

# VAT and Scotland's Deposit Return Scheme (DRS)

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## Executive Summary

Scotland's DRS is to be launched on 16 August 2023.<sup>1</sup> Since the Scottish Government first committed to a DRS, there has been much confusion surrounding the application of VAT, with APSE being one of the earliest and loudest advocates for clarity on the issue.<sup>2</sup> (Please read our February 2022 report [Deposit Return Scheme: Lessons from Scotland and implications for the rest of the UK](#) for more information).

On 14 February 2023, the Scottish Government published a letter confirming VAT will not be charged on redeemed deposits in the deposit return scheme (DRS) for drinks containers. However, the letter confirmed VAT will be payable on the 20p deposits that have not been redeemed, with the producer liable for the tax.

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<sup>1</sup> <https://depositreturnscheme.zerowastescotland.org.uk/fags#:~:text=About%20the%20scheme,-What%20is%20a&text=They%20work%20by%20charging%20anyone,consumers%20on%2016%20August%2023>.

<sup>2</sup> <https://apse.org.uk/index.cfm/apse/news/articles/2022/the-deposit-return-scheme-what-local-authorities-think/>

The letter explains that Minister for Green Skills, Circular Economy and Biodiversity, Lorna Slater MSP, received a letter from Financial Secretary for the Treasury, Victoria Atkins MP, confirming that “wherever a container is returned for recycling, and the corresponding deposit is redeemed, VAT will not be applied to the deposit amount”. The letter then goes on to state that VAT will be “due on deposits that have not been redeemed, with the liability falling on the producer who originally issued it.”

The letter was published alongside a factsheet which, according to the Scottish Government, was issued by the Treasury outlining the UK government’s stance on the issue. The factsheet noted that “*a definitive description of future VAT rules... will be published following Spring Budget 2023... Stakeholders will have an opportunity to comment on the effectiveness of new rules when a technical consultation on the required secondary legislation is published at Spring Budget 2023.*”

On 29 March, the UK Government published this technical consultation detailing how VAT will be accounted for under statutory deposit schemes.

This briefing provides a catalogue of recent announcements on the issue of VAT on deposits, including the:

1. Letter from Lorna Slater MSP.
2. Treasury factsheet.
3. Draft UK Government legislation detailing how VAT will be accounted for under statutory deposit schemes.
4. Scottish Government’s request for a DRS internal market opt-out.
5. APSE’s comment on the VAT decision.

## **1 Letter to HM Treasury from Lorna Slater MSP<sup>3</sup>**

Below is the letter in response to UK Government confirmation of how VAT will be applied to Scotland’s Deposit Return Scheme. It was sent on 13 February 2023 and published on 14 February 2023.

*To: HM Treasury*

*From: Minister for Green Skills, Circular Economy and Biodiversity, Lorna Slater MSP*

*13 February 2023*

*Dear Victoria,*

*Thank you for your letter of 10 February regarding the application of VAT in relation to Scotland’s Deposit Return Scheme (DRS).*

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<sup>3</sup> <https://www.gov.scot/publications/deposit-return-scheme-letter-to-hm-treasury-february-2023/pages/text-of-letter/>

*Your letter confirmed that, wherever a container is returned for recycling, and the corresponding deposit is redeemed, VAT will not be applied to the deposit amount but VAT will be due on deposits that have not been redeemed, with the liability falling on the producer who originally issued it.*

*We welcome this decision which will give businesses the long needed clarity they have been asking for in order to prepare for the launch of Scotland's DRS in August.*

*Information will be published on the Scottish Government's website, and we will work with Circularity Scotland, the scheme administrator, and industry to ensure this information is communicated to businesses.*

*I understand the UK Government will formally announce the changes, including further details, in the spring budget.*

*Kind regards,*

*Lorna Slater*

## **2 HM Treasury factsheet on accounting for VAT on deposits<sup>4</sup>**

Below is the factsheet from HM Treasury on accounting for VAT on deposits issued under statutory Deposit Return Schemes (DRS). The factsheet was published alongside Lorna Slater MSP's letter on 14 February 2023.

