



not for profit | school trading

the team



Kathryn Burton
partner
020 7969 5515
kburton@haysmacintyre.com



Adam Halsey
partner
020 7969 5657
ahalsey@haysmacintyre.com



David Sewell
partner
020 7969 5568
dsewell@haysmacintyre.com



Richard Weaver
partner
020 7969 5567
rweaver@haysmacintyre.com



Tracey Young
partner
020 7969 5654
tyoung@haysmacintyre.com



Les Jones
charity consultant
020 7969 5538
ljones@haysmacintyre.com

Consideration of the principal legal, tax, VAT and accounting implications of trading activities carried out by schools.

This fact sheet summarises the principal issues concerning schools' non-primary purpose trading activities.

Provided that a charity is acting within its powers, charity law allows it to derive income from a wide range of sources, the income from which would generally be exempt from income and corporation taxes.

A notable exception to the generally relaxed attitudes towards how a charity should be able to raise funds is the area of trading, and this can prove to be an issue from the point of view of both charity and tax law.

Most schools supplement their income by fundraising and they also generate further funds through other activities. These are permissible to the extent that they are ancillary to the running of the school; however when they are carried out on a larger scale and more for the purposes of making a profit, they may jeopardise the school's charitable status and the related tax benefits. It is therefore important to identify which activities of the school constitute trading and to consider whether it is appropriate for the school to carry these out.

Where there is a danger that undertaking an activity could cause the school to breach charity law or incur an unnecessary tax liability, it is common practice to hive it off into a subsidiary company. This is considered in more detail in our schools subsidiary trading companies factsheet (CHA 049).

the position generally

Tax - The trading activities of a school are only exempt from tax if certain conditions are met. These are:

- the profits from the trade are applied for the purposes of the charity; **and, either**
- the trade is carried out in fulfilment of the primary purposes of the charity or is ancillary to these purposes; **or**
- the income from the trade is considered "small" in relation to the other income of the charity; **or**
- the "trade" is carried out to raise funds for the charity and falls within the VAT exemption rules for fundraising events.



Anne Gregory-Jones
tax partner
020 7969 5520
agregory-jones@haysmacintyre.com



Graham Elliott
VAT partner
020 7969 5610
gelliott@haysmacintyre.com

The education of pupils in a fee charging school is usually a trade carried out as part of its charitable purpose and so profits are generally exempt from tax. Other trading activities which are ancillary to the primary purpose will also be exempt. Additionally, the small trade exemption allows for a school's non-charitable trading activities to be exempt if the aggregate turnover from all such trades does not exceed the lesser of £50,000 and 25% of the school's gross income.

VAT - Whilst school fees are exempt, other trading income, whether or not part of its charitable objects, may be taxable and, if the turnover exceeds the limit (currently £70,000) the school would need to register for and charge VAT on the trading income which is standard rated.

Charity law – Provided that the activity poses no significant risk to the charity's assets, charity law permits charities to carry out non-primary purpose trading in order to raise funds.

The assessment of the significance of the risk involves an element of judgment; however, a lottery or trading that qualifies for the small scale trading exemption would generally be considered not to involve significant risk.

In comparison, VAT-exempt fundraising events do not escape consideration and the Charity Commission strongly advises that events with a significant turnover should be carried out through a subsidiary trading company. They go on to say that in some cases charity law will require this.

the tax and VAT implications of seven activities commonly undertaken by schools are summarised briefly below:

- **Lettings**

Tax - The letting of land and buildings is not taxable unless services such as staffed catering and boarding facilities are included. Similarly, the provision of well-equipped computer rooms with support staff, and all related facilities, could also be seen as trading. Whenever services are provided, it is probably best to err on the side of caution and put such activities through a trading company.

VAT - The letting of land and buildings is exempt unless certain kinds of service are included, e.g. where the significance of the letting lies principally with a supply of catering. Subject to certain conditions, bookings for sporting facilities are exempt. When boarding and catering facilities are provided to non-pupils, this is only exempt if the supply is made from the school to another eligible body such as another not-for-profit organisation or one that teaches English as a second language.

- **School Shop**

Tax - Sales to pupils of school specific uniform and necessary sports equipment, as well as basic toiletries and fresh fruit in boarding schools, is exempt as being ancillary trade. Sales of these items to others, or other items such as standard clothing and school uniform to pupils, will be seen by HM Revenue and Customs (HMRC) as not ancillary to the primary purpose of the school.

