

VAT and Direct Marketing

The definitive guide for the charity sector

Brightsource

Introduction

Confusion and misinformation abound within the charity sector with regard to VAT and direct marketing. This is hardly surprising given the succession of VAT Notices issued by HM Revenue and Customs since the last change in the law in April 2000, when the VAT Act was amended to allow advertising for a charity to be zero-rated. Differing interpretations of this new act led to much uncertainty, and Revenue and Customs subsequently published an explanatory VAT Notice (701/58), which included a concession allowing 'pre-printed appeal letters' and 'collection envelopes' (along with collection boxes and label stickers), to be zero-rated. However, this VAT Notice also stated that any charity promotion aimed at a *selected individual* was specifically excluded from any VAT relief.

So, on the face of it, a personalised charity mail pack did not count as 'advertising' and could no longer be zero-rated – unless the format was such that it could escape VAT under the Printed Matter Regulations. To make matters worse, the government seemed to be saying that if a mailpack failed to gain a zero-rating through this route, then the charity also had to pay VAT on all preparatory services as well, such as list buying and agency creative and account handling fees.

Then in June 2001, Revenue and Customs issued another version of VAT Notice 701/58. This included an 'Extra Statutory Concession', which essentially allowed most direct mail formats likely to be used by a charity to be zero-rated, effective from April 2000.

This Notice was then revised yet again and reissued in March 2002. One of the changes was to state that charities could not use the Extra Statutory Concession in conjunction with the 'package test' – the long established means of gaining VAT relief for many direct mail packs under the rules for printed matter, (contained in a different VAT Notice, 701/10). This other VAT Notice has also been changed recently – the latest version, issued in August 2003, states that from this date a charity *could* use the Extra Statutory Concession in conjunction with the 'package test'...

Hence the continuing uncertainty that exists within many charities. In response to many requests, Brightsource (formerly Target Direct Print) has prepared this briefing paper to help clarify the current VAT rules and how they apply to the different marketing communications produced by charities. We have focussed on direct mail and doordrops, as this is the area where the confusion is greatest. We also discuss when a charity must 'single source' the different services required to produce a marketing campaign, in order to gain full VAT relief.

Ways in which a charity can gain relief from VAT

There are four primary routes through which a charity's advertising and direct marketing communications may be fully or partially zero-rated. These are:

1. when an **advertisement** falls under the definition of advertising in VAT Notice 701/58 (*Charity advertising and goods connected with collecting donations*). If it meets these criteria, it can get what I will refer to as 'Charity Advertising Relief'
2. where a **direct mail pack which only contains printed items** qualifies for VAT relief using the 'package test' described in VAT Notice 701/10 (*Zero-Rating of Books etc*). In this case it gets what I will refer to as '*Package Test Relief*'. Charities may use the Extra Statutory Concession to pass the 'package test' much more easily than a commercial organisation, because the Concession allows personalised appeal letters, outer envelopes and reply envelopes to be zero-rated when supplied to a charity.
3. where a **print item** (such as a leaflet or brochure) can be zero-rated under VAT Notice 701/10 (*Zero-Rating of Books etc*). I shall refer to this as '*Printed Matter Relief*'. (This relief applies equally to charities or commercial organisations.)
4. where a **direct mail pack containing a non-print item** qualifies for partial VAT relief using both the Extra Statutory Concession

in VAT Notice 701/58 (*Charity advertising and goods connected with collecting donations*), and also Printed Matter Relief referred to above. If it does, it gets what I will refer to as '*ESC and Printed Matter Relief*'.

The criteria for each of these routes to VAT relief will be described later. In some instances (for example an insert produced for a charity), more than one option might be applicable. These four kinds of VAT relief relate to the VAT liability of the end product – the production of a TV ad, or the printing and personalisation of a mailpack.

But we also need to consider a second issue, the VAT liability of creative or other services leading up to the production of a charity's marketing communication. When does a charity need to 'single-source' the preparatory services with the production of the end product, in order to maximise VAT relief?

Single Sourcing

If the end product can be zero-rated under the *Charity Advertising Relief* route described above, then all the different services associated with the production of the advert or mail pack (creative, photography, list buying, print management) can also be zero-rated.¹ This applies regardless of whether a charity is buying these different services separately or through one source. Hence if a charity buys media space from a media independent, creative services from an agency, and print and production services from a print management company, then each supplier should zero-rate their services.