*The UK Government fully supports the environmental objectives of the Scottish Deposit Return Scheme (DRS) and is committed to ensuring that the DRS functions effectively. The Government want to make it as easy as possible for customers to return their bottles under the scheme and for businesses to redeem their deposits.*

*This factsheet sets out how we envisage the VAT rules functioning. This anticipates changes to the VAT rules which will be announced at Spring Budget 2023. However, the UK Government recognises the need for early engagement with participating businesses to ensure that they're able to begin making the system changes required to comply with scheme rules ahead of the scheme going live on 16 August 2023.*

*Businesses should use this fact sheet as a guide to assist them in preparing for future legislative changes, rather than as a detailed description of the changes. For a definitive description of future VAT rules, we urge businesses to refer to legislation and detailed guidance that will be published following Spring Budget 2023. Stakeholders will have an opportunity to comment on the effectiveness of new rules when a technical consultation on the required secondary legislation is published at Spring Budget*

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<sup>4</sup> <https://www.gov.scot/publications/deposit-return-scheme-letter-to-hm-treasury-february-2023/pages/vat-and-the-deposit-return-scheme/>

2023.

HMRC expects the rules to operate as follows:

1. *At the point of sale, no business will account for VAT on the deposit amount.*
2. *VAT will be due only on unredeemed deposits that are associated with unreturned containers.*
3. *Only the first person in a supply chain (referred to as producers) charging a DRS deposit will have to account for VAT on unredeemed deposits, and only if their supply of the drink was standard rated.*
4. *No other businesses further along the supply chain, such as wholesalers and retailers, will account for VAT on deposits at any point.*
5. *Producers will calculate the VAT due on unreturned deposits based on their total DRS sales less DRS returns, in accordance with VAT regulations expected to become law in the early summer.*
6. *To facilitate this, information on returned products will need to be collected at return points and passed to producers. A producer may contract with a scheme administrator to collect containers and manage deposits who will then provide them with this information.*
7. *Producers will then use this information to account for the VAT due on unredeemed DRS deposits on their VAT return.*
8. *If containers are returned in a subsequent VAT period they will be included in the next calculation, so overtime the correct amount of VAT will be accounted for to HMRC.*

### **3 Draft regulations: VAT provisions for drink deposit return schemes<sup>5</sup>**

As noted in the factsheet, the necessary changes to the VAT rules are included in the Spring Finance Bill 2023 (at clause 314, which introduces new sections 55B, 55C and 55D to the Value Added Tax Act 1994).<sup>6</sup> According to the Government website:

*The 2023 Spring Finance Bill introduces legislation on how VAT will be accounted for when deposits are charged under statutory deposit schemes. It will provide for the exclusion of the deposit amount from the taxable amount when qualifying sales are made and require that VAT is only accounted for on the deposits of drink containers that are not returned.*

*It also establishes who must account for that VAT and provides for regulations to be made to establish*

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<sup>5</sup> <https://www.gov.uk/government/consultations/draft-regulations-vat-provisions-for-drink-deposit-return-schemes>

<sup>6</sup> <https://bills.parliament.uk/bills/3435/publications>

*when and how they must do so. We are consulting on these regulations.*

*The regulations are intended to provide for:*

- *Definitions of certain terms used.*
- *The method by which businesses required to account for VAT on unreturned deposits must do so.*
- *Additional rules for businesses that cannot distinguish returned containers of a product that was sold both with and without VAT (eg because some supplies of that product were made in a tax warehouse and some in free circulation).*
- *Error correction.*
- *A tax point for deposit scheme administration services.*

*A VAT notice containing additional rules will be published in due course.*

The UK Government are consulting on these regulations and the consultation closes at 11:30pm on 17 May 2023. More information can be found [here](#).

## **4 Scottish Government's request for a DRS internal market opt-out**

Pursuant to the draft regulations on VAT provisions for deposit return schemes, the cost of the deposit will initially be met by the producer, who will have to add 20p to every product before it is sold. Because that would mean different prices for the same products on either side of the border, it requires an opt-out from the Internal Market Act.

