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quality learning skills

VAT & FE

College Finance Directors' Group

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Registered with the Charity Commissioners

Editor: Jackie Mace
Designers: Dave Shaw and Pat Kahn
Printed by: Hobbs the Printers Ltd, Totton, Hampshire

ISBN 1 85338 531 X

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Foreword

Welcome

The concept of a guide to the application of value added tax in the further education sector was initially instigated by talks within the Colleges Finance Directors' Group. We originally envisaged a short booklet that would seek to bring into a single publication elements of the various HM Customs and Excise VAT publications that impact on FE colleges. We perceived a need for such a document, given the complexity and breadth of the VAT regime under which colleges operate. The final publication is 168 pages; this is perhaps a demonstration of the very real complexity of this subject.

A guide for FE

As noted, this guide is primarily for the FE sector. By that we mean FE colleges established under the Further and Higher Education Act 1992 in England and Wales, the Further and Higher Education (Scotland) Act 1992, and the Education (Northern Ireland) Order 1998. While created for the FE sector, it should also be of value to other non-profit-making bodies providing educational and/or vocational training services in the UK and, in particular, to those bodies that come within the eligible body definition laid out in Group 6 of Schedule 9 – *Bodies falling within the statutory exemption*. This guide can therefore be usefully read by schools, universities and other bodies providing educational or training services which are precluded from making distributions and re-apply profit made to the continuance or improvement of such supplies.

In the United Kingdom, the FE sector is currently funded by Government through divergent mechanisms. In England, funding comes through the Further Education Funding Council, in Wales through Further Education Funding Council of Wales, in Scotland from Scottish Further Education Funding Council (formerly known as Scottish Office Education and Industry Department), and in Northern Ireland from the Department of Education Northern Ireland. Each has its own funding process and through such has its own methodology and descriptors for the funding provided. This guide has been based on the descriptors presently existing in England, but the reader will be able to recognise and, if necessary, convert the terms to those applying to their particular environment.

The guide is not written for the complete VAT novice. It assumes a basic level of comprehension of how the VAT system works. Any reader without this knowledge is directed as a starting point to *The general guide to VAT*, publication reference 700 – available from your local VAT office. The guide may be particularly useful to readers with sound experience of VAT in a standard-rated commercial environment who need to broaden that experience to fit the FE sector. We hope it will be an early point of reference for all college finance managers.

The guide has been published in loose-leaf format with the specific intention of updating it in future. Whether updates follow will depend on the reaction to the guide from the FE sector. To this end, the co-authors and editors would be pleased to receive your feedback and input, especially where there are any errors or inconsistencies and areas where more/less information is required.

This guide has been written purely for information and reference. It represents the contributors' understanding of facts and positions at the time of writing. It is not and has never been intended as a tax planning document. From to time to time in the text, there are statements to the effect that a particular point is complex and that you should seek further advice. This comment has been inserted by the contributors on the basis of their expertise. You are reminded that advice can be obtained from both HM Customs and Excise and your professional adviser.

Overview of the FE VAT position

Business and non- business activities

The VAT position of colleges is complicated since certain activities are undertaken as a statutory function and colleges cannot charge fees for tuition. Those activities which are wholly funded by grants are not undertaken in furtherances of business and are called 'non-business' in VAT terminology. Such income sources are outside the scope of VAT.

The activities of a college which are funded by fees, contracts and sale of goods and services are those which are in furtherance of business. In providing goods and services which are in furtherance of business, the college is making a supply. A supply of goods is where exclusive ownership passes from one person to another, whilst a supply of service is where payment in money or kind is made.

The fact that colleges are charities does not affect whether an activity is pursued in furtherance of business or not. HM Customs and Excise and the courts have agreed that the provision of education in return for tuition fees is a business activity. As is noted below in greater detail, education fees earned by colleges are exempt from VAT, however exempt income is still generated by a business supply.

Eligible bodies

Where normally the provision of education including training and examination is being made by way of business by what is called an eligible body it is exempt from VAT. A full list of those organisations that are treated as eligible bodies is at Appendix 9. For the purpose of this guide, it is important to note that FE colleges are eligible bodies. However, subsidiaries of colleges are not eligible bodies unless, in the unlikely situation, they are non-profit-distributing educational charities in their own right.

The VAT law that exempts the provision of education and training also exempts income generated from goods and services which are closely related to education when provided by the eligible body directly to its students. The exemption also covers goods and services closely related to education provided by one eligible body to the students of another eligible body.

Definition of education

The term 'education' is not defined in the VAT law and therefore should take a wide meaning. HM Customs and Excise anticipate that the process of 'education' involves a student being taken through a learning path directed by the lecturer or tutor. Education involves lectures, seminars, conferences and tutorials.

The exemption for education is broad and is not limited by any of the following:

- Duration
- Subject or requirement to take an examination
- Price or profit
- Location (assuming it takes place in the UK).

Consultancy

An issue to be aware of is that there is a grey area between education and consultancy. The provision of consulting services is not exempt.

HM Customs and Excise view consultancy as a general advisory, problem solving and offering services like, for example, the following:

- Materials testing
- Writing software or developing products or processes
- Business efficiency and needs studies
- Collection of statistics and market research information.

Training

It is worth noting that there is a separate and specific exemption for training ultimately funded by UK Government. This exemption applies to funding provided, for example, by TECs and the FEFC. The exemption for Government-funded training applies to the provision of services ultimately funded by Government and therefore applies regardless whether the trainer is an eligible body.

VAT recovery

The VAT a college incurs on expenditure, including capital purchases, is reclaimable to the extent that it can be attributed to taxable income. Such attributable VAT is known as input tax.

As noted above, colleges have varied income sources, primarily either outside the scope of VAT or exempt from VAT. Consequently, the amount of input tax could be proportionally small since most VAT on expenditure will be attributable to non-taxable income.

The recovery of VAT depends on being able to identify input tax directly attributable to taxable income and also on the method of apportioning VAT between non-businesses, exempt and taxable activities.

Chapter 3 defines input tax and goes on to discuss alternative methods of recovery. There is no prescribed method of VAT recovery, the most efficient of which could vary according to individual circumstances.

Acknowledgements

HM Customs and Excise consider this publication to be a useful guide on VAT and its effect on the FE sector.

We are grateful to HM Customs and Excise for their agreement in allowing this guide to reproduce extracts from official public notices. In particular, we acknowledge the assistance of HM Customs and Excise Government and Education Policy Division, London, and the Cambridge VAT Office Centre of Expertise and their respective colleagues.

The guide does not contain any special concessions, nor does it constitute a binding agreement with HM Customs and Excise. The guide is based on generally accepted principles and the legislation and published case law as at August 1999.

Finally, the Editors must thank the contributors for their unstinting efforts in producing their sections of the guide. Contact addresses and phone numbers for these contributors are provided in Appendix 10. In alphabetical order, they are:

- Andrew Baker of Davies Mayers Tax Advisers*
- Ian Reid of Arthur Andersen
- David West of Ernst & Young
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*When work on the guide began, Andrew Baker was head of KPMG's VAT services to colleges up to January 1999.

1 Income

1·1 Introduction

The purpose of this chapter is to give guidance on the VAT treatment of the income sources a typical college is likely to encounter.

1·2 Grant income

1·2·1 **FEFC grant – recurrent** *Outside the scope*
Grant income provided by the FEFC on behalf of the DfEE for the provision of education and vocational training for full-time students who have a statutory right to receive free education.

1·2·2 **FEFC grant – capital** *Outside the scope*
Now usually assessed as part of the recurrent grant, this relates to funds provided by the FEFC in respect of a specific capital development project.

1·2·3 **ESF grants** *Outside the scope*
European Social Fund monies provided by the European Commission, normally for a specific project in connection with a vocational training or employment initiative.

1·2·4 **ERDF grants** *Outside the scope*
Similar to ESF grants, the European Regional Development Fund is grant funding, again received from the European Community, relating to employment initiatives specifically aimed at regions with high unemployment.

1·2·5 **HEFCE** *Outside the scope*
Grant income received from the HEFCE for students enrolled by colleges for HE courses, e.g. HND, HNC, etc.

1·2·6 **Restructuring grant** *Outside the scope*
Now being phased out, this is specific grant funding from the FEFC to colleges, in respect of redundancy costs following colleges move out of local authority control in 1993.

1·2·7 **YT grants** *Outside the scope*
Now known as Modern Apprenticeships, money received by colleges usually from the TECs for providing vocational training to school leavers and other youngsters as part of a government training programme.

1·2·8 **Miscellaneous grants** *Outside the scope*
Income received from any other bodies, governmental or otherwise, where the provider is funding education or training, but receives no benefit.

1·3 Education fees

1·3·1 Tuition fees – students (full- and part-time) *Exempt*

Income received for the provision of education or vocational training received for all students who do not qualify to receive free education. The definition of education is very wide ranging and covers a structured learning programme provided over a period, regardless of any recognition or qualification being obtainable. VAT liability is unaffected by whether the fee is paid by the student, employer or local authority.

1·3·2 Tuition fees – full-cost courses for businesses *Exempt*

Courses specifically designed for or commissioned by businesses for their employees. VAT liability is unaffected by whether there is a profit motivation intended or realised.

1·3·3 Tuition fees – overseas students *Exempt*

Income received from non-UK students for the provision of education and vocational training, regardless of age or whether the course is full- or part-time.

1·3·4 Tuition fees – EFL *Exempt*

Income received from UK and non-UK students for an EFL course, whether held during the normal term time or vacation periods. VAT exemption covers the whole course package, including accommodation and catering, whether supplied in-house or bought in, but the provision of extra curricular events and trips may lead to a VAT liability under the Tour Operators Margin Scheme (TOMS) (see 1·5·10).

1·3·5 Distance learning *Exempt*

Fee income received from students enrolling in a distance learning package is VAT exempt provided the student is subject to assessment by the college, otherwise the income will be subject to VAT. The exemption covers all materials sent to the student (although fully printed matter may be treated as zero-rated if paid for in addition to the course fee).

1·3·6 Registration fees *Exempt/non-business*

Fees charged to students, whether fee paying or non-fee paying, for administration of registration/enrolment application.

1·3·7 **Examination fees – college** *Exempt*
Fees charged by a college to its enrolled students to take part in an examination organised and supervised by the college.

1·3·8 **Examination fees – examination board** *Disbursement*
The college is acting as agent of the examination board in the collection of its fees. Income collected does not therefore belong to the college, but the examination board, and should be excluded from the college's VAT accounting records. Any administration or handling charge collected from the college students (or the examination board) would qualify to be VAT exempt.

1·3·9 **Conferences/lectures/symposia, etc.** *Exempt*
VAT exemption for supplies of education and training made by colleges extends to the above supplies when organised by or on behalf of the college, provided the supply has an educational motive.

1·4 Teaching contracts and training income

1·4·1 HE franchise fees *Exempt*

HE franchise fees are an exempt supply by an FE college to an HE institution.

1·4·2 Access funds *Disbursement*

Funding provided by DfEE to provide financial assistance to students requiring such help for whatever reason, to enable them to complete their course.

1·4·3 Examination and accreditation service *Exempt*

Income received by colleges for examination and accreditation services or for the loss of their staff when being used by examination boards and similar organisations.

1·4·4 TEC projects *Standard-rated/exempt/outside the scope*

Special programmes devised and funded by local TECs for training or capital spend initiatives to assist the local employment environment would be outside the scope. Projects specially commissioned by the TEC would be exempt if a supply of vocational training and standard-rated in most other cases.

1·4·5 Workplace provider income *Standard-rated*

When unemployed students are placed with a work provider as part of a vocational training course, any income received by the college, either directly from the work provider or through retention of the student daily allowance, is subject to VAT as a deemed supply of staff by the college.

1·4·6 Job Club *Standard-rated*

Regarded by HM Customs and Excise as advisory services rather than a supply of education/training and therefore failing to qualify for VAT exemption.

1·4·7 New Deal *Exempt*

Income received by colleges for the provision of vocational training programme using funds originating from the Employment Service is VAT exempt. Short courses and tasters are also VAT exempt if separately identifiable. Supplies of career advice and other guidance is subject to VAT.

1·5 Student non-fee income

1·5·1 Items sold to students in class *Exempt*

Any item sold to students in class which is relevant to or required as part of the course, qualifies to be treated as VAT exempt as a supply closely related to a supply of education/training. The hire to students of any equipment used as part of an exempt supply of education, will also qualify for VAT exemption.

1·5·2 Items sold to students and others in college shop

Standard-/zero-rated

HM Customs and Excise differentiate items sold in class from the same item sold in a college shop, whether the shop is operated by the college or franchised to a third party. Items sold will follow their normal VAT liability, i.e. standard-rated or zero-rated.

1·5·3 Book sales *Zero-rated*

All sales of fully printed matter (books, booklets, leaflets, magazines, newspapers, etc.) are zero-rated for VAT purposes. However, zero rating is restricted to printed matter and therefore items supplied on other forms of media (e.g. CD-ROM, cassette, etc.) are subject to VAT at the standard rate.

1·5·4 Library income – hire *Exempt/zero-rated*

Charges for use of library (resource centre) facilities are zero-rated to the extent that the charge relates to the use of books, but any charge for the use of any other facilities would be VAT exempt to students, standard-rated to any other persons.

1·5·5 Library income – fines *Zero-rated*

Normally regarded as a charge for the hire of books and therefore zero-rated, rather than being a compensation payment and therefore outside the scope of VAT.

1·5·6 Photocopier charges *Exempt/standard-rated*

Charges made to students for use of photocopiers in connection with course work qualifies to be treated as VAT exempt as a supply incidental to a supply of education/training. Charges to other users, including staff, are subject to VAT. In situations where a photocopier may be used by students, staff and others, the college has the option to account for VAT on all income received or estimate an apportionment based on a review of use covering a representative period. Printing of materials by a college on behalf of students would be VAT exempt if the supply does not qualify as zero-rated in its own right (see 1·7·7 and 1·7·8).

1·5·7 **Car park charges** *Exempt/standard-rated*
Charges made by a college to students for parking on college premises qualifies to be treated as VAT exempt as a supply linked to a supply of education. Charges to all other persons are subject to standard-rated VAT. This would include the hire of the whole car park to an operator at weekends, holidays, etc. even though it is the operator making the car park charge to the car owner (see 4·6·2·5).

1·5·8 **Nursery/crèche charges** *Exempt*
Fees charged by a college for crèche facilities are VAT exempt, whether the charge is made to students, staff or even third parties.

1·5·9 **Course trips** *Exempt*
Income received by a college from students travelling on an organised trip, which may or may not include supplies of accommodation, is VAT exempt if the supply is an integral part of the course being undertaken by the student. This remains the position, regardless of whether the college makes a profit from the supply, either intentionally or inadvertently.

1·5·10 **Other trips** *Standard-rated*
Any other trip organised by a college that is not regarded as being in the course of a supply of education is liable to VAT under TOMS. Under TOMS the college is required to account for VAT on the profit margin. The profit margin is calculated by reference to the difference between income received by the college from participants and the total cost of the items constituting the package (e.g. travel, accommodation, excursions, etc.).

1·5·11 **Bus travel to college** *Zero-rated*
Charges made to students for bus transport from home to college and back home is a zero-rated supply of transport when supplied by the college. The supply would qualify for zero rating even if made by the college to the local authority who make the onward supply to the student. Similarly the supply of bus transport by the bus company to the college would again be zero-rated (see 2·8).

1·6 Trading income – student based

1·6·1 **Restaurant meals** *Exempt/standard-rated*
Meals served in training restaurants run by students receiving vocational training are VAT exempt when supplied to other students of the college and subject to VAT when supplied to staff, visitors and members of the general public. VAT to be accounted from the gross takings received from non-students.

1·6·2 **Alcoholic drinks** *Standard-rated*
All sales of beers, wines, spirits, soft drinks, etc. sold with meals served in training restaurants, are subject to VAT regardless of whether the sale is to students or to others.

1·6·3 **Sales of prepared food** *Zero-rated*
Sales of meals and other food such as bread and cakes prepared by students which is intended to be consumed off the premises is zero-rated as a supply of foodstuffs.

1·6·4 **Hairdressing** *Standard-rated*
Supplies of hairdressing services by students receiving vocational training are subject to VAT when supplied to anybody being charged for the supply.

1·6·5 **Beauty therapy** *Standard-rated*
Supplies of beauty therapy services by students receiving vocational training are subject to VAT when supplied to anybody being charged for the supply.

1·6·6 **Motor vehicle repair** *Standard-rated*
Supplies of motor vehicle repair services by students receiving vocational training are subject to VAT when supplied to anybody being charged for the supply.

1·6·7 **Sales of items** *Standard-rated*
Any items that are sold separately to supplies provided in 1·6·4–1·6·6 will be subject to VAT, unless sold to a student for use in class (see 1·5·1).

1·6·8 **Travel agency commission** *Standard-rated*
Commission received by a college for travel services supplied by students receiving vocational training from a travel agency.

1·6·9 **Insurance commission** *Exempt*
Commission received by colleges from insurance companies for acting in an intermediary capacity between the insurer and the insured for a supply of insurance qualifies for VAT exemption.

1·6·10 **Sale of items produced in class (including agricultural and horticultural items)**

Standard-/zero-rated

Income received for sales of items produced by students as part of their classwork follows its normal VAT liability. Items produced in the course of most supplies of education/training will be subject to standard rate VAT but horticultural/agricultural colleges do produce many zero-rated items of foodstuffs as detailed below:

a. Zero-rated:
   - Cereals
   - Fruit
   - Vegetables
   - Dairy products
   - Meat and poultry
   - Fish
   - Live animals for human consumption
   - Animal feeding stuffs
   - Seeds
   - Culinary herbs

b. Standard-rated:
   - Wool
   - Flowers
   - Cider
   - Pet food
   - Thatching material.

1·6·11 **Sales of student concert/play tickets**

Standard-rated/exempt

The sale of tickets for performances by students are normally subject to VAT. However, VAT exemption is available if the performance qualifies to be treated as a one-off fundraising event (see 1·9·12).

1·6·12 **College ball/dance ticket sales** *Standard-rated/exempt*

Tickets sold for dances and similar events organised by a college on behalf of its students are subject to VAT when sold to students or any other person, unless qualifying as a VAT-exempt, one-off fundraising event (see 1·9·12).

1·7 Trading income – college

1·7·1 Conference facility hiring *Exempt/(standard-rated)*

The hire of conference facilities are normally VAT exempt as a licence to occupy land but subject to VAT if the college has elected to tax the building (see 4·7). The hire of any additional facilities such as lighting and sound equipment, OHP and laser projector, flipcharts, etc. is all subject to VAT.

1·7·2 Catering services *Standard-rated/exempt*

All supplies of catering services supplied by a college to outside parties are subject to VAT, unless supplied to another VAT-exempt educational institution making a supply of education to its students, in which case the supply would qualify for VAT exemption.

1·7·3 Accommodation services *Exempt/standard-rated*

Income received for accommodation services supplied to college students, candidates for admission, students of another eligible education institution qualify for VAT exemption. VAT exemption also applies to supplies to overseas students or students from non-eligible institutions if receiving education from the college making the supply. All other supplies of accommodation services are subject to VAT at the standard rate (see 4·6·2·3).

1·7·4 **Hire of sports facilities** *Exempt/(standard-rated)*
The hire of pitches, sports halls and other facilities for use for a sporting activity is subject to VAT at the standard rate. The supply is VAT exempt if the grant of the facilities is for:

- A period of hire exceeding 24 hours
- A series of ten or more periods, whether or not exceeding 24 hours, where the following conditions are satisfied:
  a. Each period is in respect of the same activity carried out at the same place
  b. The interval between each period is not less than one day and not more than 14 days
  c. Consideration is payable by reference to the whole series and is evidenced by written agreement
  d. The grantee has exclusive use of the facilities, and
  e. The grantee is a school, a club, an association, or an organisation representing affiliated clubs or constituent associations.

However, the supply reverts to being subject to VAT at the standard rate again if the college has elected to tax the sports facilities. All supplies to VAT exempt institutions will be VAT exempt if the hire is for the use of the institution's students in the course of a supply of education (see 2·9 and 4·6·2·6).

1·7·5 **Sport pay and play income** *Exempt/standard-rated*
Supplies by colleges to members of the general public for use of the college's sports facilities qualify for VAT exemption, regardless of whether the college has elected to tax the facilities. However, if the college operates a membership scheme for use of the facilities, fees paid by members are VAT exempt and income received from non-members is subject to VAT at the standard rate.

1·7·6 **Sports membership subscription** *Exempt*
As per 1·7·5, membership subscription fees received from members of the general public for the use of a college's sports facilities qualify for VAT exemption.

1·7·7 **Printing services – fully printed matter** *Zero-rated*
Supplies of the following items by a college printing department qualify for zero-rating when supplied to third parties: books, booklets, brochures, programmes, leaflets, pamphlets, magazines, journals, music, maps, etc. (see 2·3 and 5·2).