To restate this important point another way: if an advert being produced for a charity has *Charity Advertising Relief*, then the client can purchase services independently from a variety of suppliers and not be charged VAT by any of them. (The charity should however supply a VAT zero-rating declaration to each supplier.)²

However, this approach does *not* hold true where *Package Test Relief* is being used to gain zero-rating for a mailpack. In these circumstances, all services 'ancillary, integral or incidental'³ to the end product (e.g. list buying, creative, print management etc) can only be zero-rated if there is a *single source of supply*

to the client.⁴ Under single sourcing rules (or 'single supply'), the VAT liability of related or ancillary services follows the VAT liability of the end product, (i.e. the mail pack or other printed item). So if a mailpack is zero-rated using *Package Test Relief*, but the client buys lists, creative, and print from three separate suppliers, then only the print can be zero-rated. The list broker and creative agency would have to standard-rate their services. Alternatively, the charity could ask for its suppliers to route their invoices through a single supplier, and thus escape VAT on all the services contributing to the end product. *Any supplier in the supply chain can act as the 'single source'*.

Single sourcing is also required if a charity wishes to avoid paying VAT on the design costs of producing a brochure, for example, where the print costs will be zero-rated under the *Printed Matter Relief*.

The situation becomes more complicated when a mailpack or doordrop contains a *non-print item* such as a pen or an audio tape. In this case, the inclusion of the non-print item makes the pack ineligible for the package test. (See page 5 for more information on the test.) VAT must be charged on the production cost of the pen, or tape etc (as standard-rated items). But given that a charity can claim zero-rating on all elements in the mailpack that qualify for relief under *ESC and Printed Matter Relief*, the preparatory services related to these other elements can also be zero-rated,⁵ *as long as the supply is single-sourced*. (The Extra Statutory Concession has the effect – for charities – of classing outer and reply envelopes, and appeal letters, as zero-rated print items.)

To summarise this point: where a non-print item is created and produced (e.g. an audio tape or pen), it must be standard-rated, and that proportion of the creative agency fee required to create it should be standard-rated.

The VAT and single sourcing matrix for charities

The table below draws together the two issues outlined earlier:

- the VAT liability of different types of charity marketing communications
- whether there is a requirement to single source any associated preparatory services in order to maximise VAT relief.

Type of marketing communication	Examples	VAT liability	Single sourcing requirement
Advertising in someone else's time and space	TV and cinema ads, outdoor and press advertising, inserts	Zero-rated under <i>Charity Advertising Relief</i>	No need to single-source
Direct mail and doordrops containing only printed items	Mailpacks or door drops containing personalised or unaddressed letters, reply envelopes, zero-rated print such as leaflets, brochures, flyers, newsletters, and one, possibly two, standard-rated items such as stickers, calendars, raffle tickets, greetings or Xmas cards, posters, or postcards	Almost all instances can be zero-rated under <i>Package Test Relief</i> (combined with the Extra Statutory Concession)	Single-sourcing required
Direct mail and doordrops containing an item not printed on paper or card	Mailpacks or doordrops which contain a pen, an audio tape, etc	Charities should gain partial relief on those print items that can be zero-rated under <i>ESC and Printed Matter Relief</i>	Single sourcing required for items gaining VAT relief under the <i>ESC and Printed Matter Relief</i> . Single sourcing not relevant to the 'non-print' item which cannot escape a standard VAT rating.
'Stand alone' printed items	Leaflets, newsletters, brochures, folders, posters, that are <i>not</i> part of a mailpack or doordrop	<i>Printed Matter Relief</i> will enable charities to zero-rate some items.	Single sourcing required to gain VAT relief on creative services related to zero-rated print items. Single sourcing not relevant to standard-rated print items.

'Charity Advertising Relief' in more detail

This relief is available to all charities, but not their trading companies, i.e. wholly owned subsidiaries. The relief covers *all types of advertisements placed in any medium which communicates with the public.*⁶ The advertising must be carried in someone else's advertising time and space.⁷ Broadly this includes TV, cinema, radio, posters, outdoor and bus advertising, inserts, press ads, web

sites (other than the charity's own web site), as well as all kinds of ambient media. Items such as banners, till rolls, beer mats, balloons, calendars, the reverse of car park tickets, carrier bags, painted vehicles, all qualify as an advertising medium, *as long as the charity is being charged for the advertising space.*

