


VAT for schools and colleges



The VAT law applicable to schools and colleges can be confusing and, even whether or not a school is registerable, is not straight forward. This article covers some VAT aspects that affect schools and colleges.

VAT can be an overhead

VAT is neutral to businesses that are fully within the VAT regime. However those that are not in business, usually referred to as being “outside the scope” and those that whilst in business have transactions that are classified as exempt recover very little or none of input VAT on their purchases.

Qualification for exempt education

For supplies of education to be exempt it is not necessary to be a charity. Education is exempt if it is supplied by an eligible body. Eligible bodies include schools within the meaning of the Education Act, UK universities, colleges or halls of such universities, further/Higher Education bodies, Government Departments/Local Authorities, bodies which are precluded from distributing profits; and where profits must be devoted to the exempt education, and bodies which teach English as a foreign language.

Relevance of being a charity

The construction of a charitable or residential building is zero-rated. It is therefore advantageous to have a new building classified as a “charitable building” because VAT would not be charged on the cost of construction.

As VAT only applies to business transactions, the uninitiated would assume that a school run by a charity is not in business, but this is not so for VAT purposes. A school supplies education which is treated as a business activity for VAT purposes, unless it is funded by a Local Authority or Government Department, in which case it is regarded as a non-business activity.

Are schools charitable buildings?

When VAT was a relatively new tax, this aspect was tested in the Courts and cases still arise. Customs have said that any building, such as an assembly hall at a fee-paying school would be deemed for VAT purposes to be a business, as would a sports hall at a Foundation School that is regularly made available to the wider community for a charge, even if it is not a profitable activity.

However, there have been cases where the charity has successfully argued that its activities were not an “economic activity” for VAT purposes. For example in Yarburgh the Chancery Division held that zero-rating applied to a supply to a charity of a building which was then rented out at a nominal rate for use by a playgroup.

This judgment was followed in the case of St Paul’s Community Project where the court held that the use of certain parts of premises for running a day nursery was not business premises, so that construction work was zero-rated.



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Whilst some cases have moved the boundaries, Customs regard the facts of such cases as unique and their first stance is always that fees for education is a business activity. VAT will therefore be added to the cost of constructing a new building which is likely to be substantially irrecoverable.

If a school building is let out to third parties, it may be possible to “opt to tax” the rental income and thereby recover a proportion of the VAT on the cost of construction under the Capital Goods Scheme.

The cost of new residential building such as school boarding houses or university halls of residence would normally be zero rated for VAT, provided at least 95% of the floor area of the building is for residential purposes.

Fundraising by charities

The Children’s Society case resulted in a successful argument that the aim of fundraising was to obtain funds for the general purposes of the charity. Consequently the VAT on the costs of raising the funds was recoverable in proportion to the taxable business supplies to the total.

Therefore if a charitable school pays a fundraiser, say, £200,000 plus VAT to raise funds and 30% of its activities are VAT-able (standard or zero-rated) then in principle, and in simple terms, it would be able to recover 30% of the VAT on the fundraisers costs.

Other income

Exemption from VAT applies to items of income which are closely related to education. HMRC list the following as items that would not be exempt and would require registration if the total income exceeds the registration limit: sales of goods from school shops, campus shops and student bars,

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sales from vending machines, separately charged laundry, sales of uniforms and sports clothing (clothing designed for children, would be zero-rated), admission charges to plays, concerts, dances etc. (although these may well be exempt as either cultural or fundraising activities), fees and commissions from an external party permitted to use the premises or do its own business within the school.

Many schools and colleges therefore have significant amount of VAT-able income and should consider whether it is necessary to register for VAT if income from such sources may be approaching the VAT registration threshold.

Partial exemption

Schools will usually try and maximise the amount of revenue they receive from outside sources which hopefully will be predominantly VAT-able (standard or zero-rated). The school has to have a method of recovering a proportion of input tax on its costs and if this is based on anything other than income the method needs to be agreed by Customs. Customs will seek to reduce the percentage as much as possible and the school will argue that it should be higher.

There is a self certifying mechanism which requires taxpayers wanting a new agreement to declare that the method is fair and reasonable. Customs have a right to challenge the basis at a later date. Since it can be very subjective and there can be more than one method that gives a fair and reasonable result, it is easy to see how disputes with Customs may arise.

Foundation schools and Academies

Local authorities have a special method for recovering VAT on their costs. When the governors of a Foundation School make a purchase acting as the agent of the Local Education Authority (LEA), or use funds donated to the LEA, they can recover VAT on the costs. The LEA must meet certain conditions that it is not possible in a brief article such as this to cover but can be found on the HMRC website. There is no recovery of input VAT in respect of any grants the Foundation School receives for construction works direct from the Department for Education, rather than the LEA. This is because such funds belong to the governors and not the LEA.

Academies are independent of the Local Authority but can now recover the VAT on costs relating to their primary purpose activities by claiming this directly from HMRC.

Caution

VAT for the education and Charity sector is a very wide and complex subject and cannot be covered in great detail in a short article. Therefore it is important that you seek specialist professional advice to ensure that you maximise your assets and minimise the risk of getting it wrong.

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