1·7·8 **Printing services – other** *Standard-rated*
Supplies of the following items by a college printing department are subject to VAT at the standard rate when supplied to third parties: stationery (compliments slips, letterheads, envelopes, etc.), posters, business cards, forms, invoices, etc. (see 2·3 and 5·2).

1·7·9 **Room hire** *Exempt/standard-rated*
Income received for hire of rooms for meetings and similar purposes is VAT exempt, regardless of the length of hire, subject to whether the college has elected to tax the building concerned. The hire of facilities within a room (e.g. computer or laboratory equipment) or separate charges for additional items to be included with room hire (e.g. OHP, flipcharts, etc.) are subject to VAT at the standard rate (see 2·9 and 4·7).

1·7·10 **Rental income** *Exempt/standard-rated*
Any other income not previously mentioned for the grant of an interest in land or buildings is an exempt supply for VAT purposes, subject to the college electing to tax the land or building concerned (see 4·7). Rental of domestic accommodation to caretakers and other staff is exempt from VAT.
Note. An election to tax does not apply to residential properties.

1·7·11 **Gaming machines** *Exempt/standard-rated*
Income received from the owner of gaming and similar entertainment machines is VAT exempt as a supply of a licence over land, subject to an election to tax made by the college. Where the college owns or hires the machine and is responsible for the takings received, the income is subject to VAT, even if the machine is situated in the student common room.

1·7·12 **Vending machine – sanitary and health items**
Standard-rated
Takings received from machines dispensing sanitary and health items are subject to VAT wherever the machines are situated on the college campus.

1·7·13 **Telephone call-box receipts**
Outside the scope/standard-rated
Money taken by a college from telephone call-boxes is only subject to VAT in certain circumstances and you should check with the telephone company before declaring VAT on such income. VAT is not due on the sale of telephone call cards.

1·8 Refectory and other catering income

1·8·1 Meals to students *Exempt*

Any catering supplied to students of the college or another educational institution whose students are receiving an exempt supply of education at the college, qualifies for VAT exemption. The exemption applies to catering supplied to students from any outlet operated by the college, not just the college refectory.

1·8·2 Meals to staff and visitors *Standard-rated*

Catering supplied to anyone other than students is subject to VAT at the standard rate. Where students and other diners share the same facilities and the catering staff are unable to differentiate the VAT liability of the sale at the point of sale, the college has the choice of either accounting for VAT on all takings or apportioning takings on the basis of an estimate. The estimate should be calculated by conducting a review of refectory takings for a representative period. The review should be of at least one week's duration and should be updated annually, using different academic terms and periods of the term each time.

1·8·3 Confectionery *Standard-rated*

All sales of confectionery sold to students or others, wherever sold on the college campus, are subject to VAT at the standard rate. Exceptionally, confectionery sold over the counter in a refectory to students may be treated as VAT exempt if the catering staff have no means of differentiating takings at the point of sale between sales of confectionery and supplies of catering.

1·8·4 Bar sales *Standard-rated*

All sales of alcoholic drinks are subject to VAT at the standard rate, whether sold to students or others, and wherever sold on the college campus.

1·8·5 Vending machine – confectionery and soft drinks *Standard-rated*

Confectionery and soft drinks sold from vending machines are subject to VAT at the standard rate, whether sold to students or others and wherever sold on the college campus.

1·8·6 Vending machine – snacks and hot drinks

Standard-rated/exempt

Snacks (sandwiches, pies, crisps) and hot drinks sold from vending machines are subject to VAT at the standard rate, wherever they are situated on the college campus. However, if HM Customs and Excise can be satisfied that a particular machine(s) is located where the only users are students (e.g. student common room) or the college is able to conduct an acceptable apportionment review of sales to students or others, the income may qualify to be treated as VAT exempt.

1·9 College income – other

1·9·1 Research fees – eligible bodies *Exempt*

Income received for a supply of research conducted on behalf of another institution qualifying to supply education/training VAT exempt will qualify for VAT exemption. However, the college will need to differentiate between supplies of research and consultancy services (see 1·9·3). Although the difference is not clearly defined, general guidance states 'research' is gaining or expanding knowledge, whereas 'consultancy' is exploiting knowledge previously obtained.

1·9·2 Research fees – non-eligible bodies *Standard-/zero-rated*

Research services supplied to any other customers will be subject to VAT at the standard rate. Services supplied to non-UK customers will be outside the scope with credit (the equivalent of zero-rated), unless supplied to EC customers who are private individuals or anybody not receiving the supply in the course of business.

1·9·3 Consultancy fees *Standard-rated*

Supplies of consultancy services are subject to VAT at the standard rate, regardless of to whom they are supplied. As per 1·9·2, the supplies are outside the scope of VAT with credit when supplied to non-UK customers, unless the customer is located in another EC member state and is a private individual or does not receive the supply in the furtherance of business.

1·9·4 Management fees *Standard-rated*

Income received by a college for a supply of management services to subsidiary or associate companies and third parties is subject to VAT. This would even be the case for supplies to overseas customers.

1·9·5 Royalties from EC-based payer *Standard-/zero-rated*

Income received from the exploitation of college intellectual property through the receipt of licence fees or royalties is subject to VAT at the standard rate. Income received from customers located outside the UK is outside the scope with credit (the equivalent of zero-rated), unless the customer is a private individual or is not receiving the supply in the furtherance of business.

1·9·6 Royalties from non-EC-based payer *Zero-rated*

Income received by way of royalties or licence fees is outside the scope of UK VAT with credit, which is the equivalent treatment afforded to zero-rated supplies.

1·9·7 **Staff hire** *Standard-rated/exempt*
The supply of staff by a college is subject to VAT at the standard rate, even when supplied to another VAT exempt eligible body institution. However, if the staff concerned are engaged to perform a specific supply of education/ training to the students of another eligible body the supply will qualify for VAT exemption (see 2·11).

1·9·8 **Sale of assets – land and property**
Exempt/(standard-rated)
The sale of any property owned by a college is a VAT exempt supply. However, the college may elect to tax the sale of any property (apart from residential premises) in which case the sale is subject to VAT at the standard rate (see 4·7).

1·9·9 **Sale of assets – other** *Standard-rated*
The sale of any college assets other than land and property are subject to VAT at the standard rate, even if the item is being sold as scrap. However, the following issues should also be considered.

- If no VAT was recovered on the item at the time of purchase there is no requirement to account for VAT on any sale proceeds.
- If the item was originally purchased second hand with no VAT charged, VAT on disposal need only be paid on the profit margin (if any), i.e. sale price less original purchase price.
- If the item being sold is a motor car, VAT need only be brought to account on the profit margin (if any), i.e. sale price less purchase price, even if the car was bought new with VAT charged on the full selling price.

1·9·10 **Minibus hire with driver** *Zero-rated*
Provided the minibus has a seating capacity of 12 or more, the supply of hire with driver qualifies as being zero-rated for VAT purposes, regardless of to whom the supply is being made.

1·9·11 **Minibus hire without driver** *Standard-rated*
The hire of a minibus without driver will be subject to VAT at the standard rate regardless of to whom the supply is being made.

1·9·12 **Fundraising events, e.g. open days** *Exempt/zero-rated*
Due to the college's charitable status fundraising events organised by them qualify for VAT exemption, regardless of whether the college retains the income or gives all or a proportion to a charity. VAT exemption only applies to one-off events e.g. annual open day, summer ball, etc. It is not available to a series of regular events, such as a monthly disco. The exemption applies to all income received in connection with the event including income that would normally be treated as standard rate, e.g. bar sales, car parking, etc. However, income normally zero-rated would continue to be zero-rated, e.g. programme sales.

1·9·13 **Sale of tickets for concerts/plays (non-student performers)** *Exempt/standard-rated*
The income from these types of events would normally qualify for VAT exemption under the criteria described in 1·9·12. Where those criteria are not met, the income would be subject to VAT at the standard rate.

1·9·14 **Sales of raffle tickets, lotteries, etc.** *Exempt*
Any income retained by colleges from various forms of betting and gaming activities (including bingo) qualifies for VAT exemption, provided the college is complying with all the necessary legislative conditions associated with such activities, otherwise the income received is subject to VAT at the standard rate.

1·9·15 **Sponsorship** *Standard-rated*
Money provided by a business to a college with the primary intention of receiving a promotional benefit is subject to VAT at the standard rate, whatever form the promotion takes.

1·9·16 **Advertising** *Standard-rated*
Supplies of advertising by a college in a prospectus, programme, hoarding, etc. is subject to VAT at the standard rate, unless it is from a charity which qualifies for zero rating.

1·9·17 **Donations/endowments** *Outside the scope*
This is income received by the college that falls outside the above category of sponsorship, i.e. it is money given to the college for which the donor, either corporate or individual, receives no intended or expected benefit. A minor benefit such as an acknowledgement in a programme or the naming of a chair would be insufficient to be regarded as sponsorship.

1·9·18 **Bank interest** *Exempt*
The receipt of any interest from the deposit of money qualifies for VAT exemption. If the money is deposited outside the EC, the income becomes outside the scope with credit.

1·9·19 **Dividend income** *Outside the scope*
Income received by way of dividend payment from shares bought in subsidiary, associate or third-party companies, is wholly outside the scope of VAT wherever the location of the company in which the college has purchased shares.

1·9·20 **VAT and tax refunds** *Outside the scope*
The receipt of a refund of VAT or other tax from HM Customs and Excise or the Inland Revenue is not income by way of business and is consequently outside the scope of UK VAT.

1·9·21 **Insurance claims** *Outside the scope*
The receipt of insurance payouts is outside the scope of VAT since the college is receiving compensation for loss.

1·9·22 **Award ceremony spin-offs** *Standard-rated*
Commissions from photographers, gown hirers or licences to take photographs or videos, and the sale of photographs and videos is standard-rated.

2 Charity and other VAT reliefs on expenditure

2·1 Introduction

This chapter explains what relief from VAT colleges may claim or should check to see if they have been correctly applied by suppliers. FE colleges are charitable corporations created under the Further and Higher Education Act 1992. They are exempt from registration with the Charity Commissioners and this is the answer you should give to suppliers who ask for a charity registration number.

As charities, colleges are able to claim relief from being charged VAT on a limited range of goods and services. Often, to make a claim, a certificate of status has to be given to the supplier to put them 'on notice' that relief applies. As charitable providers of education, otherwise known as eligible bodies, certain exemptions apply in relation to supplies colleges buy in from other eligible bodies, provided the goods and services are for the use of students.

2·2 Charity advertisements

Charities are able to claim zero rating for advertisements for the purpose of raising funds or making known the objectives of the charity. Consequently relief can be claimed for advertisements of fundraising events and to promote the charitable activities of a college.

Zero rating is available for advertisements in two categories of specified media, as follows:

a. The broadcast on television or radio, or the screening in a cinema of an advertisement
b. Publication of an advertisement in any newspaper, journal, poster, programme, annual, leaflet, brochure, pamphlet, periodical of similar publication.

It is noted that advertisements on or in any other media i.e. stationery, calendars, clothing, banners, etc. do not qualify for relief. The relief for advertisements includes the services used in connection with the preparation of a published (category (b) above) advertisement.

The zero rating of advertisements has in the past been an area that has caused confusion. Prior to 1 June 1996, by concession, HM Customs and Excise said job advertisements which carried a charity mission statement could qualify for zero rating. The law never provided for this and the concession was withdrawn following clarification by tribunal cases. HM Customs and Excise's guidance is that advertisements for staff vacancies, governor appointments and works contracts do not qualify for VAT relief since their main purpose is not to make known the college's objects. On a similar basis, a concession for stationery containing mission statements, was also withdrawn in September 1996.

HM Customs and Excise recommend that charities issue a certificate to claim zero rating of qualifying advertisements. The law is silent about the use of certificates. However, if a certificate is used, it must be used validly since incorrect declarations are potentially punishable by a fine equal to the tax not paid.
See Appendix 1 for a copy of a certificate.

2·3 Stationery and printed reading matter

As a general rule, stationery is liable to VAT at the standard rate. However, printed reading matter, like books, pamphlets, newspapers, periodicals, music, maps, leaflets and brochures, is zero-rated.

There can be a grey area between what is stationery, and thus liable to standard rate VAT, and zero-rated reading matter. For example, the courts have ruled that the following are standard-rated:

- Diaries
- Leaflets printed on card or laminated paper
- Books that contain a significant proportion of space available for writing or completion of forms (HM Customs and Excise untested rule of thumb is that if over 25% is available for completion, the document is stationery).

When an item qualifies for zero rating, if its design, production and delivery are ordered at the same time and under the same contract as its printing, the overall supply will be zero-rated. However, if these services are separately supplied, they are standard-rated.

Printed reading matter is generally zero-rated and consequently there is no requirement for a college to issue a VAT certificate. Reading matter on compact discs, microfilm and on the Internet does not, in HM Customs and Excise's view, qualify for zero rating.

2·4 Disabled access and alteration to buildings

Certain alterations to existing college buildings qualify for zero rating. The alterations have to improve disabled access and are advised to be notified to the supplier using a VAT certificate (see Appendix 2). The law provides for relief of the following:

- Chair or stair lifts designed for use in connection with invalid wheelchairs
- Construction of ramps or widening doorways or passages for the purpose of facilitating a handicapped person's entry to or movement in any building
- The service of providing, extending or adapting a bathroom, washroom or lavatory for use by handicapped persons in a building used for charitable purposes. This includes the installation of sanitary ware
- The supply to a charity providing a permanent or temporary residence or day centre for handicapped persons of services necessarily performed in the installation of a lift for the purpose of facilitating the movement of handicapped persons between floors in that building. This includes goods used in connection with the installation services.

Handicapped means chronically sick or disabled, and this includes the old and infirm. If a college provides to disabled students, either on loan or for sale, equipment solely designed for the disabled, the college can obtain the equipment zero-rated, for example, braille keyboards. The service of altering goods to make them suitable for use by a handicapped person also qualifies for zero rating.

2·5 New build residences and non-business buildings

The construction of a new building for use as residential accommodation for students is zero-rated, provided the user gives the builder a VAT certificate (see Appendix 4). The law requires the issue of a certificate to the builder. The construction of a new building for sole use for a non-business charity purpose is zero-rated, again upon certification (see 4·2·1). Non-business use means other than that which will generate a college, directly or indirectly, income from tuition fees and charges for lettings (see Appendix 9. *Glossary*).

2·6 Conversions of property and alterations to listed buildings

This VAT relief applies only in relation to residential buildings. If a non-residential building is converted into residential use, subject to several conditions, its sale onward is a zero-rated supply, thus giving rise to a right of recovery of input tax on conversion costs. To achieve the VAT relief required, a number of steps have to be taken and this is an area beyond the scope of this guide (also see 4·4·4). The approved alteration of a listed building which is already in residential use is zero-rated (see 4·8).

2·7 Fuel

The reduced rate of VAT (currently 5%) applies to fuel used for a qualifying non-business charitable purpose, residential accommodation and to small domestic use quantities. To obtain the reduced rate, a college is recommended to use a certificate to put the supplier on notice that the reduced rate applies (see Appendix 3).

The VAT Act lists the quantities of fuel which are automatically reduced rated because they fall within the domestic use threshold, e.g. less than one tonne of coal per delivery, 150 therms of gas per month, 2300 litres of gas oil per month or 1000 kilowatt hours of electricity per month.

Where a supply is partly for a qualifying use and partly not, the following rules apply:

- If at least 60% of the fuel is supplied for a qualifying use, the whole supply shall be deemed as qualifying
- In any other case, an apportionment shall be made.

The VAT position has to be assessed for each metered supply. For example, if electricity is measured as 50% for qualifying residential use and 50% for commercial use, then 50% would be liable to 5% VAT and the balance liable to 17·5% VAT. However, if in the example residential use was 61%, then the whole supply would be 5% VAT-rated.

2·8 Public transport

The provision of passenger transport in a vehicle that can carry 12 persons (including the driver) is zero-rated. The provision of transport assumes the services of a driver are included, otherwise the hire of a vehicle alone is standard-rated. The hire of coach transport should be zero-rated, while the provision of college minibuses and coaches can also be structured to obtain zero rating.

2·9 Accommodation hire

When a college hires sports facilities for a series of 10 or more sessions, i.e. on a block booking basis, this should be an exempt supply by the supplier (see 1·7·4). This assumes the supplier has not opted to waive the exemption (see 4·7).

Where colleges hire in the use of rooms, halls and property, it is worthwhile noting whether, when VAT has been charged, it has been correctly charged by the supplier. Normally, if VAT is being charged, the landowner will have made an election to tax or exercised an option to waive exemption. If necessary, you can ask a landowner to confirm whether an election has been made.

If on a field trip, a college uses accommodation owned and charged for by another eligible body, the charge to the college should be exempt if it is used by the college's students.

2·10 Training of the unemployed ultimately funded by Government initiatives

The provision of training and retraining for the unemployed under a UK Government sponsored initiative is normally VAT exempt, regardless of whether the trainer is an eligible body. The status of monies received from the TECs and the FEFC fall under this category. Consequently, if a college uses this funding to buy in training services from an outside provider, VAT should not be charged. The exemption does not, however, apply to any other goods or services bought with training money.

2·11 Staff hire

Where a college is hiring in staff, the VAT treatment of their payroll can vary according to the type of staff and the contractual arrangements.

2·11·1 Catering staff

If a college uses an external contractor to manage its catering facilities on an agency basis, the recharge of site specific payroll costs is accepted by HM Customs and Excise as a VAT-free redistribution of costs between joint employers. This treatment is concessional and does not apply to other types of staffing arrangements like cleaners or security staff.

2·11·2 Agency staff

If a registered agency providing a college with temporary staff, contracts to supply temporary employees under an agency contract, the payroll element will be charged free of VAT, while the management fee shall be liable to VAT. This treatment only applies to registered agencies and is due for withdrawal soon. It is noted some agencies will not separate their management fee from the payroll recharge and therefore they will charge VAT on the full value of their charge.

2·11·3 Teaching staff

If a college contracts another eligible body for the provision of teaching staff or for the provision of teaching services, this is an exempt supply.

2·11·4 Administration, technical or support staff

The separate provision of these staff is normally taxable unless supplied by a registered agency (see 2·11·2).

These points on the buying in of staff may apply in reverse to colleges providing staff to other organisations (see 1·9·7).

3 Input tax

3·1 Introduction

A college incurs VAT on a wide range of the supplies it receives. Although the initial funding of FE colleges by the FEFC when they vested in 1993 was aimed at compensating them for the VAT cost, subsequent funding rounds have seen the grant reduce irrespective of the increasing VAT costs being borne by colleges. Therefore, it is in the interests of colleges to identify and implement ways of ensuring they only incur VAT where appropriate and where the VAT cost is unavoidable, to recover the maximum permissible.

This chapter aims to set out the necessary steps through which a college should be able to minimise its VAT liability and ensure it recovers the amount it is entitled to. The steps may be broken broadly down into two:

- Should the college incur VAT on the supply to it?
- If the answer is yes, is the college entitled to recover a proportion of the VAT it has incurred?

3·2 Should the college incur VAT on the supply to it?

Initially a college needs to determine whether it should incur VAT on any supplies to it. This should be answered when goods and services are being ordered and it may be prudent to include tests in the college's purchase ordering system to ensure this question is addressed at this stage.

Broadly, colleges may incur VAT on the following types of costs:

- Goods and services purchased from another taxable person
- Goods imported from non-EC countries
- Acquisitions from EC member states, and
- Services received from abroad subject to the reverse charge.

The amount to be claimed is the VAT properly chargeable and not the VAT actually charged where this is different. The consequences of this are as follows:

a. If the supplier is not a taxable person but shows VAT on the invoice, the VAT is not input tax and there is no automatic right of deduction. However, by concession, HM Customs and Excise may allow a claim in these circumstances where they are satisfied that:
   i. The college is neither involved in nor has a close knowledge of the supplier's business
   ii. It is reasonable for the college to consider that it had been lawfully charged VAT
   iii. The claim is made in respect of goods and services genuinely supplied at the stated value.

b. If the supplier is a taxable person but has failed to register for VAT, any VAT charged is recoverable as input tax by the college even though there can be no valid VAT invoice because the supplier has no VAT registration number.

c. VAT wrongly charged on a supply, etc. which is outside the scope of VAT, exempt or zero-rated is not input tax.

It is advisable for a college to ascertain at the earliest opportunity whether VAT is properly chargeable and will be appropriately charged by a supplier. Preferably when goods and/or services are being ordered, checks should be made by a college in respect of each transaction to confirm whether the supply is liable to VAT; whether the supplier is registered for VAT; and, where appropriate, will be charging VAT on the supply.

3·3 Is the college entitled to recover a proportion of the VAT it incurs?

There are a number of conditions which a college will have to meet to be entitled to claim a credit for input VAT. These are as follows.