This rule that the 'advertising space must be owned by someone else' means that posters within a charity's own shops, and the design and build of its own web site, fail to get relief from VAT. 'Marketing and advertising

addressed to selected individuals or groups' is also specifically excluded from relief,⁸ unless it qualifies for *Package Test Relief* or *ESC and Printed Matter Relief*. Therefore *telemarketing and email marketing are always standard-rated*, but as noted earlier, direct mail packs can achieve either full or partial VAT relief. What do Revenue and Customs mean by 'selected individuals or groups'? Their definition is 'people selected by individual home, business or email address, whether named or not'.⁹ Adverts targeted at general groups, such as readers of a trade or religious magazine, are not considered to be selected. Neither are groups of people in particular parts of the country who are, for example, targeted by a general poster campaign in their area.¹⁰

Any form of general marketing and promotion which doesn't fall into the categories above will also attract VAT. Other examples of standard-rated items are:

- Face-to-face fundraising
- Advertising or promotions on charity's own website
- Exhibition stands and space
- Commemorative items such as pens or adult clothing.

The Extra Statutory Concession (ESC) in more detail

This concession allows the following print items to be zero-rated when supplied to a charity:¹¹

- Collecting envelopes
- Pre-printed appeal letters
- Outer envelopes
- Reply envelopes

An appeal letter can be a single or multiple sheet letter; *the primary purpose of the letter must be a request for donations*; and it must be a letter, not just a form to fill in and return with a donation.

It can be personalised or unaddressed. Both outer and reply envelopes must either be over-printed with an appeal request related to that contained in the letter, or be clearly distinguishable from the charity's usual

stationery. So if a charity mail pack contains only these items, together with printed items that have always been zero-rated (leaflets, brochures, etc – see below for a more complete list), then the whole pack is zero-rated.

'Package Test Relief' in more detail

However, if a mailpack contains one or more standard-rated items, it may still be possible to gain full VAT relief using the *Package Test Relief* route.¹² The 'package test' can be applied in several ways:¹³

- If a pack contains more zero-rated than standard-rated items, then the pack as a whole can be zero-rated.
- If there are equal numbers of zero-rated and standard-rated items, the liability of the pack as a whole is decided by the cost of the elements. If the zero-rated items cost more, then the pack as a whole can be zero-rated.

The outer envelope is not taken into consideration when using the package test.¹⁴

A list showing the VAT liability of some common print items is given below in the section on 'Printed Matter Relief'. Charities have an advantage over commercial organisations in that they can use the Extra Statutory Concession to zero-rate appeal letters and reply envelopes as part of the package test.¹⁵

But remember this key point – *the package test can only be applied if the mailpack contains printed matter only*. The package test cannot be used as a possible route to a zero-rating if the pack contains anything which is not 'printed on paper or card', (e.g. a pen, audio tape, video cassette etc.) In these circumstances, the best that can be achieved is to avoid VAT on those elements of the pack that are zero-rated.

‘Printed Matter Relief’ – what is zero-rated and what is standard-rated?

If you are trying to achieve zero-rating through the package test, or if you are producing a ‘stand alone’ print item, you need to identify which items are zero-rated and which are standard-rated. This information is also needed when there is a need to apportion VAT on the items in a mailpack when using *ESC and Printed Matter Relief* to minimise VAT on a pack containing a non-print item.

Zero-rated	Standard-rated
Non-personalised letter*	Stickers
Leaflets	Photographs
Flyers	Greetings cards
Brochures	Certificates
Catalogues	Separate reply device
Newsletters	Bookmarks
Personalised letter**	Questionnaires
Reply envelopes**	Book covers
	Vouchers
	Bingo/competition cards
	Invitations, postcards
	Lottery or raffle tickets
	Printed pictures
	Pens
	Videos
	Audio cassettes

Generally it is fairly obvious what category something falls into. A more extensive list is given in Section 8 of VAT Notice 710/10. One area to watch for is that the surface area of a leaflet, brochure or flyer given over to a reply device is less than 25% of the total area. If it exceeds 25%, the item is no longer zero-rated.¹⁷

Summary

- if the marketing communication qualifies for *Charity Advertising Relief*, all services and supplies relating to the communication are zero-rated, and there is no need for the charity to single-source.
- most mailpacks can be fully zero-rated using *Package Test Relief*, but a charity needs to single source if it wishes to get preparatory services zero-rated as well.
- similarly, for mailpacks containing a non-print item which can only be partially zero-rated through *ESC and Printed Matter Relief*, the charity should single-source all those preparatory services relating to zero-rated elements of the pack. (It makes no difference if the preparatory services relating to the standard-rate ‘non-print’ item are single-sourced or not.)

