

Potential change in VAT rules for education

Here at CT we've been working closely with our independent school clients to help them better understand the potential impact of manifesto proposals prior to the next general election.

What is being proposed?

One of the policy proposals being put forward by the Labour party is to remove the VAT exemption on supplies of education (and other closely related supplies) by independent schools which allows such organisations to exempt school fees.

Initially it was also part of the proposal to withdraw charitable status from private education institutions which would potentially come with other tax changes for private schools such as the eligibility to claim gift aid on donations. However, this proposal has been withdrawn.

Impact on independent schools

The removal of the VAT exemption would mean a large proportion of income received by independent schools would become 'taxable' and would require most independent schools to register and account for VAT on school fees. The main impact of this would be added VAT to school fees, but also potentially other services closely linked to education such as meals, boarding/accommodation, school trips and other school activities which have traditionally been seen as being incidental to the provision of education and this is outlined in HMRC's current guidance.

VAT registration allows businesses and organisations to recover VAT on expenditure to the extent that taxable income is received. This would be of benefit to any school that registers for VAT, and most schools have considered how much this VAT recovery position could offset the addition of VAT on fees and other activities. In our work with independent schools, we've been assessing how much VAT would need to be passed on to parents paying the fees. Registering for VAT may also open up opportunities to recover VAT on historic capital costs as well as ongoing maintenance, repairs and overhead costs.

Is there anything schools can do now?

Some of the initiatives considered by independent school to help mitigate the impact of VAT include allowing parents to pay for multiple terms in advance. Other potential ideas include splitting out the various services provided by schools to take advantage of other VAT reliefs and exemptions.

All of the above proposals and more will require careful consideration to ensure that independent schools do not fall foul of future legislation as well as avoiding any action which could potentially have a negative impact on internal procedures for schools.

Main Obstacles & Challenges

Fees in advance

We have advised clients who are considering payment in advance schemes that future legislation could include anti-forestalling measures which could catch any early payment of fees before the VAT charge comes into effect. This commonly accompanies legislation where there is going to be an advance change in VAT rate or the treatment of a particular supply of goods or services. It is usually designed to ensure that there is no large scale avoidance or abuse. Whilst it is not certain yet whether this would be introduced, we would recommend that any school considering this measure explains the risk to parents willing to pay in advance like this.

Splitting services

Because education and its closely connected services have been a settled area of VAT law for decades, it's never been fully tested whether these other closely connected services might qualify under some of the other exemptions with VAT law such as the welfare exemption. We expect that schools will seek to challenge this should the law be changed, particularly in relation to board and accommodation, trips and after-school clubs. There is also a measure which reduces the effective VAT rate on short term accommodation where this is for 28 days or more so there may be scope to utilise this provision to limit the amount of VAT that would need to be passed on to parents.

Our advice to schools at present is to investigate whether it would be feasible, in accounting terms, to split the income it receives from parents into distinct areas so it might be possible to take advantage of any other exemptions or reliefs should school fees be made subject to VAT.

How can CT help?

As part of our work we've been outlining what the potential financial impact these proposed VAT changes might have on independent schools and their financing. This has allowed our clients to improve their understanding of how the potential VAT cost to parents can be best managed and reduced to a minimum, as well as insulating the body to be in the best position possible should these changes come into effect.

As stated, with potential for VAT registration also comes opportunities for our clients such as the potential for VAT recovery. Part of our work has included providing an overview of an organisation's likely VAT recovery position by undertaking a modelling exercise which can be used as a guide to minimise the overall VAT bill on the organisation itself and the parents.

If you consider that your school or organisation would benefit from discussing these proposals further or if you would like to receive a quote for our services, we would be delighted to hear from you.

Please contact our specialist VAT team at VAT@ct.me or call our VAT Director, Iain Masterton on 0131 558 5800.