3·3·1 Supply to a VAT-registered claimant

For a college's input tax claim to be valid, the supply must have been made to it and the college must be a taxable person (i.e. registered for VAT). This is fundamental and overrides the concept of who paid for the supply or who may have possession of the relevant invoice or other evidence. Where, for example, a college pays for goods or services which are supplied to a third party, the college does not have the right to deduct the VAT charged on the supply. This applies whether the payment was due to a legal or a normal commercial practice. Examples of where this could occur include:

- Payment of legal costs awarded against the unsuccessful party in litigation (see 3·4·16)
- Payment of a landlord's costs by the tenant for the drawing up of a lease
- Payment by a college of the costs of a viability study undertaken by a bank in respect of the college's activities.

Strictly, the condition that the supply must have been made to the taxable person results in input tax on employees' reimbursed subsistence expenses being irrecoverable. In practice, a supply which is *prima facie* to an employee of the college, can be treated as made to the college provided the college meets the full cost and the supply is legitimately financed by the college for its purposes. Typical examples of employee expenses are as follows:

- Subsistence costs (see 3·4·18)
- Removal expenses arising from staff relocation or transfer (see 3·4·19).

3·3·2 Direct link to actual supply

The VAT must relate to an actual supply, acquisition or importation. In essence there must be a direct and immediate link with the taxable transaction to be recoverable. Therefore, where a college makes a payment in advance but the goods are never physically supplied, input tax cannot be reclaimed as no supply has taken place.

3·3·3 Disallowance of input tax (blocked input tax)

Where the supplies to a college are subject to input tax restriction, in the form of a Treasury blocking order or otherwise, it cannot be reclaimed. Input tax cannot be claimed on the following:

- Goods acquired under a margin scheme, for example, second hand goods such as cars or the tour operators margin scheme supplies
- Goods and services for business entertainment
- Purchase of a new motor car where it is not going to be used exclusively for business use
- Certain accessories installed in motor cars, e.g. a radio phone, unless for business use
- Certain articles installed in new dwellings
- Assets acquired as a transfer of going concern (TOGC), for example, where, say, two colleges merge to form an entirely new entity. The activities of the former colleges may be transferred as going concerns to the new entity. If VAT is charged and the transfers qualify as TOGCs the new entity has no right to deduct it as input tax even if the college has paid the amount in good faith. However, where HM Customs and Excise are satisfied that the merging colleges have declared and paid the VAT they have charged to the new entity, they may allow the new entity to recover the VAT charged as if it were input tax.
- Where a college provides domestic accommodation to its employees in order to facilitate the running of the college, the expenditure is regarded as being incurred partly for a business purpose. Instances where a college may provide accommodation for staff include for caretakers or lecturers or where a college has a farming enterprise.
  If a college pays for:
  a. Goods which become the property of its employees
  b. The domestic fuel and power of its employees
  c. The private telephone calls of employees,

  the VAT incurred is treated as the college's input tax, but the college must account for output tax as a supply of goods or services as appropriate.
- Goods imported by a college where:
  a. At the time of importation the goods belong wholly or partly to another person
  b. The purposes for which they are to be used include private use by a member of staff.

  In such cases, the VAT due on the import is not deductible as input tax.

3·3·4 When to claim (accounting period)

It is essential for a college to determine when it is entitled to claim VAT as errors could result in penalties and interest costs being incurred by the college where these are identified by HM Customs and Excise. The claim should normally be made in the accounting period in which the supplies were received. A taxable person (i.e. a college registered for VAT) is entitled, at the end of each VAT period, to credit for so much of its input tax as is deductible.

Input tax should be claimed by colleges on the VAT return for the period in which the VAT was charged, i.e. the period covering:

- Supplies of goods and services, the supplier's tax point
- Goods acquired from another EC country, the date of acquisition
- The import of goods from countries outside the EC, the date of importation
- Goods removed from an HM Customs and Excise and/or Excise warehouse, the date of removal.

3·3·5 Record of input tax and suppliers' invoices

3·3·5·1 Records

If a college wishes to recover input tax, it must keep a record of all taxable, including zero-rated, supplies it receives and acquisitions made in the course of its business. The records must give details of each transaction and the VAT charged unless HM Customs and Excise allow otherwise. In practice, HM Customs and Excise may accept alternative means of identifying input tax; however, it is essential to obtain HM Customs and Excise's agreement to the method adopted.

Prior to 1 September 1997, colleges were entitled to adopt the input tax recording arrangements set out in the agreement between the Committee of Vice-Chancellors and Principals (CVCP) and HM Customs and Excise (also known as the Concordat), referred to as Tunnelling (paragraph 42 of the Concordat). Under this arrangement colleges were only required to record input tax incurred in respect of taxable supplies made by the college. However, after that date the Tunnelling concession on input tax recording has been withdrawn and colleges are required to adopt normal input tax recording arrangements.

Normally, HM Customs and Excise will require VAT registered entities such as colleges to compile a list of all the VAT invoices they receive for each VAT return period. They will also require the following:

a. The amount of VAT charged in each instance on goods and services received by a college including any VAT paid at import or removal from a bonded warehouse. Where adjustment is required for a credit received from suppliers this should also be listed and any VAT shown on the credit note must be deducted.
b. The amount of VAT due on any goods imported by post (other than Datapost) with a value of £2000 or less and on certain services received from outside the UK (i.e. imports of services from abroad).
c. The VAT exclusive value of all supplies received, including all such goods and services in (a) and (b) above.

The summary must be in the same order as the invoices are filed (or clearly cross referenced), and the VAT amounts logged against each entry must be totalled for each VAT period. An add-list is an acceptable alternative providing the summary shows the VAT and values itemised separately and the invoices are filed in the same order as listed. Cashbook accounting for input tax is also acceptable, i.e. claiming input tax when goods and services are paid for. In practice, from a cashflow perspective, it is more advantageous to claim input tax as it is incurred rather than when it is paid.

3·3·5·2 **Suppliers' invoices**

Where the supply is from another taxable person, a college must hold a VAT invoice or a document treated as such. An invoice marked as 'pro forma' or 'this is not a VAT invoice' is not acceptable for the purposes of reclaiming VAT. There are, however, a number of exceptions to this rule. These are as follows:

Supplies with a value of £25 or less

No VAT invoice is required where the total expenditure, including VAT, is £25 or less and relates to telephone calls from public or private telephones, purchases through coin-operated machines or car park charges (except for on-street parking meters which are statutory fees levied by local authorities and not subject to VAT).

Less detailed invoices

Normally the invoice or other document should contain the full particulars required for a valid VAT invoice. However, HM Customs and Excise may accept as satisfactory evidence an invoice which only has the following:

a. An identifying number
b. The customer's name and address
c. The tax point (i.e. the document has a date on it)
d. The supplies are for business purposes
e. The consideration must not exceed £100 (inclusive of VAT)
f. HM Customs and Excise have concerns for petrol and diesel; the particulars should include the vehicle registration number in place of the name and address of the college.

Originals and acceptable alternatives of invoices
Custom concern regarding photocopied invoices is that there is a risk of duplicate input tax claims. Colleges must, therefore, hold the originals of invoices to substantiate claims for input tax. HM Customs and Excise may accept a photocopy of the original as evidence in support of claims provided each photocopy is certified as being a true copy of the original by a responsible officer of the college and the original is produced to HM Customs and Excise if they require sight of it.

Invoices sent by fax or e-mail
Invoices sent in the form of a fax or an e-mail are acceptable provided they can be preserved for six years.

Cash and carry wholesaler's invoices
If the invoice is in the form of a till receipt with the description of the goods represented by codes it is acceptable evidence provided an up to date copy of the wholesaler's product code list is kept with the till receipt.

Invoices in the name of employees of the college
Invoices made out to employees in certain circumstances are acceptable evidence of entitlement to recover input tax (see 3·3·1).

Destruction or loss of invoices
In the vast majority of cases where invoices in support of an input tax claim are lost or destroyed, input tax claims have been rejected by HM Customs and Excise and their ruling has been upheld in many instances by the tribunals and courts. The tribunal and the courts only have a supervisory jurisdiction in these situations. Where a college's records and invoices are lost or destroyed, the burden of proof would be on the college to demonstrate that HM Customs and Excise were acting unreasonably in rejecting a claim not supported by records and invoices. HM Customs and Excise would normally suggest that duplicates are obtained from suppliers.

3·3·5·3 **Evidence of VAT on imported goods or goods removed from bonded warehouse**

On the importation of goods, if a college is the importer, the college will receive evidence of payment of import VAT, form C79 (Import VAT Certificate). This is normally issued on the twelfth day of the month following the date of the import of the goods. It should have the college's VAT number on it and a three digit number suffix which is the import entry number. This document serves the same purpose as a VAT invoice to evidence input tax claims. The date on the C79 is the accounting date for the recovery of the VAT.

Photocopies of the C79 can be used to evidence input tax claims providing the original can be produced if required. If a C79 is lost, replacements can be obtained from HM Customs and Excise (for up to six years after the date of issue). There are certain imports or goods removed from bonded warehouse which do not appear on the C79, for example, imports with a value not exceeding £600 (evidence: monthly VAT certificates), or postal imports with a value exceeding £2000 (evidence: authenticated copy 8 Single Administrative Document).

3·3·5·4 **Evidence of VAT on goods acquired from another EC country**

On the acquisition of goods from another EC country, a college must hold a document required to be issued from another EC country's tax authority (i.e. the equivalent of a VAT invoice). It should show the supplier's VAT number including alphabetical country identifier code (e.g. DK for Denmark), the college's VAT number prefixed by 'GB', the consideration for the supply, the date of issue and a description sufficient to identify the goods. The document should not have any VAT amounts included.

3·3·5·5 **Evidence of services received from abroad**

Where services are received from outside the UK, the relevant invoice from the supplier should be held by the college to support the claim for input tax.

3·3·5·6 **Records of non-deductible costs**

Colleges should retain evidence of these costs even though they are not entitled to claim the input tax (for details of types of non-deductible costs see 3·3·3).

3·3·6 Amount of recoverable VAT

If a college wishes to recover input tax incurred in respect of its taxable supplies it will be required to implement the procedures detailed below. This normally requires a two-stage calculation to identify VAT on expenditure that relates to taxable income.

However, a college may only wish to recover either input tax directly attributable to taxable supplies and/or apply the 20% and 5% rule (for further details see 3·3·8). If this is the case the college must obtain HM Customs and Excise's agreement to the chosen approach (method). Many colleges do wish to recover a proportion of VAT which on the face of it is neither wholly attributable to its taxable, exempt, or non-business activities. If this is the case, colleges need to identify a suitable method to recover input tax calculated as attributable to taxable supplies. The following sections set out the process to achieve this objective.

3·3·7 Use for a business purpose (including non-business/business calculations)

3·3·7·1 Basic points

In determining whether the VAT incurred by a college is recoverable the college needs to establish that the supplies it has received are for a business purpose. There is no definition in the VAT legislation of what is meant by for a business purpose. Colleges educate certain categories of students free of charge; this is because the students in question are either entitled to free education (i.e. students under the age of 19 years) or the college makes no charge (i.e. unemployed students aged 19 years or over). For VAT purposes, the provision of education in these circumstances is considered by HM Customs and Excise to be a non-business activity. Any VAT incurred in making these supplies is not input tax and is not recoverable by the college.

3·3·7·2 **Attribution methods**

For most colleges it is impossible to determine whether VAT incurred by the college is in respect of its non-business or business activities. HM Customs and Excise's approach in these circumstances is that colleges must adopt the following procedure.

- Identify as far as possible VAT on purchases wholly attributable to either a business or non-business use. Any VAT on purchases wholly attributable to a non-business purpose is not input tax.
- Apportion the remaining VAT between the non-business and business activities. There is no legislation setting out any particular formula or approach which must be adopted, but there is a legal requirement to do the calculation and the outcome must be fair and reasonable. In practice, any formula to identify business VAT is likely to be based on the following principle:

$$\frac{\text{Business activities}}{\text{Business activities} + \text{Non-business activities}}$$

In practice, the alternative formulae are as listed overleaf.

a. **Income apportionment**
The formula is as follows:

$$\frac{\text{Business income of the college}}{\text{Business income and non-business income of the college}}$$

Where an income values approach is being contemplated, colleges will need to allocate the income received into taxable, exempt and non-business activities. It may be appropriate to seek assistance and advice from your advisers on this matter.

b. **Student numbers**
A typical formula using student numbers is as follows:

$$\frac{\text{Number of fee-paying students enrolled at the college}}{\text{Total number of students enrolled at the college}}$$

This calculation is normally based on full-time equivalents.

c. **Student units**
A typical formula using student units is as follows:

$$\frac{\text{Number of units earned by fee payments students} \times \text{FEFC recurrent grant}}{\text{Total number of units}}$$

d. **Alternatives**
There may be other measures which a college could use, however, the alternative will need to be acceptable to HM Customs and Excise in that it is capable of fairly reflecting business and non-business activities of the college over time.

i. *Curriculum time*

$$\frac{\text{Classroom time of fee-paying students}}{\text{Total classroom time of all students}}$$

ii. *Staff time*

$$\frac{\text{Staff time spent teaching fee-paying students}}{\text{Total staff time spent teaching all students}}$$

3·3·7·3 **Annual adjustment**

An annual calculation is normally required in respect of the four VAT return periods which make up the college's VAT year (this commonly ends on 31 July each year). For further details see 3·3·8·3.

3·3·7·4 **Alternative approach for purchase of capital goods**

The Lennartz approach may be adopted for VAT on goods. This approach came about as a result of the VAT case on which the European Court ruled. Were a college to adopt this approach, it would recover all the VAT incurred immediately. However, when the goods were used for a non-business purpose, output tax would be charged on the deemed supply of services. HM Customs and Excise are considering asking the European Commission for a derogation to continue their current practice of apportionment when the goods are acquired.

3·3·8 Use for a taxable purpose (including partial exemption calculations)

3·3·8·1 Basic position

From a college's perspective, having identified the input tax attributable to its business activities it needs to identify the VAT it is able to recover.

A college has non-business, taxable and exempt activities. It cannot recover VAT in respect of its non-business activities. Equally, it cannot reclaim VAT in respect of its exempt business activities. Where input tax cannot be claimed because it relates to exempt supplies, it is known as exempt input tax and the VAT-registered business is described as partly exempt for VAT purposes.

To calculate the amount of recoverable input tax, a college needs a partial exemption method which may need to be approved by HM Customs and Excise. To determine the amount that is recoverable input tax, a college needs to take the following steps:

- **Allowable input tax – general provisions**
  The amount a college is entitled to recover at the end of each VAT return period is as much of the input tax on supplies, acquisitions and importations in the period as is attributable to the following supplies, made or to be made by the college in the course or furtherance of its business activities.
  a. Taxable supplies i.e. supplies of goods and services made in the UK other than exempt supplies
  b. Supplies outside the UK which would be taxable if made in the UK
  c. Supplies of services which:
     i. Are supplies to persons who belong outside the EC, or
     ii. Are directly linked to the export of goods to a place outside the EC, or
     iii. Consist of the making of arrangements for the supply of services within (a) and (b) above, provided that the supply is exempt (or would have been exempt if it were made in the UK) by virtue of it being a supply of insurance or financial services.

- **De minimis limits**

  There are statutory limits which, if exceeded, an entity such as a college will suffer a restriction on the amount of input tax it is entitled to recover. The value of input tax incurred by a college is likely to exceed these limits. However, separately VAT-registered college subsidiaries may not. The limits are referred to as the 'de minimis limits'. They are as follows.

  a. Where in any prescribed accounting period (VAT return period) or longer period the exempt input tax of a taxable person (i.e. a VAT-registered college):
     i. Does not amount to more than £625 per month (or £1875 per quarter, or £7500 annually) on average
     ii. Does not exceed more than one half of all his input tax for the period concerned, all such input tax in the period is treated as attributable to taxable supplies.

     Therefore, the entity (i.e. the VAT-registered college) is treated as fully taxable and entitled to recover all its input tax.

  b. Where applying the de minimis limit provisions to a longer period (for a definition of longer period please refer to 3·3·8·3. *Annual adjustments*, below):
     i. Any treatment of exempt input tax as attributable to taxable supplies in any prescribed accounting period (VAT return period) is disregarded
     ii. No account is to be taken of any amounts which may be deducted or payable under the capital goods scheme (see 3·4·2).

  'On average' means the average over the prescribed accounting period, or for a longer period. For group registrations, the rules apply to the group as a whole.

3·3·8·2 **Methods of calculating recoverable input tax**

If a college is not entitled to be treated as fully taxable, it will suffer a restriction of the amount of input tax that is recovered. However, as is the case with most colleges, it is impossible to a large extent to allocate input tax directly to either taxable, exempt or non-business activities. Therefore, a college needs to identify a method to calculate the amount of unallocated (residual) input tax which is recoverable in addition to that which is directly attributable to taxable supplies.

The VAT legislation sets out a standard method for calculating the amount of recoverable residual input tax. However, alternative methods (special methods) may be adopted with the consent of HM Customs and Excise.

The standard method

The standard method requires the following steps to be undertaken. In order to ascertain the amount of residual input tax that is recoverable, input tax must be analysed under the following headings:

a. Input tax on purchase invoices taxpoint dated in the relevant period
b. Input tax on goods and services used exclusively for the purposes of making exempt supplies. This is wholly disallowed (subject to the de minimis rules and should be kept in mind for subsidiaries in particular)
c. Input tax on goods and services used for a non-business purpose. This VAT should have been identified by the non-business/business exercise (see 3·3·7)
d. Input tax on goods and services used partly for making taxable and exempt supplies (residual input tax). For most colleges, the residual input tax figure will be arrived at using one of the calculations in 3·3·7·2.

The standard partial exemption method formula is applied to ascertain the amount of residual input tax which is recoverable. The formula is as follows:

$$\frac{\text{The value of taxable supplies}}{\text{The total value of all supplies}}$$

(the ratio expressed as percentage and rounded up to the next whole number).

In calculating the fraction above, the value of the following supplies should be excluded:

- The value of self-supplies, for example, the self-supply of stationery
- The value of incidental real estate or financial transactions
- The value of supplies of capital goods acquired for use in the business
- The value of any supply on which no output tax is charged because the input tax on the purchase was blocked, e.g. the sale of a used car for which input tax was not recoverable on the acquisition, unless the car was sold at a profit in which the exclusive VAT-exclusive margin is included
- Reverse charge services (i.e. imports of services from abroad)
- The value of a transfer of a going concern (a supply which is neither a taxable or exempt supply).

What constitutes an incidental supply can be viewed in two ways. First, it can be a one-off situation, for example, the sale of a building by a college. Second, it could be regular income, for example, bank interest which is received passively.

Special methods

HM Customs and Excise may approve or direct a taxable person (i.e. a VAT-registered college) to use another method other than the standard method. As in the case of the standard method, the same exclusions apply.

A college using a method approved or directed as above must continue to use it until HM Customs and Excise approve or direct the termination of its use.

Any direction as above for either the use of, or termination of the use of, a method takes effect from the date of the direction or such later date as HM Customs and Excise specify.

A special method can be any method agreed by HM Customs and Excise and devised to suit the needs of the particular entity, for example, one based on the ratio of:

- The number of taxable transactions to the total number of transactions (taxable and exempt) carried out
- The area of a building used for making taxable supplies to the total area of the building
- The input tax on the goods and services used in making taxable supplies to the input tax on the goods and services used in making taxable and exempt supplies
- The value of goods and services used in making taxable supplies to the value of goods and services used in making taxable and exempt supplies.

The ratio should be expressed as a percentage (without rounding up).

A special method may also be based on separate calculations for different sectors of the entity or, in the case of a group registration, for each member of the VAT group.

HM Customs and Excise may approve a provisional claim in each quarter based on the recoverable proportion for the previous tax year (after annual adjustment).

HM Customs and Excise should be informed of any change in the entity which has a substantial effect on the amount of input tax recoverable. The special method will then be reviewed by HM Customs and Excise and, if no longer suitable, a direction to stop using the method will be issued. The taxable person must then either use the standard method or propose an alternative special method.

Education institution special method – 20% and 5% rule

Under the former HE sector Concordat agreement (paragraph 43), HM Customs and Excise allowed colleges recovery of VAT for three areas where both taxable and exempt supplies were made. Under the agreement colleges are not required to record or recover input tax in respect of the activities. However, to determine the amount of recoverable input tax attributable to the activities the following formula is applied:

Output tax accounted for in respect of the activity
× Agreed percentage
= Recoverable input tax

For taxable accommodation and catering the percentage is 20%. For bars the percentage is 5%.

Although the Concordat agreement has been withdrawn, if the 20% and 5% rule forms part of a college's partial exemption special method agreement and providing a college's method is still operative, these percentages can continue to apply until such time HM Customs and Excise renegotiates the matter with the college.

3·3·8·3 **Annual adjustments**

The deductions of input tax for each prescribed accounting period (i.e. a VAT return period) are provisional whichever method is adopted. This is because the amount deductible in some such periods may be unfairly affected, e.g. by seasonal variations. Normally, it is a requirement to recalculate the amount of input tax reclaimable over a longer period than a single VAT return period. If a special method is being used, the letter of approval will state whether an annual adjustment is required.