The Scottish Government have therefore made a request for an exemption. A UK Government spokesperson said the request was received by the Inter-Ministerial Group for Environment, Food and Rural Affairs on 6 March 2023.

Should the UK Government deny the request for an exemption, this would mean that the DRS rules would only apply to drinks bottled in Scotland, which would "which would leave Scotland-based producers at a disadvantage."<sup>7</sup>

According to media reports, the Scottish Secretary is currently in discussions with cabinet colleagues about rejecting the plea.<sup>8</sup> This would delay the rollout of the scheme in Scotland until 2025, concurrent with the rollout of the scheme across the UK.

To date, no decision on the opt-out has been made by the UK Government.

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<sup>7</sup> <https://www.bbc.co.uk/news/uk-scotland-64624421>

<sup>8</sup> <https://www.heraldscotland.com/politics/23381947.uk-government-set-refuse-drs-internal-market-opt/>

## 5 APSE Comment: Avoiding a tax on recycling

In APSE's report [Deposit Return Scheme: Lessons from Scotland and implications for the rest of the UK](#), published in February 2022, APSE made the following recommendation for UK and Scottish governments on the matter of VAT on deposits:

*"We would respectfully request that the Scottish Minister for Finance and the Economy, Kate Forbes, MSP and Lorna Slater MSP, Minister for Green Skills, Circular Economy and Biodiversity write to their counterparts in Westminster to demand an urgent resolution to this matter."*<sup>9</sup>

Notwithstanding the fact that, at the very least, it has brought some long-needed clarity to the issue of VAT on deposits, APSE welcomes the Treasury's announcement on VAT as it resolves the three substantive issues with VAT application APSE had raised in our aforementioned report:

1. The complexity of VAT on returned articles adds an unnecessary burden in administering a scheme, which is designed to help support a circular economy. Adding VAT to returned articles would run counter to the stated public policy intentions of both the Westminster and Scottish governments.
2. VAT on returned articles may generate an additional burden on consumers dependent upon the point at which the VAT is charged. Should this translate to additional charges to consumers, then it is de facto a perverse form of taxation on consumers who choose to do the right thing and participate in the scheme.
3. The price point of 20 pence on returned articles was not an accidental conclusion or figure. This is a round sum and can easily be commuted by consumers, e.g. 'If I return 5 bottles I will receive a £1 back'. If VAT is top sliced from the sum it risks breaking the psychology of the price point of 20 pence, and its ease of multiplication on returned articles.

The APSE research team took the liberty of checking the VAT position on similar schemes emerging in Europe. It would appear that a value added tax on returned articles has not been implemented elsewhere based on communications with European researchers/academics. Whilst the principle of 'producer pays' has led to some price increases passed on to consumers in terms of the product costs, consumers have not been expected to pay a value added tax on 'doing the right thing'. This appears to be a counterintuitive measure, which might be best described as a 'tax on recycling'.

By following the recommendations put forward by APSE in February 2022, this 'tax on recycling' appears to have been avoided by the UK and Scottish governments.

It remains to be seen whether the UK Government will exempt the DRS from the operation of the UK Internal Market Act. If it refuses, it is debatable whether Scotland's DRS scheme will be able to go ahead as planned.

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<sup>9</sup> <https://apse.org.uk/index.cfm/apse/research/current-research-programme/the-deposit-return-scheme/>

In any event, England, Wales and Northern Ireland are expected to introduce a DRS in 2025 (and if Internal Market Act approval is not forthcoming then Scotland will presumably join the UK-wide approach). The new VAT regime will apply equally to DRS schemes introduced anywhere in the UK so, sooner or later, producers, retailers and those involved in waste collection will have to fully understand the new scheme.

For those involved in local authority waste collection, APSE are here to help. The take-up of APSE's 2022 VAT recommendations by Scottish and UK governments demonstrates the extent to which APSE are at the forefront of ensuring local authority voices are heard at the highest level. Through our network of over 250 UK local authority members, APSE will continue to make the case for the full involvement of local authorities in the rollout of these schemes.

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