*treated as a leaflet¹⁵

**only zero-rated for charities (under the Extra Statutory Concession and the package test for charities)¹⁶

Some common questions

Are doordrops and HDS treated in the same way as mailpacks?

Although they are unpersonalised, because of the element of selection by postcode – and as they are not ‘advertisements which are placed on someone else’s advertising time or space’ – they do not qualify for *Charity Advertising Relief*. But a charity should be able to get a full zero-rating on most doordrop packs through *Package Test Relief*. A leaflet which is being used as a doordrop should be designed to meet the *Printed Matter Relief* criteria – in particular, that any reply device is less than 25% of the total area of the leaflet.

What about inserts?

Inserts for charities always qualify for VAT relief under the Charity Advertising Relief rules, and are therefore zero-rated. This also means that the client can source services from several suppliers without worrying about VAT (and that the reply device doesn’t need to be restricted to 25% of the area of the insert).

What about a job that gets cancelled?

Intention is the key. If costs are incurred from a range of suppliers with the intention of producing a zero-rated ad or a zero-rated mail pack, then these costs can still be zero-rated.¹⁸

What about courier charges?

Our interpretation is that the test is whether the delivery charges are linked to the production of a zero-rated product. If so, then they can be zero-rated.

What are the differences between a leaflet (zero-rated), and a card (standard-rated) or a poster (standard-rated)?

In the words of the latest VAT Notice, whether a particular product qualifies as a leaflet ‘is a matter of fact and impression’. A leaflet is on ‘limp paper’, its finished size (folded or unfolded) should not be greater than A4, it conveys information, and should be intended to be held in the hand for reading by individuals (rather than hanging up for general display).¹⁹

References

- 1: Sections 4.1, 4.4, 4.5, VAT Notice 701/58, March 2002
- 2: A standard declaration is available in VAT Notice 701/58. Charities do not need to make subsequent declarations for repeat orders. A charity must also give its suppliers evidence that it is a charity.
- 3: Section 6.2, VAT Notice 701/10, August 2003
- 4: Section 6.4, VAT Notice 701/10, August 2003
- 5: Section 6.5, VAT Notice 701/58, March 2002
- 6: Section 3.1, VAT Notice 701/58, March 2002
- 7: Section 3.1, VAT Notice 701/58, March 2002
- 8: Section 3.3, VAT Notice 701/58, March 2002
- 9: Section 3.3, VAT Notice 701/58, March 2002
- 10: Section 3.2, VAT Notice 701/58, March 2002
- 11: Section 6.1, VAT Notice 701/58, March 2002
- 12: Revenue and Customs used to allow the VAT liability of a mail pack to be assessed through another test, whether there was a ‘significant’ item in the pack. A significant item was defined as something which, if it was removed from the pack, would make the remaining items meaningless or less useful. The VAT liability of the whole pack was then determined by that of the significant item. This significance test has now been dropped from the latest (August 2003) version of VAT Notice 701/10, Zero-rating of Books etc.
- 13: Section 6.5, VAT Notice 701/10, August 2003
- 14: Section 6.5, VAT Notice 701/10, August 2003
- 15: Section 6.3, VAT Notice 701/58, March 2002
- 16: Section 6.6, VAT Notice 701/10, August 2003
- 17: Section 3.4, VAT Notice 701/10, August 2003
- 18: Section 4.6, VAT Notice 701/58, March 2002
- 19: Section 3.3, VAT Notice 701/10, August 2003

VAT Notices are available online at www.hmrc.gov.uk

Disclaimer

The VAT legislation is complex and subject to differing interpretations. This document gives Brightsource’s interpretation. Our long experience in print management for charities means we are confident that this briefing paper is accurate and authoritative. However, we cannot take responsibility or be held liable for the application of this interpretation by other organisations.

Brightsource is a full service print management company. We offer a unique combination of expertise in direct marketing campaigns, unrivalled experience in the charity sector, a personal and bespoke approach to client service, and transparency in terms of our remuneration. We offer free advice on VAT mitigation, and offer a single-sourcing service to our clients in order to manage their exposure to VAT.

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