Tax year

The period over which an adjustment is normally made is a tax year. For a taxable person this means:

a. The first period of 12 calendar months commencing on 1 April, 1 May or 1 June, according to the prescribed accounting periods (i.e. VAT return periods) allocated to it, next following a college's effective date of registration, or
b. Any subsequent period of 12 calendar months commencing on the day following the end of the college's first, or any subsequent, tax year.

However, HM Customs and Excise may approve or direct that a tax year be for a period other than 12 months or commences on a different date. A tax year will normally, therefore, end on 31 March, 30 April or 31 May. Where monthly returns are made it will normally end on 31 March. A number of colleges have in fact opted for a tax year which coincides with their financial year end, i.e. 31 July.

There are circumstances, however, where the above is not the case. There may be a situation where, for example, a subsidiary which formally was able to recover all the VAT it incurred, as it only made taxable supplies, commences to make exempt supplies and incurs input tax in respect of its exempt supplies. It needs to determine the period over which an adjustment is to be made.

Where it incurs exempt input tax throughout a tax year, its longer period corresponds with that tax year. However, if the subsidiary did not incur exempt input tax during its immediately preceding tax year or registration period in which case its longer period (i.e. adjustment period) begins on the first day of the first prescribed accounting period (i.e. VAT return period) in which it incurs exempt input tax and ends on the last day of that tax year. In which case the adjustment period (i.e. the longer accounting period) would commence, if the exempt input tax is incurred after the first VAT return period of a tax year, in the second, third or fourth VAT return period depending on which VAT return period in which input tax attributable to an exempt supply is incurred.

Where, however, its only exempt input tax is incurred in the last accounting period (i.e. VAT return period) of its tax year, no longer accounting period is applied in respect of that tax year (i.e. no annual adjustment is required).

Having an adjustment period for three or less VAT return periods could be a disadvantage in some circumstances. If, in our example, the subsidiary made taxable supplies in the first three periods of the tax year and only incurred exempt input tax in the last, the taxable supplies would not be taken account of in any calculation to determine the amount of recoverable input tax incurred in the last period. This would be the case unless the subsidiary agreed with HM Customs and Excise in advance of the situation arising, for example, to have a tax year which covered all the prescribed accounting periods for the year.

Where a college or its subsidiary incurs exempt input tax during its registration period, its longer period begins on the first day on which it incurs exempt input tax and ends on the day before the commencement of its first tax year.

In the case of a college ceasing to be taxable during a longer period, that period ends on the day it ceases to be taxable. HM Customs and Excise may allow a longer period to apply which need not correspond with a tax year.

Calculation of the annual adjustment

Where all the exempt input tax in the longer period cannot be treated as attributable to taxable supplies, then, unless HM Customs and Excise dispense with the requirements, a college must calculate the reclaimable proportion of any remaining input tax not directly attributed on the same basis as in each of the prescribed accounting periods but using the figures for the longer period. Any difference between the amount of reclaimable input tax recalculated at the end of the longer period and the total amount provisionally deducted during the prescribed accounting periods is an over or under declaration of VAT and must be entered on the VAT return for the first tax period (i.e. VAT return period) after the end of the longer period (unless HM Customs and Excise allow otherwise).

If the recalculation shows that the exempt input tax is below the de minimis limits, any input tax not already reclaimed is an under deduction of VAT and should be entered on the next VAT return.

3·3·8·4 **Example partial exemption calculation**

The following example illustrates the operation of a partial exemption calculation to determine the amount of VAT which is recoverable in respect of VAT costs which cannot be attributed to either taxable, outside the scope or exempt supplies. It has been assumed in the example that any attribution of input tax to particular supplies has already taken place. The following assumptions have also been made in respect of the example:

- Residual VAT-incurred formula (business/non-business calculation)

$$\frac{\text{Business income of the college}}{\text{Business income and non-business income of the college}} \times \text{Residual VAT-incurred tax} = \text{Residual input tax}$$

- Taxable input tax formula (partial exemption calculation)

$$\frac{\text{The value of taxable supplies} \times \text{Residual input tax}}{\text{The total value of all supplies}} = \text{Recoverable input tax}$$

The total value of supplies equals taxable and exempt supplies (excluding non-business income of the college)

- Value of all taxable supplies (i.e. standard-rated and zero-rated supplies) in the tax year £116 057·17

  Typical taxable supplies included in this figure are shop takings, sales of books and other publications, travel agency commissions, refectory sales to staff, consultancy fees, hire of residence rooms to third parties out of term time, training, restaurant sales, sponsorship, miscellaneous photocopying charges and management charges to subsidiaries.

- Value of all exempt supplies in the period £2 107 683·11

  Exempt supplies typically that would be included in this figure would be fees paid by the LEA, HE fees including franchise fees, external course fees, full- and part-time course fees paid by students, crèche charges, residence charges to students and staff, and lettings.

- Value of income excluded from the calculation — £10 392 451·86

  Excluded from the partial exemption calculation typically would be bank interest (incidental), insurance commissions (incidental), grants (i.e. from the FEFC, ESF and Access, which relate all or in part to a college's non-business activities), and donations.

- Residual input tax incurred in the tax year and declared on the college's VAT return — £267 056

- It is assumed that the college applies the 20% and 5% rule. Therefore, the method adopted would be considered to be a special method by HM Customs and Excise and the college would not be allowed to round up any recoverable percentage to the nearest whole number.

To calculate the amount of VAT which is recoverable in the example, the college would initially calculate the amount of VAT attributable to its business activities. The next step would be to calculate the amount of business input tax which was attributable to its taxable activities and, as such, recoverable.

Step 1. Calculation of business input tax
Calculation of business input tax:

$$\frac{£2\,223\,740{\cdot}28 \times £267\,056}{£12\,616\,192{\cdot}14} = £47\,071{\cdot}50$$

Step 2. Calculation of recoverable input tax

$$\frac{£116\,057{\cdot}17 \times £47\,071{\cdot}50}{£2\,223\,740{\cdot}28} = £2456{\cdot}66$$

The college would be entitled to recover approximately 0·9% of the input tax it incurs. If this amount is more or less than that provisionally claimed during the year, the college would be required to include the amount required to be adjusted on the return for the VAT period following the tax year end.

These calculations are subject to annual adjustment.

3·3·8·5 **Records and accounts**

In addition to the records which are normally required, a partially exempt business such as a VAT-registered college must also maintain the following:

- How taxable and exempt input tax has been calculated in each VAT return period and longer period
- How the simplification (abolished in the 1999 Budget) and de minimis rules have been applied
- Any further information that HM Customs and Excise have stipulated in any agreement which has been reached with the college concerning business/non-business/ partial exemption method.

3·4 Allocation and recovery of input tax (special cases)

3·4·1 Partial exemption

3·4·1·1 Adjustment for change of use of goods and services

A college will be required to make adjustments to the amount of input tax that has previously been claimed in respect of goods and services where its initial intention was to make:

a. Taxable supplies and recover all the input tax incurred, or
b. Exempt supplies and not recover any input tax

and its intention or actual use changes in the case of (a) to make exempt or a combination of taxable and exempt supplies and for (b) to make taxable or a mixture of taxable and exempt supplies. These regulations apply where the goods and/or services have not been used and either the intention or actual use changes from that initially envisaged. These regulations apply for a period of six years commencing on the first day of the prescribed accounting period in which the attribution was determined.

If a college triggers these regulations, it must account for an amount equal to the input tax which would or would not have been recoverable in accordance with the method the college had in place at the time the input tax was first attributed. The adjustment should be made on the VAT return for the prescribed accounting period (i.e. VAT return period) in which the use occurs or the intention changes.

Where, however, a college recovers input tax based on an intention to make taxable supplies but before those supplies are made, the liability changes and those supplies become exempt, no clawback is due. In the reverse situation, no pay back can be claimed.

Should any of these situations arise it would be advisable to notify HM Customs and Excise of the details and it may be advisable to discuss the matter with your advisers.

3·4·2 Capital goods scheme

3·4·2·1 Basic points

Since incorporation in 1993, many colleges have been redeveloping their campuses. In some cases, this has meant having fewer sites which has involved constructing buildings and/or refurbishing existing buildings on preferred sites, or replacing existing buildings with more modern facilities. Colleges have also significantly increased their spend on computer hardware and software. This has meant for the colleges concerned spending significant amounts on goods and services and, in many cases, VAT has been incurred in respect of these costs. These transactions, in particular construction costs, may trigger the application of the capital goods scheme. The scheme applies to certain items of computer equipment and land and buildings which are used for non-taxable purposes. The provisions do not apply to any such capital items acquired or brought into use before 1 April 1990.

When a capital asset is acquired, the normal rules for claiming input tax apply. If the asset is used wholly in making taxable supplies, input tax is recoverable in full; if used wholly in making exempt supplies, none of the input tax is recoverable; and if used for making taxable and exempt supplies a proportion of the input tax may be claimed under the partial exemption rules. Where subsequently in a period of adjustment there is a change in the extent of taxable use, an input tax adjustment has to be made. If taxable use increases, a further amount of input tax can be claimed and, if it decreases, some of the input tax already claimed must be repaid.

3·4·2·2 Capital items within the scheme

Capital items to which the provisions apply are any items of the following descriptions which the owner (i.e. the college; these provisions could equally apply to a college's wholly owned subsidiary or subsidiaries if they qualify as the owner) uses in the course of or furtherance of its business, and for the purpose of that business, otherwise than solely for the purpose of selling that item (i.e. items purchased for resale, such as stock-in-trade, are not covered by the scheme). All values are VAT exclusive.

a. A computer, or an item of computer equipment, worth £50 000 or more supplied to, or acquired or imported by the college. Any delivery or installation costs should be included unless invoiced separately. If imported, the value for VAT at importation (including import duty) should be taken. In practice the scheme will mainly cover mainframe computers as the £50 000 limit applies to individual items of computer equipment, not complete systems. Excluded are computer software and computerised equipment, e.g. a computerised telephone exchange or lift system (unless installed as a fixture in a new building covered under (b) to (e) below).

b. Land, a building or part of a building or, after 2 July 1997, a civil engineering work or part of a civil engineering work where the value of the interest supplied to the college, by a taxable supply other than a zero-rated supply, is £250 000 or more. When determining whether the value of the supply is £250 000 or more, any part of that value consisting of rent (including charges reserved as rent) is excluded provided that, after 2 July 1997, it is neither payable nor paid more than 12 months in advance nor invoiced for a period in excess of 12 months. Not included is the freehold of a piece of bare land purchased for possible future development, e.g. acquired for a land bank and not used before development or sale.

c. A building or part of a building where the college's interest in, right over or licence to occupy it:
   i. Is treated as self-supplied to college, or
   ii. As, on or before 1 March 1997, treated as self-supplied to college.

   In each case, the value of the supply must be £250 000 or more.

d. A building not falling, or capable of falling, within (c) above constructed by the college and first brought into use by the college after 31 March 1990 where the aggregate of:
   iii. The value of taxable grants relating to the land on which the building is constructed made to the owner after that date, and
   iv. The value of all the taxable supplies of goods and services, other than any that are zero-rated, made or to be made to him for, or in connection with, the construction of the building after that date is £250 000 or more.

e. A building which the college alters, or an extension or an annex which the college constructs, where additional floor area is created in the altered building, extension or annex, of 10% or more of the original floor area before the work was carried out. The value of all taxable supplies of goods and services, other than any that are zero-rated, made or to be made to the owner after 31 March 1990 for, or in connection with, the alteration etc. must be £250 000 or more.

f. A civil engineering work constructed by the college and first brought into use by the college after 2 July 1997 where the aggregate of:
   v. The value of taxable grants relating to the land on which the civil engineering work is constructed made to the owner after that date, and
   vi. The value of all the taxable supplies of goods and services, other than any that are zero-rated, made or to be made to him for, or in connection with, the construction of the civil engineering work after that date is £250 000 or more.

g. A building which the college refurbishes or fits out where the value of capital expenditure on the taxable supplies of services and of goods affixed to the building, other than any that are zero-rated, made or to be made to the college or its subsidiary for, or in connection with, the refurbishment or fitting out in question after 2 July 1997 is £250 000 or more.

The costs under (d) and (e) include all those involved in making the building ready for occupation e.g. professional and managerial services, demolition and site clearance, building and civil engineering contractors' services, materials used in the construction, security, equipment hire, haulage, landscaping, fitting out, etc.

3·4·2·3 **The period of adjustment**

The period of adjustment consists of five successive intervals for:

a. Computers etc. under 3·4·2·2(a) above, and
b. Land, buildings and civil engineering works under 3·4·2·2(b) above where the interest has less than 10 years to run at the time it is supplied to the college (e.g. an eight-year lease).

For all other land and buildings not within (b) above the period of adjustment consists of 10 successive intervals.

3·4·2·4 **First interval**

Subject to the special case below and the rules in 3·4·2·6 and 3·4·2·7 below, the first interval commences, as the case may be where:

- The college or its subsidiary (i.e. as owner) is a registered person when it imports, acquires or is supplied with the item as a capital item or when he appropriates an item to use as a capital item, the date of importation, acquisition, supply or appropriation,
- The capital item falls within 3·4·2·2(c)(i) above, on the date of the self-supply under those provisions, where the capital item falls within 3·4·2·2(c)(ii) above, on the date that the college or its subsidiary (i.e. as owner) first uses the building or, if later than 1 April 1990, and
- The capital item falls within 3·6·2·2(d)–(g) above, on the date that the college or its subsidiary (i.e. as owner) first uses the building, altered building, extension, annex, civil engineering work or building which has been refurbished or fitted out and runs to the end of the day before the commencement of the tax year following that date i.e. it normally runs to the following 31 March, 30 April or 31 May depending upon its prescribed accounting periods (VAT return periods), see 3·3·7.

Where the college or its subsidiary (i.e. as owner) is not registered when he first uses an item as a capital item:

- If it subsequently becomes a registered person, the first interval commences on his effective date of registration and ends on 31 March, 30 April or 31 May depending upon the prescribed accounting period (VAT return period) allocated to him, and
- If it is subsequently treated as a member of a group for VAT purposes, the first interval corresponds with, or is that part still remaining of, the then current tax year of the group
- The extent to which a capital item is used in making taxable supplies does not change between what would otherwise have been the first interval above and the first subsequent interval under 3·4·2·5 below
- The length of the two intervals taken together does not exceed 12 months, and
- The first interval applicable to the capital item ends on what otherwise would have been the end of the first subsequent interval, i.e. the two periods are combined to become the first interval.

3·4·2·5 **Subsequent intervals**

Subject to the rules in 3·4·2·6 and 3·4·2·7 below, each subsequent interval corresponds with a longer period applicable to the college or, if no longer period applies, a tax year. In either case, this will normally run to the following 31 March, 30 April, 31 May or 31 July where a college's VAT year ends at the same time as its financial year end. Some colleges may have agreed an alternative VAT year end to suit their own circumstances.

3·4·2·6 **VAT groups**

These provisions only apply after 2 July 1997. On the first occasion during a period of adjustment that a college or subsidiary which owns a capital item:

a. Being registered for VAT subsequently becomes a member of a VAT group, or
b. Being a member of a group for VAT purposes ceases to be a member of that group (whether or not it immediately becomes a member of another such group the interval then applying ends on the day before the college becomes a member of the group or the day the college or its subsidiary ceases to be a member of the group (as the case may be). Each subsequent interval (if any) applicable to the capital item ends on the successive anniversaries of that day.

The provisions applying before 3 July 1997 are as follows. On any occasion during a period of adjustment where (a) or (b) above applied, the interval then applying ended on the day before the college or its subsidiary (i.e. as owner) became a member of the group or the day the college or its subsidiary (i.e. as owner) ceased to be a member of the group (as the case may be).

Where (a) above applied, each subsequent interval (if any) ended on the last day of a longer period applicable to the group or, if no longer period applied, the last day of a tax year of that group.

Where (b) above applied:

i. If the college or its subsidiary (i.e. as owner) immediately became a member of a second VAT group, subsequent intervals (if any) ended on the last day of a longer period applicable to the second group or, if no longer period applied, the last day of a tax year of that group, and
ii. Otherwise, the next interval (if any) ran to the following 31 March, 30 April or 31 May depending upon the prescribed accounting periods allocated to the owner when registered alone. Each subsequent interval (if any) corresponded with a longer period applying to the owner or, if no longer period applied, a tax year of the college or its subsidiary (i.e. as owner).

3·4·2·7 Transfers of businesses as going concerns

Where a college or its subsidiary (i.e. as owner) of a capital item transfers it during the period of adjustment in the course of the transfer of its business or part of its business as a going concern (the item therefore not being treated as supplied):

a. If the new owner takes over the registration number of the original owner, the interval applying at the time of the transfer does not end at that time but on the last day of the longer period applying to the new owner immediately after the transfer or, if no longer period then applies, on the last day of his tax year following the day of transfer, and
b. If the new owner does not take over the registration number of the original owner, the interval then applying ends on the day before the owner transfers the business or part. Each subsequent interval (if any) applicable to the capital item ends on the successive anniversaries of that day. Before 3 July 1997, each subsequent interval (if any) ended on the last day of a longer period applying to the new owner or, if no longer period applied, the last day of a tax year of the new owner.

As the new owner takes over responsibility for applying the capital goods scheme, in order to make the necessary calculations (see 3·4·2·8) it will need to know for each relevant capital item:

- The date of acquisition and number of remaining intervals in the period of adjustment
- The total input tax incurred
- The percentage of that input tax which was claimed on the item in the first interval.

3·4·2·8 **Method of adjustment**

Where the extent to which a capital item is used in the second or later interval is greater or less than it was used in the first interval, an adjustment is required calculated by the formula:

$$\frac{\text{Total input tax on the capital item} \times \text{The adjustment percentage}}{\text{Number of adjustment period intervals (i.e. 5 or 10)}}$$

'Total input tax on the capital item' is as follows:

- For a capital item within 3·4·2·2(a) or (b) above, it is the VAT charged on the supply, acquisition or importation. Any VAT charged on rent (including charges reserved as rent) is excluded unless, after 2 July 1997, it is payable or paid more than 12 months in advance or invoiced for a period in excess of 12 months.
- For a capital item within 3·4·2·2(c) above, it is the VAT charged on the supply which the owner is treated as making to himself, and
- For a capital item under 3·4·2·2(d)–(g) above, it is the aggregate of the VAT charged on the supplies described, other than VAT charged on rent (if any),

and includes any VAT treated as input tax under the rules relating to pre-registration or pre-incorporation input tax.

'The adjustment %' is the difference (if any) between the extent, expressed as a percentage, to which the capital item was used (or is regarded as being used) in the making of taxable supplies at the time the original entitlement to deduction of the input tax was determined* and the extent to which it is so used or treated in the subsequent interval in question. Where the college or its subsidiary (i.e. as owner) of a building within these provisions grants or assigns a tenancy or lease in the whole or part of the building and the premium (or if no premium is payable the first payment of rent) is zero-rated, any subsequent exempt supply arising from the grant (e.g. rent) is disregarded in determining the extent to which the building is used in making taxable supplies.

* Formerly this said 'is used (or is regarded as being used) in making taxable supplies in the first interval applicable to it'. This was changed by the 1999 Budget.

The percentage is:

- Where the item is used wholly for making taxable supplies, i.e. 100%
- Where it is used wholly for making exempt supplies, i.e. 0%
- Where it is used for making both taxable and exempt supplies. Normally it is the percentage calculated by the residual input tax partial exemption annual adjustment formula for the respective year (although HM Customs and Excise may allow, or direct, the use of another method). Where the standard method is used (see 3·3·8) the same percentage applies to the whole of the non-attributable input tax. If a special method is used (see 3·3·8(b)) involving different calculations for different parts of the business, the percentage to be used is that which applies to the part of the business in which the capital item is used.

Where, after 2 July 1997, 3·4·2·6(a) or (b) above or 3·4·2·7(b) above applies, subsequent intervals do not necessarily correspond with the annual adjustment period for partial exemption purposes and the attribution of total input tax is determined by such method as is agreed with HM Customs and Excise.

Where during an interval the use of a capital asset changes from one of these categories to another (or different percentages are calculated in different parts of the business and the item moves from one part of the business to another), the percentage of taxable use for the interval overall must be calculated taking into account the number of days of use in each category during the interval.

Example

A college refurbishes a building on its campus for which the VAT on business usage is £525 000. For the first eight intervals and for 170 days in the ninth interval it is used by the college for its own purpose of which the percentages of tax are as follows:

Interval 1	3%	*Interval 6*	6%
Interval 2	4%	*Interval 7*	6%
Interval 3	3%	*Interval 8*	6%
Interval 4	6%	*Interval 9*	6%
Interval 5	6%		(first 170 days)

For the remainder of the period of adjustment the building is sublet to a subsidiary of the college.

Interval 1
Initial input tax claim

$$= £525\,000 \times 3\% = £15\,750$$

Interval 2
Additional input tax claimed from HM Customs and Excise

$$= \frac{£525\,000 \times (4–3)\%}{10} = £525$$

Interval 3
There is no difference between the recovery rate in interval one and interval three, therefore, no adjustment is required.

