive VAT demand (with interest and penalties), which cannot be invoiced on to the client.

Because VAT is a tax on turnover rather than profit, it can frequently be overlooked by therapists who might mistakenly believe they are not making enough to be within the charge. However, it is for this very same reason that failure to operate the tax properly can prove very costly and therefore VAT is a tax that should not be overlooked by practising psychotherapists.

Fergal Maher FCCA, CTA

Fergal is Taxation Director with BCK Accountants Ltd and has over 20 years' experience providing taxation compliance and consultancy services to a wide variety of Irish based SME's and individuals.