VAT - Sales of certain items essential for use in the classroom and school meals will be exempt. School uniforms are not seen as essential and are taxable at the standard rate or the zero rate if they qualify as children's clothing. Sales of all other items, including snacks outside normal school meal times, are treated in the same way as for independent retailers: either standard or zero rated. Confectionery sold from vending machines will be standard rated, whether or not it is sold in the dining room during mealtimes.

- **School Trips**

Tax - Educational trips are not taxable whether the income is received as principal or agent. If the trip is non-educational, such as ski trips, or there are unconnected third parties going on it, any profits would be taxable either as trading, or, as 'other profits or gains', subject to the small trading exemption.

VAT - Educational trips within the UK are exempt. Where the School provides foreign travel or holidays it will fall under the potentially complex Tour Operators Margin Scheme (TOMS). The margin (if any) on trips inside and outside the EU are treated as being subject to VAT at the standard rate and zero rate respectively; so, if such trips make a loss or break even, there is no profit margin that can be subject to VAT.

- **Sponsorship**

Tax - Sponsorship income is not taxable if it is effectively a donation and the sponsor only receives their name printed in acknowledgement. If the references to a sponsor amount to an advertisement then the payment could be trading income and may be taxable.

VAT - The VAT and tax treatment is similar: donations are outside the scope of VAT whilst advertisements are standard rated. However, any sponsorship associated with a one-off fundraising event will also be exempt from VAT. As a "rule of thumb", sponsorship tends to be regarded as an advertisement if the sponsor receives more than a bare acknowledgement of their donation, e.g. if their logo is displayed.

- **Commissions**

Tax - Other income, such as insurance commission, may be taxable as 'other profits or gains', subject to the small trading exemption. Such items can often be agreed to be incidental income of the primary purpose of the trade, depending on their precise nature.

VAT - There is VAT on certain kinds of commission income but insurance commission is generally exempt. Commission paid to agents recruiting pupils from abroad can also cause a problem as when the agents belong outside of the UK, special rules governing imported services are triggered. The school is then obliged to declare VAT on the purchase as though it was a sale by the school. It may be desirable to route these services through a trading subsidiary as, whilst this would not avoid incurring VAT on these purchases, it would potentially help the school to avoid the need to register for VAT.

- **Bussing**

Tax - it should be possible to argue that the provision of safe transport for the pupils is expected by the parents and is ancillary to the supply of education.

VAT - the supply of passenger transport in a vehicle designed or adapted to carry 10 or more passengers is generally zero-rated but may be exempt if it is ancillary to a supply of education by an eligible body. If the school acquires the buses themselves, any VAT could well be irrecoverable; however, acquiring the buses through a trading subsidiary could allow VAT to be recovered on the purchase of the vehicle and running costs with the onward supply of passenger transport to the school being zero-rated. The supply of passenger transport in vehicles with a capacity of less than 10 is standard-rated, so any charges here would give the school an irrecoverable VAT cost.

- **Transactions in land**

Tax - although charities are usually exempt from tax on their capital gains, anti-avoidance measures mean that problems can arise from certain transactions in land. It is recommended that professional advice is sought when acquiring, developing and selling land.

accounting

The Charity SORP requires the school's income to be shown gross and distinguished between charitable activities (e.g. school fees and ancillary trading income) and activities from generated funds. This would include trading activities such as lettings (if not ancillary) whether or not they were carried out through a subsidiary company, whose activities are consolidated on a line by line basis. Similarly, the related costs of those activities are disclosed under the heading "Costs of generating funds."

For skiing and other trips and certain insurances where the school is acting as agent (banker) on behalf of the pupils and staff, the transactions should not be treated as income and expenditure of the school. However, where the school is acting as principal, the transactions should be 'grossed up' on the face of the statement of financial activities. Any advance payments received from pupils and/or deposits paid on their behalf would be recorded in creditors and debtors respectively.

If a subsidiary company is used, its income and expenditure, where material, should be consolidated in the school's accounts and should be disclosed in a note to the school's accounts together with the gift aiding of any surplus.

conclusion

These are complex issues and we recommend that you consult your usual engagement partner or Graham Elliott for VAT advice or Anne Gregory-Jones for advice on other tax matters.

haysmacintyre
Fairfax House
15 Fulwood Place
London
WC1V 6AY

t 020 7969 5500
f 020 7969 5600
e marketing@haysmacintyre.com
w www.haysmacintyre.com
 @haysmacintyre

about haysmacintyre

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