Intervals 4–8
Additional input tax is recoverable from HM Customs and Excise for intervals 4–8. The amount recoverable for each interval is:

$$\frac{£525\,000 \times (6–3)\%}{10} = £1575$$

Interval 9
Input tax is payable to HM Customs and Excise in the interval. The calculation is as follows:

$$\frac{170}{365} \times \frac{(6–3)\% \times £525\,000}{10} = £733{\cdot}56$$

$$\frac{195}{365} \times –3\% \times \frac{£525\,000}{10} = –£841{\cdot}38$$

As the building is being let on an exempt lease for the remaining 195 days of interval 9 the input tax is wholly attributable to an exempt supply. Therefore the college will have to refund a proportion of the amount it initially claimed in period 1. Overall the college would be required to refund £107·82 to HM Customs and Excise.

Interval 10
The college would be liable to refund HM Customs and Excise a further £1575.

3·4·2·9 **Sale of assets and deregistration**

Where, during an interval other than the last interval, the college or its subsidiary (i.e. as owner) of a capital item either:

- Supplies it, or
- Is deemed to supply it on ceasing to be a taxable person, or
- After 20 October 1995, would have been deemed to supply it on ceasing to be a taxable person but for the fact that VAT on the deemed supply would not have been more than £250 (whether by virtue of its value or because it is zero-rated or exempt),

then:

a. If that supply is a taxable supply, the owner is treated as having used the capital item for each of the remaining complete intervals wholly in the making of taxable supplies, and
b. That supply is an exempt supply, the college is treated as not using the capital item for each of the remaining complete intervals in making any taxable supplies.

For the interval in which the capital item is sold, the change of use adjustment compared to the first interval is calculated in the normal way as if the item had been in use for the whole of that interval. This applies whether it was sold on the first or last day of the interval.

For the remaining complete intervals in the period of adjustment, the recovery percentage will be 100% where (a) above applies or 0% where (b) above applies, but this is subject to the following two provisos:

i. The aggregate of the amounts which may be deducted in respect of the remaining complete intervals cannot exceed the output tax chargeable on the supply of the capital item.
ii. After 2 July 1997, a disposal test applies. Where the total amount of input tax deducted or deductible by the college or its subsidiary (i.e. as owner) as a result of:
    - The initial deduction
    - Any normal adjustments made in intervals up to and including the interval of supply or deemed supply, and

- Any adjustment which would otherwise have been made for remaining complete intervals

exceeds the output tax chargeable on the supply of the capital item, unless HM Customs and Excise allow otherwise the owner must pay to HM Customs and Excise, or as the case may be deduct, such an amount as results in the total input tax deducted or deductible being equal to the output tax chargeable on the supply of the capital item.

The disposal test is an anti-avoidance measure to ensure that partly exempt businesses, such as banks, insurance companies, educational establishments, sports clubs and providers of private health care do not obtain an unjustified tax advantage, for example by making a substantial exempt supply of a long lease of a property followed immediately by the taxable disposal of the freehold for low consideration. HM Customs and Excise do not intend that the disposal test should be applied to bona fide commercial transactions. Given the policy objective, the disposal test will not be applied:

- To sales of computer equipment
- Where the owner disposes of an item at a loss due to the market conditions
- Where the value of the item is reduced for other legitimate reasons (e.g. accepting a low price for a quick sale)
- Where the amount of output tax on disposal is less than the total input tax only because of a reduction in the VAT rate
- Where the item is used only for taxable (including zero-rated) purposes throughout the adjustment period (which includes the final disposal).

Where there is an unjustified tax advantage, a college must calculate the net tax advantage (i.e. the overall benefit derived from the avoidance device, normally the amount of input tax that would still be subject to adjustment under the scheme were it not for the sale of the capital item less any output tax due on the sale) and then work out how much of the net tax advantage is unjustified. Normally this could be achieved by using the ratio that the value of the final taxable sale bears to the value of both the exempt supply and the final taxable sale. If an asset is sold without ever having been used, HM Customs and Excise do not regard it as a capital item for the purposes of the scheme.

Example
The facts are the same as in the example in 3·4·2·8 above except that the building is sold in interval 9 for £3 000 000, the current market value.

Intervals 1–8
No change

Interval 9
The college would be liable to pay HM Customs and Excise £1 682·82. In essence, by selling the property the college accelerates the repayment of the VAT incurred in respect of the building.

3·4·2·10 **Lost, stolen, destroyed or expired assets**
If, during the period of adjustment, a capital item is:

- Irretrievably lost or stolen or is totally destroyed, or
- In interest in land or buildings which expires,

no further adjustment is made in respect of the remaining complete intervals applicable to it. The normal change of use adjustment is made for the period of loss, etc. as if the item had been used for the whole period.

3·4·2·11 **Capital items temporarily not used**
Once the period of adjustment has started, if a capital item is not used for a while (e.g. a computer is overhauled), it is treated as being used during that period for the same purpose as it was previously used.

3·4·2·12 **Returns**

Where an adjustment under 3·6·2·8–3·6·2·11 above is required, the taxable person (i.e. a college or its subsidiary registered for VAT) must include the adjustment in his return for the second prescribed accounting period following the interval to which the adjustment relates or in which the supply as a result of sale, or deemed supply as a result of deregistration, takes place (i.e. the period after the one in which the partial exemption annual adjustment is made). The adjustment should be included in box 4 of the VAT return.

Where an interval has come to an end because:

- The owner of the capital asset has ceased to be a member of a group, or
- The owner (who remains a taxable person) has transferred part of his business as a going concern,

the adjustment for that interval must be included in the return for the group or transfer for the second prescribed accounting period after the annual adjustment period for partial exemption purposes in which the interval in question fell.

HM Customs and Excise may allow the necessary adjustment to be made in a later return but, with effect from 1 May 1997, only if it is a return for a prescribed accounting period commencing within three years of the end of the period when the adjustment should have been made.

3·4·3 Input tax incurred in respect of any activity other than a taxable supply

In principle input tax cannot be reclaimed on goods and services used in any activity other than the making of taxable supplies. However, in certain circumstances HM Customs and Excise policy in these circumstances is as follows:

a. **Research and development**
HM Customs and Excise accept that input tax incurred in respect of research and development costs is recoverable in part or whole subject to the activities it supports. Provided it does not relate to a non-business activity, the input tax can be treated as residual input tax.

b. **Abortive supplies**
Where a college incurs VAT in respect of an abortive supply, e.g. architects' fees in respect of an aborted project, it is HM Customs and Excise policy to treat these supplies as general overheads and the input tax is wholly or partially recoverable. If an intention to make supplies is formed and frustrated in the same VAT return period, any related input tax should be treated as residual. Otherwise an adjustment is subsequently required when the original intention is different and frustrated. Advice should be sought to ascertain the extent to which input tax in these circumstances is recoverable.

3·4·4 Supplies of services which are outside the scope of UK VAT

Where a college provides a service which would be taxable if performed in the UK for a UK customer, but the service is provided outside the UK, for example, consultancy, the value of this income according to HM Customs and Excise should be excluded from the partial exemption calculations, unless a special method is agreed. This view is the subject of ongoing dispute; you should seek advice on the latest position.

It is noted that colleges came into existence on 1 April 1993 and, therefore, cannot rely on a concession applying to pre-1 January 1993 businesses which used to get zero rating on services performed outside the UK.

3·4·5 Ultimate purpose of a transaction

It is not possible to attribute input tax to an ultimate taxable supply where it is incurred initially in respect of an exempt supply. Thus, for example, where a college incurs professional fees on the sale of, say, some land (exempt supply) with a view to funding the taxable activities of a fully taxable subsidiary, the input tax would not be recoverable.

3·4·6 Acquiring a business as a going concern (TOGC)

With effect from 1 June 1996, where a business is acquired as a TOGC and the assets are used wholly to make taxable supplies, any input tax incurred in acquiring the assets is fully recoverable. Similarly where the assets are used to make wholly exempt supplies, no VAT incurred in acquiring the business is recoverable. Where the assets are to be used for making a mixture of exempt and taxable supplies any input tax incurred (for example, on professional fees) in acquiring the business should be included in the residual input tax calculation.

3·4·7 VAT groups

When considering the attribution of input tax incurred by a VAT group, the use of the goods or services by the group as a whole must be considered. If, for example, a VAT group member uses goods or services it has received to make a supply to a fellow VAT group member who in turn uses them to make an exempt supply, the input tax is wholly attributable to that exempt supply and as such is irrecoverable.

3·4·8 Costs in settling insurance claims

Services and goods in relation to a claim are normally supplied to the policyholder (i.e. the college), not the insurer. As such, the insurer cannot treat the VAT on the supply as input tax. This normally applies to the following:

- Repairs
- Replacement of goods
- Legal costs in relation to a claim
- Supplies where the insurer exercises its right to pursue or defend a claim in the name of the policyholder or the insurer on its behalf (i.e. a surrogated claim), and
- Services of loss assessors.

3·4·9 **Credit notes and business/non-business/ partial exemption calculations**

Colleges are required to apply the following treatment in respect of credit notes received by them and they recover input tax using an agreed business/ non-business/partial exemption method:

- If received in the same period as the original supply, any input tax claim should take account of both the credit note and the original invoice
- If received in a subsequent VAT return period but in the same VAT year, no adjustment is due in the subsequent VAT return period. However, the input tax credit must be included in the annual adjustment calculation
- If received in a subsequent VAT return period but not in the same VAT year, no adjustment is required in the subsequent VAT return period. However, the annual adjustment which included the original supply to which the input tax credit relates should be recalculated to adjust for the effect of the credit note on that VAT year's calculation of recoverable input tax.

Where colleges issue credit notes in respect of supplies made by them, similar rules to those set out above in respect of input tax credit notes apply where the credit has an effect on the business/non-business/partial exemption method operated by a college.

3·4·10 **Reverse charges on services from abroad**

VAT must be accounted for on certain services received from abroad. The notional VAT calculated as output tax is also treated as input tax. However, these services are not regarded as supplies and notional input tax on them can only be claimed by a college to the extent that it is attributable to a taxable supply (i.e. it is determined by the college's business/non-business/ partial exemption method).

3·4·11 **Free supplies of catering and beverages to employees**

Where employees are provided with food and/or drinks free of charge, the college is making a taxable supply, albeit for no consideration. Any input tax attributable to the these supplies is fully recoverable.

3·4·12 Dilapidations

Where a college or its subsidiaries occupies leased premises, the lease agreement may require it to repair any damage to the property and to replace any defective fixtures and fittings. Any input tax is recoverable to the extent that the college or its subsidiaries are able to recover VAT (see 4·9·2).

However, where a college, acting in the capacity of landlord, under the terms of the lease or licence, is required to make the premises ready for occupation, any input tax is attributable to the supply to the future tenant and its recoverability depends on whether the lease is taxable (i.e. the college has opted to tax the property and the option is not disapplied or exempt).

3·4·13 Recovery of input tax (option to tax)

Input tax incurred from the date of the option tax.

3·4·13·1 Recovery of input tax on related expenditure

Once the option to tax has been made by a college in respect of land and/or buildings, it can recover input tax on any related expenditure subject to the normal rules.

3·4·13·2 Exempt supplies in relation to property

The recovery of input tax depends upon whether or not there have been any exempt supplies in relation to the property after 31 July 1989 and before the date of the option to tax.

- Where there have been no such exempt supplies, input tax incurred in relation to the property after 31 July 1989 can be recovered, subject to the normal rules.
- Where any such exempt supply has been made (before the proposed date for option to have effect), written permission must be obtained from HM Customs and Excise before the option to tax is exercised unless the conditions for automatic permission apply. If permission is received and the option exercised, application can be made to HM Customs and Excise to recover a fair and reasonable proportion of the VAT incurred in the period from 1 August 1989 to the date the option has effect, taking into account the exempt use of the property and the intended taxable use. (In practice, where written permission is required from HM Customs and Excise, the application should include a suggested attribution of input tax between non-business, exempt and taxable use.)

3·4·13·3 Repayment of input tax

Where input tax has been reclaimed in relation to the option to tax but the option cannot have effect, any input tax claimed in relation to the option is repayable.

3·4·14 **Domestic accommodation**

Any VAT incurred on domestic accommodation can be treated as input tax. Where there is also an element of private use, apportionment may be allowed between the private and business use.

3·4·15 **Business entertainment**

VAT charged on any goods or services supplied to a college or its subsidiary (i.e. as VAT registered person), or on any goods acquired or imported by it, is excluded from any credit where the goods or services in question are used or to be used for the purpose of business entertainment.

Business entertainment means entertainment (including hospitality of any kind) provided by a taxable person (i.e. a college or its subsidiary registered for VAT) in connection with a business carried on by it, but does not include the provision of any such entertainment for either or both:

- Employees of the taxable person, or
- If the taxable person is a company, its directors or persons engaged in the management of the company

unless the provision of entertainment for such persons is incidental to its provision for others.

HM Customs and Excise regard business entertainment as including:

- The provision of meals and drinks
- The provision of accommodation or facilities for sport or recreation
- Visits to theatres, night clubs, etc.
- Capital goods such as yachts, power boats, private aircraft, etc. used wholly or partly for entertaining
- Expenses of staff acting as hosts.

Hospitality

Where the cost of providing hospitality is passed on as part of the overall charge for a taxable supply, VAT incurred in providing the hospitality cannot be reclaimed. However, if the entertainment is not given gratuitously but is provided under a contractual obligation, it does not fall within the scope of the provision.

For business entertainment purposes, an employee is regarded by HM Customs and Excise to be:

- A director of a company or anyone engaged in the management of a company or a college
- Anyone casually or temporarily employed at sporting and similar events
- A self-employed person who works to the direction of a single employer (i.e. a college), uses tools provided by that employer and is paid on a fixed rate basis.

This does not include pensioners and other former employees, job applicants, shareholders (unless employees in their own right) and families of employees.

Staff entertainment

With regard to staff entertainment HM Customs and Excise accept that where a business (i.e. a college or a subsidiary) provides entertainment to its employees in order to maintain and improve staff relations, it does so wholly for business purposes. The VAT incurred is treated as input tax and recoverable to the extent that the college is entitled to recover input tax incurred in respect of its taxable business activities. Where the entertainment has no discernible business purpose and no connection with business activities, any VAT incurred is not input tax. HM Customs and Excise used to treat only 50% of the VAT incurred on entertainment of employees as input tax to reflect the personal benefit derived (although, depending on the circumstances, the percentage could be lower or higher). Businesses which have apportioned tax incurred on this basis and can show that the expenditure qualifies for full input tax deduction on the revised basis, can claim the additional VAT (subject to the three-year cap). However, with regard to staff parties with guests, for example, organised dinner dances for employees, each of whom is entitled to bring one guest free of charge, any related input tax should be apportioned on the basis that the proportion of the expenditure attributable to the guests constituted business entertainment. The entertainment of the non-employees should not be treated as incidental to the entertainment of the employees in this situation.

Not employees
Where employees take part in any business entertainment provided for persons who are not employees, none of the VAT can be reclaimed.

Mixture of supplies
Where supplies of goods and/or services are used for a mixture of business entertainment and other business use, any input tax may be apportioned.

Some goods may be used for a variety of purposes, e.g. food and drink may be used for trading stock or subsistence meals for employees, staff entertainment or business entertainment. This may be the case in a college's conference facility. Where possible, stocks to be used for entertaining should be kept separately. If, however, it has not been decided how the goods will be used at the time of purchase, a record must be kept of goods used for entertainment so the input tax recoverable can be calculated at the end of each tax period. This record forms part of the VAT records and must be available for inspection by visiting VAT officers.

Helpers at events
Such helpers (e.g. stewards and others) who are essential to the running of the event but are not full-time employees of the organisers can be treated in the same way as full-time employees and input tax may be recovered on their subsistence expenses. The business entertainment provisions do apply to VIPs, journalists and others not involved in actively running the event.

Seminars run by colleges for persons who are not employees
Where it is clear from the promotional literature that the cost of the seminar, etc. includes meals and/or accommodation, input tax can be reclaimed. Where no charge is made, VAT on meals, etc. provided for persons who are not employees cannot be reclaimed. Input tax on any separately itemised charges for hire of a room, equipment, etc. can normally be reclaimed as can VAT on subsistence expenses for employees who are involved in running the activity.

Where meals are supplied to another person who uses them for business entertainment (e.g. where a third party hires college facilities to entertain guests, etc.) any VAT incurred in making the supply may be recovered subject to the college's arrangements to recover input tax. This is because the guests are being entertained by the client. The invoice to the client must separately identify any charge made for the entertainment from other charges made (e.g. promotional fees) and output tax must be accounted for. The business entertainment provisions then apply to the client.

3·4·16 **Legal costs**

For a college to be able to recover VAT on legal costs, the legal services must be supplied for the purposes of the college's business. Any input tax recovery would be subject to a college's business/non-business/partial exemption method.

Where a court orders one party to pay costs to the other party, this sum is not consideration for any supply. Therefore, there is no liability to output tax or entitlement to recover input tax on the part of the paying party.

3·4·17 Motor vehicle costs

3·4·17·1 Purchase of a car

Apart from certain special cases, VAT cannot be reclaimed on the purchase (including acquisition or importation) of a motor car. Purchase means not only outright purchase, but also any purchase under a hire purchase agreement or any other agreement whereby property in the car eventually passes, e.g. a lease-purchase agreement.

3·4·17·2 Leasing or hiring a vehicle

If a motor car is leased or hired, only 50% of the input VAT on the rental charges is available for the credit. There are circumstances where 100% relief is available primarily where the vehicle is a business asset being used for hire or for self-drive.

3·4·17·3 Identifying qualifying cars on leasing invoices

HM Customs and Excise have agreed with a main leasing trade organisation a recommended form of invoice for leasing companies to adopt for lettings. The invoice must clearly identify whether or not the car is a qualifying car and, if it is, the amount of VAT which is potentially subject to the 50% input tax restriction. Where the leasing company has not indicated whether the car is a qualifying car or not, the lessee can assume that a car with an 'M' registration or earlier prefix is non-qualifying and recover VAT in full, subject to the normal rules. A car with an 'N' or later registration prefix should normally be treated as a qualifying car and the 50% restriction applied. Full input tax relief may however be claimed on rental charges on 'N' registration cars if the hirer incurred any VAT on rental on it before 1 August 1995.

The requirement to identify whether or not a car is a qualifying car does not apply to self-drive hire cars. Unless there is evidence to the contrary, any self-drive hire car should be treated as a qualifying car if it has a 'K' registration or later prefix.

3·4·17·4 Charges subject to the 50% restriction

There are frequently two distinct elements of the rental: basic rental for the provision of the car (including depreciation, funding cost, and a proportion of overheads/profit) and an optional additional charge (covering repairs, maintenance and roadside assistance and a proportion of overheads/profit). Provided the additional charges are separately described in the contract hire agreement and periodic invoices and are genuinely optional, VAT on the basic rental is subject to the 50% restriction; VAT on the optional charge is recoverable in full subject to the normal rules. VAT on an excess mileage charge should similarly be separated into two distinct elements on a basis identical to the split of the rental.

3·4·17·5 **Rental rebates**

Where a lessor sells a car at the end of a lease and uses the proceeds to rebate the monthly rental payments made to the lessee, a lessee who incurred a 50% input tax restriction on the rental charges on the car need only adjust for 50% of the VAT on the credit note issued by the lessor for rebate of rentals.

3·4·17·6 **Early lease termination**

Where a lease is terminated early, the leasing company may treat both the termination payment and any rental rebate as taxable or treat both as outside the scope. If it chooses to tax, it will normally set off the termination payment against any rebate and issue a VAT invoice for the difference.

Where the termination payment exceeds the rebate, any VAT is not subject to the 50% restriction. Where any rebate exceeds the termination payment, the leasing company must issue a credit note. A lessee who incurred a 50% input tax restriction on the rental charges need only adjust for 50% of the VAT on the credit note.

3·4·17·7 **Self-drive hire (daily rental)**

The 50% restriction applies to self-drive hire as well as leasing on a longer-term basis. However, by concession, HM Customs and Excise are currently prepared to accept that it does not apply if a car is used for five days or less for use in the business. If a car is hired for more than five days, the restriction applies if the car is to replace a car normally available for private use. It also applies to other hirings of more than five days unless sufficient records are kept to demonstrate that the car was hired and used for business purposes.

3·4·17·8 **Interaction with business/non-business/ partial exemption method**

The proportion of the 50% input tax restriction will be determined under a college's business/non-business/ partial exemption method.

3·4·17·9 **Repairs and maintenance**

If a vehicle is used for business purposes, VAT on repairs and maintenance can be treated as input tax provided the work done is paid for by the college. This applies even if the vehicle is used for private motoring and even if no VAT is reclaimed on any road fuel in order to avoid use of the scale charges. VAT on repairs, etc. covered by a mileage allowance or relating to a vehicle used by a sole trader or partner for private motoring only, cannot be treated as input tax.

3·4·17·10 **Accessories**

VAT charged on accessories fitted to a car when purchased cannot be reclaimed even if optional and separately itemised on the sales invoice. VAT on accessories subsequently purchased can only be treated as input tax if:

- The vehicle is owned by the business or used in the business but not owned by it (e.g. an employee's or director's own car)
- The accessory has a business use (e.g. a telephone).

3·4·17·11 **Fuel bought by the college**

VAT on all fuel purchased by the college can be reclaimed subject to the normal rules. This applies even if it is used for private motoring, if the business is partly exempt and where there is non-business (as distinct from private) motoring. If the business makes supplies of fuel where the scale charges do not apply, VAT on all purchases can be treated as input tax, but output tax must be accounted for on any private use of fuel.

3·4·17·12 **Fuel bought by employees**

Road fuel bought by an employee of a college is treated as having been supplied to a business for business purposes provided one of the following methods of reimbursement is adopted:

- The employee is reimbursed for the actual cost of the fuel
- The employee is paid an amount determined by reference to the total distance travelled by the vehicle (whether or not including private or non-business mileage) and the cylinder capacity of the vehicle.

Normally this will take the form of a mileage allowance which may also cover reimbursement of other costs. If so, input tax on road fuel is calculated by multiplying the fuel element of the mileage allowance by the VAT fraction.

HM Customs and Excise will require the college to keep a record for each employee showing:

- Mileage travelled
- Whether journeys are both business and private
- The cylinder capacity of the vehicle
- The rate of the mileage allowance
- The amount of input tax claimed.

HM Customs and Excise do not require the business to keep the invoices for the fuel bought by the employee. In most cases the expense claim will give enough information for the basic record.

Reimbursement by either method can also cover fuel bought for private use although, in such a case, the business must then account for output tax on the private use using the scale charges.

3·4·18 Subsistence costs

3·4·18·1 Flat rate

Where an employee of a college is paid a flat rate for subsistence expenses, no VAT can be claimed as input tax. If the college pays the actual cost of the supplies, input tax incurred can be reclaimed as below. If the business pays a proportion of the actual costs, it can reclaim as input tax the VAT fraction of the amount it pays.

3·4·18·2 Meals

If the college provides canteen facilities, all input tax incurred in providing these facilities can be recovered subject to the normal regulations. Any VAT incurred on meals for college employees can be treated as input tax. Where meals, etc. are provided away from the place of work, e.g. on a business trip, the VAT incurred on the employee's meal can be claimed as input tax provided that any entertainment is secondary to the main purpose of the trip. If the business trip is made solely for the purpose of business entertainment none of the input tax is recoverable.

3·4·18·3 Hotel accommodation

All VAT incurred on accommodation for a college's employees when away from the normal place of work on business trips can be treated as input tax.

3·4·19 Removal costs

Where a college reimburses employees (including new employees) for removal costs, the college can treat VAT incurred as input tax if the costs relate to:

- Estate agent's and solicitor's fees
- Storage and the removal of household and personal effects
- Services such as plumbing in washing machines or altering curtains.

Where a proportion of costs is reimbursed, a similar proportion of the input tax can be claimed. It does not matter if the invoices are addressed to the employees.

3·4·20 Pre-registration input tax

3·4·20·1 Basic points

It is the case that not all colleges are registered for VAT and in the future it may be that they wish to or be required to. Increasingly colleges are setting up trading subsidiaries which register for VAT. In all these cases there may be instances where a college incurs VAT before registering for VAT. VAT incurred before registration is not input tax; however, it can be treated as such subject to certain conditions. The VAT should be claimed on the first VAT return required to be made following registration (before 1 May 1997, on the first VAT return made). HM Customs and Excise may allow the claim to be made on a later return but, with effect from 1 May 1997, cannot allow a claim to be made more than three years after the date the first return was required. Any claim must be supported by invoices and other evidence as HM Customs and Excise require.

3·4·20·2 **Input tax on goods**

HM Customs and Excise may allow a taxable person (i.e. a college or its subsidiary registered for VAT) to treat as input tax any VAT on goods supplied to them before the date on which it was (or was required to be) registered or paid by him on the acquisition or importation of goods before that date provided the following conditions are satisfied.

- The goods are for the purpose of an activity which either was carried on or was to be carried on by the college or its subsidiary at the time of the supply or payment.
- The goods have not been supplied by or (unless HM Customs and Excise otherwise allow) consumed by the college or the subsidiary before the date with effect from which it was (or was required to be) registered. HM Customs and Excise deem this condition to be satisfied if the goods have been used to make other goods which are still held at that date.
- With effect from 1 May 1997, the goods must not have been supplied to, or imported or acquired by, the college or the subsidiary more than three years before the date with effect from which it was (or was required to be) registered. This does not apply where the college or the subsidiary was registered before 1 May 1997 and did not make any returns before that date.
- All the normal rules allow the input tax to be reclaimed.
- A stock account is compiled (and preserved for such a period as HM Customs and Excise require) showing separately quantities purchased, quantities used in the making of other goods, date of purchase and date and manner of subsequent disposals of both such quantities.

3·4·20·3 **Input tax on services**

HM Customs and Excise may allow a taxable person (i.e. a VAT-registered college or its subsidiary) to treat as input tax any VAT on services supplied to it before the date on which it was (or was required to be) registered provided the following conditions are satisfied:

- The services are for the purpose of an activity of the entity which either was carried on or was to be carried on by it at the time of such supply
- The services have not been supplied by the taxable person (i.e. the college or its subsidiary) before the date with effect from which it was (or was required to be) registered
- The services have not been performed on:
  a. Goods which have been supplied by or (unless HM Customs and Excise otherwise allow) consumed by the taxable person (i.e. the college or its subsidiary) before the date with effect from which he was (or was required to be) registered (e.g. repairs to a machine sold before registration), or
  b. With effect from 1 May 1997, goods which have been supplied to, or imported or acquired by, the college or its subsidiary more than three years before that date. This does not apply where the college or subsidiary was registered before 1 May 1997 and did not make any returns before that date.
- The services have not been supplied to the college or its subsidiary more than six months before the date with effect from which it was, or was required to be, registered
- All the normal rules allow the input tax to be reclaimed
- A list showing the description, date of purchase and date of disposal (if any) of the services is compiled and preserved for such period as HM Customs and Excise require.

3·4·20·4 **Input tax on supplies before incorporation**

HM Customs and Excise may allow a body corporate (including a company, charity, association or college) to treat as input tax any VAT on goods obtained for it before its incorporation, or on the supply of services before that time for its benefit or in connection with its incorporation, provided the following conditions are satisfied:

- The person to whom the supply was made or who paid VAT on the importation or acquisition:
  a. Became a member, officer or employee of the body (i.e. a college or its subsidiary) and was reimbursed (or has received an undertaking to be reimbursed) by the body for the whole amount of the price paid for the goods or services
  b. Was not at the time of supply, acquisition or importation a taxable person (i.e. registered for VAT), and
  c. Imported, acquired or was supplied with the goods or received the services or the purpose of a business to be carried on by the body (i.e. a college and its subsidiary) and has not used them for any purpose other than such business.
- The conditions for recovery of input tax on goods or, as the case may be, services as detailed above are satisfied. In the case of pre-incorporation supplies, the references in those conditions to supplies, etc. of goods and services to and by the taxable person (i.e. a college or its subsidiary registered for VAT) before registration are to be taken as references to such supplies to and by the person who obtained the supplies for the company before registration.

3·4·21 **Post deregistration input tax**

There may be instances where a college wishes to deregister for VAT purposes. This may be because the value of a college's taxable supplies is well below the VAT registration limit and for administrative reasons it would simplify matters. As a general rule, input tax cannot be claimed on supplies received after the date of deregistration. However, on a claim, HM Customs and Excise may refund to a person any VAT on services supplied to it after the date from which it ceased to be (or to be required to be) registered and which relate to taxable supplies of the college or its subsidiary carried on by it before deregistration. With effect from 1 May 1997, no such claim can be made more than three years after the date on which the supply of services was made (unless the college or its subsidiary ceased to be registered, or ceased to be required to be registered, before 1 May 1997 and the supply was made before that date).

This covers, for example, solicitors' and accountants' services which cannot be claimed on the final returns as the invoices are not received in time. It does not include VAT incurred in disposing of business premises after deregistration where the supply is exempt but, if such a disposal is a possibility, HM Customs and Excise can be requested to delay cancellation of registration for up to six months. Claims should be made as soon as possible after cancellation of registration on Form VAT 427. The relevant invoices must be submitted.

3·4·22 **Belated claims for input tax**

Where a partially exempt entity such as a college makes a belated claim for input tax, for example, where it has not recovered a proportion of its residual business input tax, it can only recover input tax that it would have been entitled to had it been claimed in the period in which it was incurred. The college is required to determine the amount that is recoverable using the rules in force at that time and apply any agreements (i.e. its business/non-business/partial exemption method) it has reached with HM Customs and Excise in respect of the period or periods in question. Account should be taken of the effect of this belated claim and how it arose affects input tax already claimed. If the value being claimed is below £2000 it should be included on the claimant's next VAT return or where it exceeds this amount a voluntary disclosure will be required to be submitted to HM Customs and Excise. It is likely that HM Customs and Excise will want review any claim of this nature and almost certainly they may want to visit the college to establish the credibility of the claim and the reasons for it arising.

4 Land, property and construction services

4·1 Introduction

In the following sections, *italicised* words or phrases are defined in the glossary (see Appendix 9). VAT legislation on land and property is particularly complex. Given that substantial amounts can be invested by colleges in property and construction, the adverse VAT consequences of incorrect analyses can be correspondingly large. Accordingly, it is generally recommended that further advice should be taken on any areas of doubt, and not simply in those areas that have been flagged in this chapter as being particularly complicated.

4·2 Construction services

The basic principle in the construction industry is that all supplies are standard-rated, unless they fall into one of the specific exceptions outlined below.

4·2·1 New relevant charitable use buildings

The service of construction, and the goods supplied in conjunction with such a service, of a new *relevant charitable use* building intended to be used solely for a *relevant charitable use*, can be zero-rated. However, it is important to note that zero rating does not extend to the services of sub-contractors.

For such services to be zero-rated, a certificate needs to be issued to the builder by the person intending to use the property stating that the work qualifies for zero rating. The form such a certificate should take is mandatory and an example is provided in Appendix 4. It is the responsibility of the person who issues the certificate to ensure it is correct, and that the building it relates to does qualify for relief. Where the certificate is not correct, the issuer may be subject to a penalty.

Where the building is to have mixed usage, that is to say partly a charitable purpose and partly some other purpose, it may be possible to zero rate work on the qualifying part or parts. In this case, supplies should be apportioned, standard rating those for the non-qualifying part and zero rating those for the qualifying part. You should note that HM Customs and Excise do not specify how costs should be apportioned. If it cannot be shown what parts qualify under the *relevant charitable use* clause and which do not, or if the same part of the building is used for charitable purposes at some times and for non-charitable purposes at other times, then the whole construction service ought to be standard-rated.

However, the non-qualifying use can be ignored where:

- The building will be used for a *relevant charitable use* for more than 90% of the total time the building is available
- In the case of non-business educational establishments, the number of fee-paying students is less than 10% of total students calculated on a full-time equivalent basis.

4·2·2 New relevant residential use buildings

The service of construction, and the goods supplied in conjunction with such a service, of a building intended for use solely for a *relevant residential use* is zero-rated.

As with *relevant charitable use* buildings, it is necessary for the person intending to use the property to issue a certificate to the constructor to qualify for zero rating. Such a certificate should be issued before the supply is made. An example of such a certificate is given in Appendix 4. Again, it is the responsibility of the issuer to ensure the correctness of the certificate.

Again, as with *relevant charitable use* buildings, it is necessary to apportion the costs where a building is partly used for *relevant residential use*, and partly for some other purpose. Again, the non-qualifying use can be ignored where it is less than 10% of the total time the building is available for use. Or in the case of education establishments, where the number of fee-paying students is less than 10%.

4·2·3 Alterations and refurbishments

Zero rating does not apply to the conversion, reconstruction or alteration of an *existing building*. Nor do refurbishments qualify for zero rating. This applies even where the building is a *relevant residential* or *charitable use* building.

4·2·4 Extensions and annexes

Extensions and annexes to *existing buildings* are normally standard-rated.

However, where an annex is constructed and is intended for use solely for a *relevant charitable purpose*, it can be zero-rated if:

- It is capable of functioning independently from the *existing building*, and
- The only or main access to:
  a. The annex is not via the *existing building*
  b. The *existing building* is not via the annex.

This provision does not allow the enlargement of or extensions to existing charity buildings to be zero-rated. Again, when seeking to zero rate construction services, it is necessary to issue the main contractor with a certificate, stating that the work qualifies for zero rating. An example of such a certificate is included in Appendix 4.

4·2·5 Specific inclusions and exclusions from zero rating

4·2·5·1 Professional services

Those services provided by an architect, surveyor or other such person working in a similar consultancy or supervisory capacity can never be zero-rated. Such professional services must always be standard-rated, even if they relate to buildings which qualify for zero rating.

4·2·5·2 Items ordinarily installed

In certain circumstances, a person supplying construction services, which qualify for zero rating, can also zero rate items ordinarily installed. These are building materials that HM Customs and Excise accept can be zero-rated when incorporated into a dwelling or other qualifying building. A list of such items can be found in Appendix 5.

4·3 Self-supply of construction services

4·3·1 Basic outline

In certain circumstances it is held that a self-supply of construction services has taken place. This is the case when a person, in the course or furtherance of his business, uses his own employees to construct one of the following:

- A building, or
- An extension to any *existing building*, such that an area of not less than 10% of the original building is added, or
- A civil engineering work.

It also applies when your own employees carry out any demolition work as part of any of the works listed above.

When such a self-supply takes place, the service is treated as both supplied to and by the business. As such, output VAT must be accounted for on the open market value of the services provided. This output tax can though be reclaimed as input in the same period VAT return, to the extent that it applies to taxable supplies.

4·3·2 Monetary limits

The self-supply rules are subject to a de minimis limit, this is currently £100 000. Therefore, the rules will apply when the open market value of any self-supply is over £100 000. Supplies that would ordinarily be zero-rated can be excluded from this amount.

If the value of any self-supply exceeds the capital goods scheme limit (currently any building or refurbishments with a value over £250 000) then VAT adjustments will be required in future years. The capital goods scheme is covered in more depth in 3·4·2.

4·3·3 Further advice

This is a complex area of VAT law and further advice is recommended where the self-supply rules are potentially an issue.

4·4 Zero-rated freehold sales

4·4·1 New relevant charitable use buildings

The first grant of a *major interest* in a new *relevant charitable use* building is zero-rated. Subsequent *grants* are exempt from VAT. Technically, any such exempt supplies would be subject to the option to tax, but in practice the option would be likely to be disapplied (see 4·7·3).

4·4·2 New relevant residential use buildings

The first grant of a *major interest* in a new *residential use* building is zero-rated. Subsequent *grants* are exempt from VAT. Again, this would be subject to the option to tax, however in practice the option would typically be disapplied (see 4·7·3).

4·4·3 Part-constructed buildings

Where a building is purchased or sold only part constructed, it will qualify for zero rating, providing the sale of the building would have been zero-rated if complete.

4·4·4 Converted buildings

The first grant of a *major interest* in a *non-residential* building or a *non-residential* part of a building which has been converted into a building intended for use as a dwelling or for a *relevant residential use* can be zero-rated. As above, all subsequent *grants* will be exempt, subject to the option to tax, although in practice the option might well be disapplied (see 4·7·3).

4·5 Change of use of zero-rated buildings

4·5·1 Basic outline

In certain circumstances, a change of use of a building qualifying for zero rating, i.e. a new *residential* or *charitable use* building, will lead to standard rate VAT being charged.

4·5·2 Trigger events

There are two possible events that will trigger a VAT liability in such a case. Subject to the relevant time limits (see below), they are:

- The disposal of any building which qualified for zero rating, which is not intended to be used as a *relevant residential* or *charitable use* building after the sale. In such a case, the sale will be standard-rated and not exempt.
- A change of use without a change of ownership. Where the owner or *major interest* holder of a property changes its use from a *relevant residential* or *charitable use* building to some other purpose, a self-supply is deemed to have taken place. This means that the owner is deemed to have supplied himself a non-qualifying building. However, by concession, where the non-qualifying use represents less then 10% of the overall use, HM Customs and Excise will ignore such use.

4·5·3 Time limits

The above two provisions apply only within 10 years of the completion of the building. Generally speaking, a building is deemed completed when it is finished according to the original plans.

4·5·4 Calculation of the self-supply charge

Where a self-supply occurs, the VAT chargeable will be the amount that would have been due if the original supply had been standard-rated, rather than zero-rated. Thus, effectively standard-rated VAT is applied to the original supply.

4·5·5 Further advice

This is another complex area of VAT legislation, it is therefore suggested that further advice be sought where you believe there has been a change in the use of a qualifying building.

4·6 Other freehold sales, grants of leasehold interests and lesser rights over land

4·6·1 The basic rule

The basic rule for freehold sales and the granting of leases, licences and other rights over land is that they are exempt from VAT. This rule is of course subject to all the provisions mentioned in this guide which would cause a supply to be taxable at either the standard rate or zero rate including the option to tax (see 4·7). The main standard-rated exceptions are listed below. If you are in any doubt over whether a supply is exempt, you should seek professional advice.

Note that in the following paragraphs 'new' is taken to mean a property completed in the last three years. A building will be considered complete from the earlier of the date of full occupation or the date on which a certificate of completion is issued by an architect or surveyor.

4·6·2 Exceptions to the basic rule

4·6·2·1 Certain part-completed/new buildings

The grant of the freehold of a part completed or a new building, which is not designed as a dwelling, nor intended for use for a *relevant residential* or *charitable use*, is standard-rated and not exempt.

4·6·2·2 Part completed/new civil engineering works

Civil engineering works which are sold only part complete, or sold new, are standard-rated and not exempt.

4·6·2·3 Sleeping accommodation

Sleeping accommodation, such as that provided in a hotel or board house, or by any college that offers accommodation as part of conference facilities, is standard-rated. However, sleeping accommodation provided to students is exempt, as a supply closely connected to the provision of education. Note that this provision is dependent upon the supply of education and accommodation being offered by the same body (see 1·7·3).

4·6·2·4 Holiday accommodation

The grant of any interest in, right over or license to occupy *holiday accommodation* is not exempt, but standard-rated.

4·6·2·5 **Car parking**

When a fee is charged for the use of car parking facilities, this is standard-rated. By concession, when students are charged a parking fee by an eligible education establishment, this is an exempt supply (see 1·5·7).

4·6·2·6 **Sports facilities**

Generally, the letting of any facility designed or adapted for the playing of sport, or other such physical recreation, is standard-rated. However, note that general purpose halls or dining rooms, which merely have floor markings, are not considered to be sports facilities, as such they are exempt when let out, even if let for the playing of sport. The hire of sports facilities for non-sport activities will be VAT exempt subject to option to tax.

Exemption also applies when sports facilities are supplied by a non-profit-making body (see 1·7·5).

In certain other circumstances, it is also possible to exempt the letting of sports facilities, this is when the facilities are let for a longer period. The two circumstances in which such a let can be exempt are:

- If it is let for a continuous period exceeding 24 hours, or
- Subject to the following conditions, it is let for a series of ten or more periods.

The conditions to be met are:

a. Each session is for the same sport or activity and at the same place (though a different court, pitch or lane may be used each time).
b. The interval between each letting is at least one day, and not more than 14. No adjustment can be made for public holidays within the 14 day period.
c. The series of lets are paid for as a whole, and there is written evidence to that effect.
d. The person to whom the facility is let has exclusive use of the facility.
e. The person to whom the facilities are let is either a school, a club or an association representing affiliated clubs. HM Customs and Excise accept that this is a loose definition and thus allow the lettor to decide if the letting body can be described as a club or an association. Though in some cases it may be necessary to seek advice on this matter.

4·6·2·7 **Put and call options**

Put and call options and similar rights over land are specifically excluded from the exemptions and are therefore standard-rated. This is however a complex area and it is recommended that professional advice be taken on such matters.

4·6·2·8 **Sundry**

The following are all excluded from the exemption and thus standard-rated:

- The grant of a right or licence to fish or to hunt game
- The grant of caravan/tent pitches
- The grant of a right to fell and remove timber
- The grant of a ship mooring or aircraft hangar
- The grant of a right to occupy a box or seat at a theatre, stadium or concert hall.

If any of the above may be relevant, then reference should be made to Public Notice 742 for further details.

4·7 Option to tax

4·7·1 Effect of opting to tax

The option to tax, more properly known as election to waive exemption, is an option taken to standard rate all future *grants* of any interest in, or rights over, the land or building. Thus, all future sales and leases of that property by the person who made the election will be taxable at the standard rate rather than exempt. As a result of such supplies becoming taxable, the owner of the property will generally be able to recover any input tax relating to the supply. When the option to tax is taken, it applies both to the building and the land, and buildings within its *curtilage*.

4·7·2 The scope of the option

In relation to buildings, the option to tax applies to the whole building and the land within its *curtilage*. For these purposes, the following are taken to be single buildings:

- Buildings linked internally or by covered walkways
- Complexes consisting of a number of units grouped around a fully enclosed concourse.

In relation to land, the scope of the option is solely the land specified in the election. The option does not apply to adjoining land or to buildings later constructed on the land.

4·7·3 Basic disapplications

In certain circumstances, the option to tax is disapplied. They are when the grant is made in relation to:

- A building or part of a building intended as a dwelling or solely for a *relevant residential use*
- A building or part of a building intended for a *relevant charitable use*. However, the space used by a charity for business purposes, e.g. an office, would be taxed if it is supplied for a business purpose and not merely as an area incidental to, and within, the charity's non-business operational establishment
- A pitch for a *residential* caravan
- Facilities for mooring a *residential* houseboat
- A building supplied to a relevant housing association, which has given the supplier a certificate stating that the land is to be used for the construction of a building to be used as a dwelling or for a *relevant residential use*.

4·7·4 Anti-avoidance disapplication

Anti-avoidance provisions have been introduced in relation to the option to tax. They are designed particularly to prevent partly taxable businesses, such as FE colleges, from using lease and lease back arrangements to recover more input tax than they would ordinarily be entitled to.

The rules are extremely complex and it is recommended that professional advice be taken in relation to any leasing arrangement with a subsidiary or other associated entity, or if you are in any way financing the development of a building which is to be leased to you.

4·7·5 Notification procedures

For the option to tax to have legal force, HM Customs and Excise must be notified in writing within 30 days of the election. Such notification should be sent to the local VAT office, and should state unambiguously what property is covered by the option to tax. An example of such a notification letter is included in Appendix 6.

In certain circumstances, it is necessary to obtain prior permission from HM Customs and Excise before exercising the option to tax. Briefly, if any previous exempt supply has been made in respect of the property, prior permission will be required. This is also commented upon in Public Notice 742, paragraph 8·8.

4·7·6 Recovery of input tax incurred before the option

In some circumstances, it is possible to recover all, or a proportion of, the input tax incurred prior to the effective date of the option. This is commented upon in Public Notice 742, paragraph 8·8.

4·7·7 Revocation

Prior to 1 March 1995, the option to tax was irrevocable. However, since that date, it has been possible to withdraw or revoke an option to tax, under one of the following provisions.

- It is possible to revoke the option in the initial three month period provided that:
  a. No VAT has been charged on any rent
  b. Input tax, above that which would have been recoverable under normal partial exemption rules, has not been recovered
  c. The property has not been sold as a transfer of a going concern.
- It is possible to revoke the option after it has been in effect for 20 years. To revoke an option to tax, you should contact your local VAT office, and should expect permission to be freely given provided that one of the two criteria is met.

4·8 Protected buildings

4·8·1 Definition of protected building

A protected building is one which is for, or is intended for, use as a dwelling or for use solely as a *relevant residential* or *charitable use* building, and which is either:

- A listed building, within the meaning of:
  a. The Planning (Listed Buildings and Conservation Areas) Act 1990, or
  b. The Planning (Listed Buildings and Conservation Areas) (Scotland) Act 1997, or
  c. The Planning (Northern Ireland) Order 1991, or
- A scheduled monument, within the meaning of:
  a. The Ancient Monuments and Archaeological Areas Act 1979, or
  b. The Historic Monuments Act (Northern Ireland) 1971.

4·8·2 Sale of substantially reconstructed buildings

The first grant of a *major interest* in a protected building which has been *substantially reconstructed* is zero-rated.

4·8·3 Approved alterations

The supply of construction services and materials provided in the course of *approved alterations* of a protected building are zero-rated. Explicitly excluded from this provision are the services of an architect, surveyor or any person acting as a consultant or in a supervisory capacity.

The supply of building materials intended to be used in such an *approved alteration* and to be incorporated into the protected building can also be zero-rated. However, those fixtures and fittings, as listed in Appendix 5, will be specifically excluded and therefore standard-rated.

Note that works of repair or maintenance, or any incidental alterations arising from such work, are not included in this provision.

4·8·4 Limitation of zero rating

Where alterations are carried out to a building separate from, but within the *curtilage* of, the protected buildings, they will not qualify for zero rating, unless that building is also protected.

4·8·5 Further advice

If there is any doubt about what constitutes a protected building, an *approved alteration*, or a substantial reconstruction, then it is suggested that further advice is sought. The limitations of zero rating in this area have not been precisely determined, and further advice should be obtained in any cases of doubt.

4·9 Extraordinary transactions

4·9·1 Rent-free periods

It is the view of HM Customs and Excise that there are two forms of rent-free period. The first is a true rent-free period, when the tenant has use of land or property and has to provide nothing in return for this service. This would be the case when, for example, a rent-free period is offered as compensation for a delay in occupancy. In this first case, there is no supply for VAT purposes and there is no VAT liability.

The second category is when rent is free in monetary terms but some sort of service has to be performed by the tenant; for example, the tenant may be required to redecorate or renovate a property in return for a rent-free period. In such an agreement, the rent-free period is actually given as non-monetary consideration for a supply of services.

In this second example, HM Customs and Excise consider that there is a VAT liability as a supply takes place, and that the landlord should account for output VAT. This is calculated on the open market value of the rent-free period normally equivalent to the value of the services provided by the tenant.

4·9·2 Dilapidation payments

A landlord will normally charge a dilapidation payment where a tenant has not fulfilled the obligations of a tenancy which has terminated. This would arise when the landlord has to carry out repairs and maintenance to return a property to the standard it was at when originally let. Such payments are compensation payments and, as such, are outside the scope of VAT as they are not consideration for a supply.

4·9·3 Surrenders

A surrender is where a tenant agrees to prematurely end a lease in return for a payment from the landlord. In such circumstances, the tenant is making a supply of services for a consideration to the landlord which is exempt. However, where the landlord has opted to tax, the supply will be standard-rated.

4·9·4 Reverse surrenders

A reverse surrender is where the tenant pays the landlord to end the lease. Again, such a payment is exempt unless the landlord has opted to tax the property, in which case the payment will be subject to VAT.

4·9·5 Assignments

An assignment occurs when a tenant transfers their lease to another party (the assignee). Further advice should be sought in connection with assignments, as the correct VAT treatment is currently the subject of developing case law.

4·9·6 Reverse assignments

A reverse assignment occurs when a tenant pays an assignee to take over a lease. Further advice should be sought in connection with reverse assignments, as the correct VAT treatment is currently the subject of developing case law.

4·9·7 Reverse premiums/inducements

Reverse premiums or inducements are paid by a landlord to a prospective tenant to encourage them to enter into a lease, or payments by a tenant to a third party to accept a sub-lease. It has been HM Customs and Excise's view that such payments should be standard-rated. There is, however, case law which suggests that this is not the correct treatment and that such payments should be exempt, subject to the option to tax. It is therefore suggested that further advice is sought on this matter should such a transaction arise.

4·10 Specific reliefs for charities

In certain circumstances it is possible for charities, such as FE colleges, to qualify for reliefs on work undertaken to enable disabled access. Such relief would apply to the construction of ramps, the widening of doorways or the alterations of washrooms and lavatories. For further details see 2·4.

5 Printing, imports, exports and subsidiaries

5·1 Introduction

The purpose of this chapter is to summarise those miscellaneous topics that are less frequently encountered. It outlines the special rules applicable if you print your own stationery and reading matter. These rules are designed to place a college in the same VAT position had an external printer done the work.

This chapter also covers the situations of exporting or importing goods and services. Unfortunately, this is an area where the rules are diverse since goods and services are treated differently, while trade with the European Community as opposed to the rest of the world, and also business *versus* private customers, also come under different procedures.

Finally, the subject of subsidiary companies is introduced. Subsidiaries are not used by all colleges, though about half the sector has them. The reasons for subsidiaries are diverse, ranging from tax mitigation and encouraging commercial attitudes to allowing others to participate in partnership with colleges.

5·2 Self-supply of printed matter

The self-supply of printed matter refers to the situation where a college produces in-house its own stationery and other printed matter for use in its business. To put a college in the same VAT position as would be the case if the printed matter had been bought-in, the college has to charge itself VAT on the value of self-produced printed matter.

The self-supply of printed matter only applies if the value of self-produced printed matter used for business (e.g. for support of the fee paying students' activities) exceeds the VAT registration threshold, presently £51 000. The order applies only to printed matter, not items produced by typewriting, duplicating or photocopying.

The self-supply VAT charge is calculated on the value of the printed matter had it been bought externally. Consequently, the self-supply value is to be calculated by reference to a costing record of printing materials, labour, machine usage, apportioned overheads and a fair profit margin.

For example, if a college prints its own stationery and this all relates to exempt business activities, and costs £100 000 in labour and materials, plus £20 000 overheads and 10% notional profit, the VAT due on the self-supply will be 17·5% of £132 000.

The VAT due on the self-supply has to be declared as output tax on the VAT return which covers the period when the self-produced printed matter is intended to be used. The output tax due on the self-supply is only reclaimable if it relates to a taxable activity of the college (see Chapter 3).

The input tax incurred on the purchases used to produce the printed matter is reclaimable. In the above example, if the material costs were £50 000 plus VAT, this VAT will be deductible.

The self-supply of printed matter applies to both standard-rated and zero-rated items. The self-supply of printed matter can require unregistered colleges to be VAT registered if the value of the self-supplies related to business activities exceeds the VAT registration threshold.

5·3 Import of goods and services general

The VAT treatment of imports depends on whether the supplier is from another EC country or is external to the EC, but can also depend on the type of service or good. Appendix 7 lists the countries of the EC.

Generally it should be noted that, where a college imports or exports goods and services, invoices should be converted into sterling. The rate of exchange should be the current rate or, alternatively, a college can use a rate determined in accordance with Public Notice 700.

5·4 Imports of goods from outside the EC

When goods are imported from outside the EC, they will be assessed for their VAT liability by HM Customs and Excise at the port of arrival. Goods that are zero-rated in the UK will not be subject to import VAT; however, other goods will be liable to VAT. The VAT due will be calculated on the cost of the goods, including any customs duty, excise duty and delivery costs.

If a college is VAT registered, the import agent should be given the college VAT number, prefixed with '000'. This is called a TURN number.

The VAT due at import normally has to be paid immediately in order to release the goods. Where imports are regular, it is possible to set up a bank guarantee, known as a deferment account, which allows VAT to be settled midway through the month following importation.

Provided a TURN number has been given to HM Customs and Excise at the time of importation, a C79 import VAT certificate should be sent to the college midway through the next month. The C79 is the only document which can be used to reclaim VAT on imports. The recovery of VAT on imports follows the normal rules for input tax (see Chapter 3).

5·5 Import of goods from other EC countries

The import (acquisition) of goods from the EC is treated differently dependent upon whether the recipient college is VAT registered. If the college is not registered, an EC supplier should charge the VAT applicable to its own country. If the college is VAT registered, the supplier should be notified of the college's VAT number, prefixed with 'GB'. The VAT due on the goods is then calculated under the reverse charge procedure and should be declared on the college's VAT return (in box 2) as acquisition VAT. The net value of acquisitions has to be reported in box 9.

The reverse charge procedure is necessary to eliminate the possible distortion of competition caused when comparing UK and non-UK suppliers. To restore the VAT neutral position, VAT is self-charged (at the appropriate rate) on top of the value of the goods. For example, if a French supplier sells a college a £5000 machine, the reverse charge VAT is £825.

The calculation of acquisition VAT follows the normal rules in determining VAT liability. For example, a computer would be standard-rated, while a book would be zero-rated.

5·6 Import of services from the EC and outside the EC

This applies if a college imports services for its business activities as opposed to non-business free education activities.

Certain imported services (which are listed in Appendix 8) are liable to a self-supply or reverse charge. This is to place them in the same VAT cost position as if they had been supplied by a UK-based supplier. Colleges may come across the following examples of reverse charge services:

- Charges to access data and information services
- Charges for copying text, music, etc. off the Internet
- Charges from overseas resident consultants, engineers and professionals
- Hire of equipment (except means of transport)
- Software licences
- Job advertising services.

The rules do not apply to services consumed abroad, e.g. hotels, lectures, conferences, trade show admissions and travel costs. The VAT due on reverse charge services has to be declared as output tax (box 1 on the VAT return) in the period in which the supplier is paid. The VAT calculated on reverse charge services is only reclaimable if it relates to taxable activities. If it relates to the exempt activities of a college, the reverse charge VAT is an absolute cost.

5·7 Export of goods to other EC countries

The export (dispatch) of goods to another EC country is zero-rated provided the customer provides you with a VAT number. For example, a French customer should provide their French VAT number. If the customer cannot give you a VAT number, you must apply the normal UK VAT, subject to the Distance Selling Rules (see 5·10).

When you zero rate a dispatch of goods, you must retain documentary proof of shipment. For example, certificates of shipment, delivery notes, transportation invoices, etc. The value of goods exported to EC businesses must be shown in box 8 of the VAT return (see 5·10).

5·8 Export of goods outside the EC

Where goods are exported from the UK to a customer outside the EC, the supply is zero-rated. This is conditional upon retaining proof that the goods have been exported. For example, shipping documents, certificates of export or postal export certificates. Without proof of export, the goods are subject to the normal UK VAT rules.

5·9 Export of services

The treatment of services depends on their category and also on the location and status of the customer.

First, it is important to distinguish two categories of service colleges will often come across. Certain services, for example education, catering, accommodation, entertainments, exhibitions, are supplied where they physically take place. These services are liable to normal UK rules if they take place in the UK. If they take place outside the UK, they are outside the scope of UK VAT. If they take place in another country, they could be liable to local VAT registration requirements and thus specific advice should be sought.

Intellectual services (see Appendix 8) are treated differently depending on the status of the customer. If the customer is not in business but is located in the EC, the supply is subject to normal UK rules. For example, if consultancy is supplied to a French individual, the supply is liable to UK VAT.

When these services are supplied to EC businesses or anyone outside the EC, the supply is outside the scope of UK VAT. There are also two special cases, as follows:

- Services of training provided to overseas sovereign governments (including those paid for by the Department for International Development) are VAT zero-rated by extra-statutory class concession. A college is advised to obtain a statement from the foreign government concerned to certify that the trainees are its employees.
- When a college provides intellectual services contracted for directly to the European Commission for the consumption and benefit of the Commission, the supply is outside the scope of UK VAT.

5·10 Distance selling of goods into the EC

Special VAT registration rules can apply if colleges sell goods directly to private persons and non-VAT business customers in other EC states, for example, sales of books or disks sent mail order and ordered from the Internet.

Below a turnover threshold, sales are subject to UK VAT. However, if the threshold is exceeded, a college will become liable to register in the country where the customer is based and thus charge VAT at the local rate. The turnover threshold applies separately for each EC country and the minimum annual threshold is approximately £20 000.

5·11 Statistics

If the college exports (dispatches) or imports (acquires) goods and its trade with other EC countries exceeds an annual value threshold, a monthly statistical return must be provided to HM Customs and Excise (the Supplementary Statistics Declaration). The threshold is set each calendar year and is presently £233 000 (for year 2000).

A separate statistical return has to be sent to HM Customs and Excise quarterly in respect of dispatches of goods to other EC countries. This is the EC Sales Listing or ESL. There is no monetary threshold for this return. Direct distance selling to private and non-business customers as described at 5·10 are excluded from these statistical returns.

5·12 Subsidiaries

A college may own shares in or guarantee the liabilities of a subsidiary limited company. In either case the VAT status of the subsidiary is fundamentally different to that of its parent college.

The main difference is that a subsidiary, if it covenants profits, or distributes dividends, or uses its profits for purposes other than the furtherance of education activities (ring fencing), cannot be an eligible body (see Appendix 9). This means the subsidiary's supply of education, research and training (except for Government-funded training programmes) in the UK will be standard-rated.

Subsidiaries can be registered for VAT separately from their parent or, alternatively, they can be VAT grouped with their college (see 6·2) provided the parent controls its subsidiary and both are UK resident. If a subsidiary is separately VAT registered, the VAT status of inter-trading, use of staff and facilities, etc. must be assessed from the VAT viewpoint.

Some subsidiaries prefer to have a separate VAT status from their parent. This is perhaps if they see an advantage in this when providing goods or services to their parent. Whether or not a subsidiary is VAT grouped with its parent does not affect its VAT status as a non-eligible body. If the subsidiary is VAT grouped, but can distribute profits, it is still not an eligible body.

Supplies of training services, which are ultimately funded by a Government training scheme for the unemployed, are exempt regardless of whether the trainer is an eligible body. Similarly, examination services are always exempt when they are provided to an eligible body or a student of an eligible body.

The use of subsidiaries is a complex subject and one which requires a knowledge not just of VAT but also of legal, contractual, governance, corporation tax, covenant and gift aid issues.

6 VAT compliance

6·1 Introduction

The purpose of this chapter is to give an overview of the issues that can arise following changes to a college's VAT registration status and/or corporate structure. Comment is also provided on how HM Customs and Excise deal with the sector, on what you can expect from your contacts with the department and how you should comply with VAT requirements.

6·2 Registration for VAT

Colleges must apply to be VAT registered if their taxable income (turnover) exceeds the registration threshold (presently £51 000). Taxable turnover is that which is liable to the standard, reduced and zero rates and does not include income which is exempt or outside the scope of VAT.

The registration threshold is measured on two counts, as follows:

- Taxable turnover you have received in the last 12 months, assessed on a rolling basis, or
- If you anticipate in the next 30 days alone that your taxable supplies will exceed the limit.

When a college receives from overseas suppliers reverse chargeable services for a business purpose (see 3·4·11), these must be added to your UK taxable turnover in calculating whether the threshold for registration has been breached.

The self-supply of printed matter (see 5·2), construction services (see 4·2) and the change in use of previously zero-rated buildings (see 4·5) can also require a college to become VAT registered.

If a college has taxable turnover below the compulsory turnover limit, it may still apply for a voluntary registration. This may be done in advance of perhaps embarking on a new activity which will, once income comes on stream, be taxable, or if a college makes predominantly zero-rated supplies.

A college can be separately VAT registered or, alternatively, if it controls a subsidiary and, depending on circumstances, it can have a VAT group registration with its subsidiary. Under a group, the college and subsidiary share a VAT number and any inter-group trading is ignored for VAT purposes. The use of VAT groups is covered by complex anti-avoidance legislation and therefore advice should be taken before making changes to groups.

6·3 Deregistration

If your taxable income in the next year is anticipated to be below the deregistration threshold, currently £49 000, you can apply to have your registration cancelled. Therefore, once re-registered and if you still have taxable activities, you will need to monitor the registration threshold.

On deregistration you are liable to declare output tax on the current value of goods on hand on which you have deducted any input tax. This can be a significant problem and one where you need to check your records to determine if VAT has been reclaimed in whole or part, for example under a partial exemption method. In certain circumstances, the VAT liability on deregistration may put off a college cancelling its registration.

6·4 Mergers

Where a college merges with another college or higher education body, you need to identify which education corporation, if either, is to be the successor. If a college corporation is dissolved, its VAT registration will also need to be cancelled or transferred to the successor if the latter is not VAT registered. The pros and cons of transferring a registration will depend on individual circumstances and advice should be sought on this crucial point.

Some of the main areas of difficulty in a merger concern property and college subsidiaries. In particular, where properties or computers are subject to the capital goods scheme (see 3·4·22), or where zero rating has been claimed for non-business use (see 4·2·1) and subsidiaries are separately VAT registered. These are all examples of issues for the due diligence process to consider.

6·5 Joint ventures and collaborative activities

Where a college enters into collaborative activities, the legal status of the venture needs to be determined. In particular, what is the relationship between the college and external parties?

For example, is a partnership or a new corporate body created? In this case, the new entity may need its own VAT registration and VAT may need to be charged by the college to the new entity and *vice versa*. Agreements to share profits may represent a taxable supply so should be scrutinised carefully (see 5·12 on subsidiary companies).

Many collaborative or consortium activities do not in fact create a separate entity. Often they are merely an agreement to sub-contract or franchise activities. Others may represent a supply by a college of services to other parties who wish to 'share' in an activity. These activities are capable of being complex and expensive in terms of irrecoverable VAT if they are not structured appropriately.

Some collaborative ventures involve an exchange of goods and services which may contra or for which no monetary consideration passes. Again, these ventures may contain VAT issues which will need to be separately assessed.

6·6 VAT inspections

Local VAT offices undertake routine inspection of college VAT records. In many regions, colleges are allocated to one individual VAT officer. VAT inspection frequency will depend on the size of the college and its corporate group, the complexity of accounting records and the trend of VAT returns. For example, an unexpected VAT refund request may prompt an inspection.

The VAT officer on a visit may wish to inspect the college premises, examine the books of entry and invoices. An officer with a specialism in computers may wish to review your software and document procedures for accounting for expenditure and income.

A VAT officer may request a copy of the audited accounts. However, beyond this, if management accounting information or correspondence with auditors or tax advisers is requested, you should seek professional advice before agreeing to hand over confidential documents.

When dealing with VAT officers, you should note that verbal rulings are not reliable. Areas of query or unusual treatment should be confirmed in writing. For example, you can write yourself to the VAT office to confirm your understanding of a verbal ruling and request that an acknowledgement is sent but a full reply given only if you have misunderstood a situation. All rulings must be sought on full presentation of the facts or else they will be incomplete and unreliable.

6·7 VAT disputes and appeals

Sometimes you may wish to dispute a ruling, decision or VAT assessment. If you are unhappy with a matter, you can either make an appeal directly to the VAT Tribunal Service or ask for a local reconsideration by the VAT office.

The VAT office itself will prefer you to ask for a local reconsideration, which must be undertaken by a different VAT officer. If the decision or assessment is upheld, you then are allowed to appeal to the VAT Tribunal.

Alternatively, an immediate appeal can be made directly to the VAT Tribunal Service. Under this process, it is likely that the decision or assessment will anyway be reconsidered within the VAT office well before a tribunal hearing. In this respect an appeal to the Tribunal is straightforward as it only involves completion of an application form.

When an appeal is made to a VAT tribunal and if the VAT office subsequently changes its decision or withdraws an assessment, it pays costs. Costs are only awarded from the date a tribunal appeal is made, thus any prior time costs, asking for a local reconsideration, are lost. The rate awarded for costs is what the VAT office considers to be reasonable and often not what many large city firms charge. A dispute over costs can be settled by taxing.

6·8 VAT returns

The normal routine is that VAT returns are completed quarterly. Within reason, a college can ask in advance for returns to coincide with a particular quarterly cycle or stagger. For example, returns may be staggered to coincide with a 31 July year end (which has advantages for partial exemption).

If you run special accounting periods and non-calendar month end dates, these can also be accommodated by an advance cleared change in VAT return dates. Any such requests must be made in writing to the VAT office, normally 90 days in advance of a change.

Where a college expects to be in a regular VAT refund position, say over the next year, you can request monthly VAT returns. This can be used to improve cashflow.

The due date for a return, and any payment, is the last working day of the month following a tax period end. This due date for payment can be extended by one week's worth of working days if a college agrees in writing to make payment by bank transfer (an application form is available from HM Customs and Excise).

If a return and payment cannot be made by the due date, you can ask for any surcharge penalty to be waived if you have a reasonable excuse. What is a reasonable excuse depends on your circumstances and is itself subject to appeal if HM Customs and Excise reject it.

Otherwise, if your return and payment are received late, they will be subject to a surcharge regime as follows:

- *First default.* Surcharge liability warning notice issued
- *Second default.* 2% penalty (assessed on the tax payable)
- *Third default.* 5% penalty
- *Fourth and fifth defaults.* 10% and 15% respectively (15% is the maximum).

To exit the default surcharge regime, a clean 12 months is required.

If you notify HM Customs and Excise in advance of a due date that you cannot, in the time allowed, produce an accurate VAT return, they should give you authority to use estimates. Subsequently, the estimates must be corrected in accordance with the voluntary disclosure rules noted at 6·9.

If HM Customs and Excise fail to repay a refund return within 30 days of receipt, subject to extra time allowed for their reasonable checks, they are liable to pay a 5% repayment supplement.

6·9 Correction of errors

When you identify that an error in VAT accounting has been made in a return period already completed, its correction is subject to a voluntary disclosure procedure.

If the error, together with all others identified in the current period, exceeds £2000 VAT (either over- or underpaid), it must be separately notified to the local VAT office. A form V465 or letter can be used for this purpose. Upon receipt, the local VAT office will then send you an assessment to collect any tax and interest due or initiate a refund if this is necessary.

For example, you are in period 07/99 and you identify two errors: £3500 underpaid in period 01/99 and £1000 overpaid in period 10/98. In this case, you should make a voluntary disclosure and the VAT office will assess for £2500 tax due and interest on this amount.

When the net value of errors to be corrected is less than £2000 VAT, an adjustment should be made on the next VAT return.

6·10 Interest

Default interest is charged by HM Customs and Excise in cases where tax is paid late and is collected by them, either on an assessment raised by an inspector, or initiated by a voluntary disclosure. Default interest is commercial restitution for loss of use of the tax for a period of time charged at the time of writing at 7·5% (simple interest). Interest is not charged if there is overall no tax loss. For example, if you failed to charge output tax and thus the customer could not reclaim the tax.

HM Customs and Excise will pay, in compensation, interest in cases of official error on their account. Their payment of interest is not automatic and you must request it.

6·11 Penalties

In addition to interest and default surcharges, HM Customs and Excise will charge a misdeclaration penalty of 15% in circumstances of large or repetitive errors discovered by them. The misdeclaration penalty is not invoked if errors are voluntarily disclosed before HM Customs and Excise actively make enquiries.

The misdeclaration penalty is due where either:

- A return is made and it understates the tax due, or overstates a refund, or
- HM Customs and Excise issue an assessment because a return has not been submitted.

The threshold for the penalty is the lesser of:

- £1m and 30% of the gross amount of tax, or
- £1m and 30% of the true amount of tax for the period where a return has not been submitted.

The gross amount of tax is the aggregate of input and output tax in a period, while the true amount of tax means the net tax due.

Where an error is repeated, subject to HM Customs and Excise giving a prior written warning, the threshold is the lesser of £500 000 and 10% of the gross amount of tax. The penalty is then invoked if the college goes on to make at least two further errors in value which exceed the threshold.

6·12 Three-year time limit and unjust enrichment

Except in cases of fraud, a three-year time limit applies to all adjustments of VAT. Consequently, if the due date for a return which contains an error is over three years away, there is no liability for either the college or HM Customs and Excise to correct it.

The three-year time limit applies generally and therefore affects college suppliers as well. If a college is charged VAT incorrectly, the supplier has three years to issue a credit note.

In cases where a college has accounted for output tax on a source of income incorrectly, HM Customs and Excise may refuse payment of the tax overpaid if it unjustly enriches the college. Whether HM Customs and Excise invoke the provision depends on the circumstances as to whose error it was. The HM Customs and Excise decision to refuse a repayment can be appealed against.

6·13 Record retention

The law requires that VAT records must be kept for six years. However, HM Customs and Excise have the power to reduce this time limit upon written application as to why a lesser period should be acceptable.

The capital goods scheme (see 3·4·2) requires the monitoring of expenditure on computers and building works over a 10-year period. Consequently it is advisable to keep a separate note of these items.

Where zero-rating relief has been claimed on new buildings (see 4·2·2), a note of their use should be maintained for 10 years following first physical use.

Where a college has elected to waive exemption on a property (opted to tax), the election remains in effect for 20 years. The college's permanent files should therefore keep a note of the VAT status of its buildings.

6·14 Tax points – a brief guide

The tax point is the time when a supply for VAT purposes is treated as taking place. In the most common cases, the tax point for a supply which is VAT standard rated is the earlier of:

- Receipt of payment, or
- Issue of tax invoice.

The above rule can be altered if a supply takes place but payment and invoicing is delayed by over 14 days, in which case the tax point could revert to the date goods were delivered or the date a service was completed.

For takings from vending machines the tax point is the date of emptying, for other cash receipts the date of receipt will usually be the tax point. Deposits taken as pre-payments should normally be accounted for on the date of receipt or invoicing if earlier.

For further detailed guidance on tax points, please refer to HM Customs and Excise Public Notice 700.

6·15 Bad debt relief

Where output VAT has been accounted for on a supply made by a college and the debt remains unpaid for at least six months, a bad debt relief claim can be made. The claim procedure is to reclaim VAT from HM Customs and Excise as additional input VAT on the VAT return which is signed off at least six months after the debtor invoice was issued. Where a claim is made, the customer must be notified in writing that a claim has been made.

For example, if VAT at 17·5% was originally accounted for on a sale, but the debtor does not settle the full debit, the VAT bad debt relief is 7/47ths of the outstanding amount.

Details of the claim should be kept in a 'bad debts account', which could take the form of a memorandum record of how the claim was compiled. If a debt is later recovered, the VAT bad debt relief must be disclaimed by accounting for a negative amount of input VAT on the VAT return which covers the date of recovery.

Appendices

Contents

Appendix 1

VAT certificate for charity advertising

I

(full name)

(status in organisation)
of

(name of organisation)

(address of organisation)
declare the above named charity is buying
from

(name of supplier)

(address of supplier)

The following goods or services eligible for relief from VAT under item 8 of the zero-rate group 15

(description of goods or services)

(signature)

(date)

Note to signatory
There are severe penalties for making a false declaration. If you are in any doubt about the eligibility of the goods or services you are buying, you should seek advice from your local VAT office before signing this declaration.

Note to supplier
You should retain this certificate for production to your VAT officer. The production of this certificate does not authorise the zero rating of the advertising services. It is your responsibility to ensure that the goods or services supplied are eligible before zero rating them.

Appendix 2

VAT certificate

Eligibility declaration by a charity for goods and services acquired for disabled persons

I

(full name and status in charity)
of

(name of charity)

(address of charity)
declare the charity named above is receiving
from

(name of supplier)

(address of supplier)

The following building alterations

(description of alterations)
at

(address of building)
to enable disabled persons to enter or move within the building and I claim relief from value added tax under group 12 of schedule to the Value Added Tax Act 1994.

(signature)

(date)

Note to supplier
You must keep this declaration for production to your VAT office. The production of this certificate does not automatically authorise the zero rating of the supply. You must also ensure that the goods and services you are supplying qualify for zero rating.

Note to signatory
If you are in any doubt as to whether you are eligible to receive goods or services zero-rated for VAT you should consult VAT Public Notice 701/7 or seek advice from your local VAT office before signing the declaration.

Warning
The VAT Act provides for severe penalties for anyone who makes use of a document which they know to be false for the purposes of obtaining VAT relief.

Appendix 3

Certificate to a supplier in respect of premises qualifying for reduced rate supplies of fuel and power

Address of qualifying premises

Name of business or organisation (if applicable), and VAT registration number if registered

Percentage used for a qualifying use (see VAT Public Notice 701/9)

Full name of signatory and (where appropriate) status held

I certify that the information given above is correct and complete.

I undertake to inform

(name of supplier)
if there is any significant change in the circumstances.
I understand that any incorrect statement may make me liable to a financial penalty under the VAT Act 1994, as amended.

(signature)

(date)

Appendix 4

Certificate for developers and building contractors in respect of relevant residential and relevant charitable buildings

Name and address of business/charity using the building

VAT registration number (if applicable)

Address of qualifying premises (if different from above)

Date (or estimated date) of completion of building

Estimated value of supply (£s)

I/We certify that I/we have read the current edition of Public Notice 708 *Buildings and construction*. This certificate is being issued in respect of the supply described in that Public Notice at paragraph 3·3:

The first grant of a major interest in a relevant residential building	☐ Yes ☐ No
The first grant of a major interest in a relevant charitable building	☐ Yes ☐ No
The first grant of a major interest in a building converted into a relevant residential building	☐ Yes ☐ No
The construction of a relevant residential building	☐ Yes ☐ No
The construction of a relevant charitable building	☐ Yes ☐ No
The construction of an annex to a relevant charitable building	☐ Yes ☐ No
An approved alteration to a relevant residential building	☐ Yes ☐ No

An approved alteration to a relevant charitable building ☐ Yes ☐ No

The conversion for a relevant housing association of a building into a relevant residential building ☐ Yes ☐ No

I/We certify that the information given above is correct and complete. I am/We are aware of the law as contained in group 5 or group 6 of schedule 8 of the VAT Act 1994 and claim relief accordingly. I/We also certify that this organisation (in conjunction with any other organisations where applicable) is to use this building or identified parts of this building solely for a qualifying purpose. I/We understand that if a building or zero-rated part of it is disposed of, let or otherwise used for a non-qualifying purpose within the period of 10 years from the date of its completion, a taxable supply will have been made, and this organisation (and any other organisations where applicable) will account for tax at the standard rate.

Name (print)

Position held

(signature)

(date)

Name, address and VAT registration number of developer or building contractor

Date certificate received by developer or builder

Date certificate received by VAT office

Please note that copies of Public Notice 708, *Buildings and construction*, are available from your local VAT office, your VAT adviser, or via the Internet at www.hmce.gov.uk

Appendix 5

Items ordinarily installed

The following items are those considered by HM Customs and Excise to be ordinarily installed. This is not an exhaustive list, but it gives a general idea of the items included:

- Window frames and glazing
- Doors
- Letter boxes
- Fire places and surrounds
- Guttering
- Power points
- Outside lights (fittings but not the bulbs)
- Radiators and central heating
- Fire/burglar alarms and smoke detectors
- Air conditioning equipment
- Dust extractors
- Lifts and hoists
- Communal TV aerials in flats, etc.
- Work surfaces or cupboards in kitchens
- Kitchen sinks
- Baths and basins
- Toilets
- Shower units
- Items that provide storage, e.g. fitted cupboards
- Water heaters.

On top of the above items, certain other goods can be zero-rated when installed in a new relevant charitable building:

- Blinds and shutters
- Mirrors
- Blackboards fixed to, or forming part of, the walls (education establishments only)
- Gymnasium wall bars
- Notice and display boards
- Mirrors and barres (ballet schools only).

For all of the above to be zero-rated, certain conditions must be met.

- The goods must be incorporated into the building, i.e. not free standing.
- The goods must be supplied with construction services, i.e. they must be fitted by the contractor and not simply delivered by him.
- The contractor's services must qualify for zero rating.

Where these conditions are not met, goods are standard-rated.

Excluded fixtures and fittings

The following goods are always excluded from the list of items ordinarily installed and are therefore standard-rated.

- Finished or pre-fabricated furniture (other than fitted furniture intended for use in the kitchen). Included in this will be:
  - Cabinets
  - Chairs
  - Laboratory benches
  - Desks
  - Tables
  - Dining tables
- Electrical or gas appliances other than those zero-rated as above. For example, cookers, washing machines, dishwashers, entry telephone systems (unless fitted in a block of flats).
- Carpets and carpeting material, e.g. underlay.

Appendix 6

Notification of election to waive exemption (option to tax)

Registration details

Trading name

VAT registration number

Address

Election details

Date of election

Property/properties covered by the election (give full postal address [including postcode], building names and supply highlighted plans/maps where appropriate)

I have the authority to sign this form on behalf of the above registration

(signature)

(name)

(position)

(date)

Appendix 7

Member states of the European Community

The following countries and territories are within the VAT territory of the European Community:

- Austria
- Belgium
- Denmark, except the Faroe Islands and Greenland
- Finland
- Germany, except Busingen and the Island of Heligoland
- Greece
- Italy, except the communes of Livigno and Campione d'Italia on the Italian waters of Lake Lugano
- Luxembourg
- The Netherlands
- Portugal, including the Azores and Madeira
- The Republic of Ireland
- Spain, including the Balearic Islands but excluding Ceuta and Melilla
- Sweden
- United Kingdom, including the Isle of Man.

The following territories are outside the VAT territory of the European Community:

- Andorra
- The Aland Islands (Finland)
- The Channel Islands and Gibraltar
- The Republic of San Marino
- The Canary Islands (Spain)
- The overseas departments of France (Guadeloupe, Martinique, Reunion, St Pierre and Miquelon, and French Guiana); and
- Mount Athos, also known as Agion Poros (Greece).

The following countries and territories are not part of the European Community:

- Cyprus
- Malta
- Vatican City.

Appendix 8

List of reverse charge 'intellectual' imported services

1. Transfers and assignments of copyright, patents, licences, trademarks and similar rights
2. Advertising services
3. Services of consultants, engineers, consultancy bureaux, lawyers, accountants and other similar services; data processing and provision of information (but excluding from this head any services relating to land)
4. Acceptance of any obligation to refrain from pursuing or exercising, in whole or part, any business activity or any such rights as are referred to in paragraph 1 above
5. Banking, financial and insurance services (including reinsurance, but not including the provision of safe deposit facilities)
6. The supply of staff
7. The letting or hire of goods other than means of transport
8. The services rendered by one person to another in procuring for the other any of the services mentioned in paragraphs 1–7 above
9. Any services not of a description specified in paragraphs 1–8 above when supplied to a recipient who is registered under this Act
10. Section 8(1) shall have effect in relation to any service:
    a. Which are of a description specified in paragraph 9 above; and
    b. Whose place of supply is determined by an order under section 7(11) to be in the United Kingdom, as if the recipient belonged in the United Kingdom for the purchase of section 8(1)(b).

Appendix 9

Glossary

General VAT terminology

Business *vs* non-business

The term 'business' refers to those activities funded by fees, contracts and trading activities. Non-business activities are those wholly funded by grants and donations.

Eligible body

An institution listed in the VAT Act as required to exempt its services of education, training and research. Eligible bodies are as follows:

- Universities, colleges, independent schools
- Government departments and agencies exercising their functions on behalf of a Minister of the Crown, e.g. Research Councils
- NHS Trusts and Authorities
- Local government
- Non-profit-making bodies which perform functions similar to those of a government department or local government.
- Other bodies which are providers of education, research and vocational training, which are precluded from distributing profits and which apply (ring fence) any profits made from such supplied to the continuance or improvement of such supplies.

Exempt supplies

Supplies which are not taxable because the law says that VAT is not to be charged on them. Exempt supplies differ from zero-rated supplies in that input tax on the former is generally not reclaimable.

Input tax

Tax incurred on the purchase of supplies (including imports) that are to be used for business purposes. This is different to the total VAT incurred on expenditure, some of which may relate to non-business activities.

Output tax

Tax charged on the college's supply of goods and services.

Supplies

Goods, the exclusive ownership of which passes from one person to another, or services for which payment, in money or kind, is made.

Taxable supplies
Supplies which are liable to VAT at the standard rate (currently 17·5%) reduced rate (5%) or the zero rate (0%).

Tax period
The time period for which a VAT return has to be completed – usually one or three months.

Tax points
The time when a supply is treated as taking place. The liability and rate of tax are determined by the supplier at the tax point.

Property terminology

Approved alterations
Approved alterations are those which may not be carried out unless authorised under:

- Part I of the Planning (Listed Buildings and Conservation Areas) Act 1990
- Part I of the Planning (Listed Buildings and Conservation Areas) (Scotland) Act 1997
- Part V of the Planning (Northern Ireland) Order 1991
- Part I of the Ancient Monuments and Archaeological Areas Act 1979.

In cases of protected buildings which are ecclesiastical buildings, under section 60 of the Planning Act 1990, all works of alteration are approved.

Curtilage
Curtilage has no strict legal definition, but it is generally taken to mean the land associated with a building and lying immediately around it. This may include forecourts, yards, parking bays and landscaped areas.

Existing building
A building ceases to be an existing building when:

- Demolished completely to ground level, or
- The part remaining above ground level consists of no more than a single façade or where a corner site, a double façade.

Grant of an interest in property
A grant of an interest in property is the sale or gift of the freehold or leasehold of a property. It is also the issuing of a licence to occupy land or property. A grant is also deemed to include an assignment or surrender.

Holiday accommodation
Holiday accommodation includes any accommodation in a building, chalet, houseboat, caravan or tent that is advertised, or let out as holiday accommodation, or as suitable for holiday or leisure use.

Major interest
In relation to land and property, major interest means the fee simple or a tenancy for a term certain of not less than 20 years. In Scotland, it means the estate or interest of the proprietor of the dominium utile, or a lease of over 21 years.

Non-residential
Non-residential in relation to a building means a building:

- Neither designed or adapted for use as a dwelling or a relevant residential purpose; or
- A building originally designed as a dwelling, but which has not been used as such since the introduction of VAT on 1 April 1973.

Relevant charitable use
This covers use by a charity in either or both of the following ways:

- Otherwise than in the course or furtherance of a business
- As a village hall or similarly in providing social or recreational facilities for a local community.

Note that FE colleges usually have a combination of business and non-business activities (see 3·3·7).

Relevant residential use
Buildings included in this category are those used as:

- A home or other institution providing residential accommodation for children
- A home or other institution providing residential accommodation with personal care for persons in need of personal care by reason of old age, disablement, dependence on alcohol or drugs or mental disorder
- A hospice
- Residential accommodation for students or school pupils
- Residential accommodation for members of any of the Armed Forces
- A monastery, convent or similar establishment
- An institution which is the sole or main residence of at least 90% of its residents, except where used as a hospital, prison or similar institution or an hotel, inn or similar establishment.

Substantially reconstructed
A building is substantially reconstructed when at least one of the following criteria are met.

- 60% test – this requires that at least 60% of the work performed on the building would have been zero-rated if carried out by a contractor. Though note the reconstruction does not have to be carried out by a contractor. The necessary condition is that 60% of the work on the building would qualify as approved alterations, as defined above.
- The building, as it stood before the reconstruction, must have been gutted. That is to say that no more than the external walls and external features (e.g. roof, domes, porch) were standing before the reconstruction. Again, the reconstruction does not have to be carried out by a contractor; the owner of the property can carry out the reconstruction. Listed building or scheduled monument consent for the work is not a necessary condition for this criteria to apply.

Appendix 10

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