

Zero-rating applies to epilepsy centre intended solely for non-business use by charity Quarriers (20660)

Summary

The Tribunal has held that zero-rating applied to the construction of an epilepsy centre by a charity whose predominant charitable objective was the provision of care and relief for persons suffering from epilepsy. It was not in competition with providers of similar services and, although the charity made charges to the NHS and local authorities, these did not indicate that its services were supplied in the course of an 'economic activity' for VAT purposes. This decision may be beneficial to organisations carrying on charitable activities in similar circumstances.

Background

The Appellant is a registered Scottish charity whose core activity is the provision of services for people with epilepsy. It also provides practical support and care for children and adults suffering from a physical or learning disability. It is the largest provider of epilepsy services in Scotland and is not in competition with commercial providers of similar epilepsy services in Scotland, nor is it competition with the National Health Service (NHS) in the UK. People with epilepsy are referred to the Appellant by GPs and Health Boards, through consultants.

The Appellant is funded by local authority fees, local authority and government grants and DSS fees from local authorities throughout Scotland (93% of income). About 7% of income comes from donations from various sources. The Appellant aims to break even each year, and the fees charged to those funding bodies are not based on a 'per capita' basis or cost basis but estimated and agreed in advance, in one case with a facility to reduce the following year's fee if the referrals from the funding body are fewer than expected. The Appellant effectively funds, from its own resources, any shortfall of fees in comparison to costs incurred in providing the services.

As the Appellant's existing premises for the provision of the epilepsy services were in need of substantial improvement and remote from other medical care facilities, the Appellant decided to build a new epilepsy centre in a new location, funded partly from its own resources (including fund-raising activities) and partly from sales of other land and property. Patients would live in a comfortable home environment for up to about eight weeks during assessment. The facility would include reception areas, waiting rooms, consultation areas, staff offices, 12 residential assessment beds, a video-telemetry suite, research facilities, a meeting/conference room, and sleep-over areas for relatives and administrative offices.

The Appellant sought guidance from HMRC as to whether the development would qualify for zero-rating under Item 2, Group 5, Schedule 8 VAT Act 1994, which reads:

"The supply in the course of construction of-
(a) a building ... intended for use solely for... a relevant charitable purpose;...
of any services related to the construction other than the services of an architect, surveyor or any person acting as a consultant or in a supervisory capacity

Note 6

Use for a relevant charitable purpose means use by a charity in either or both the following ways, namely-
(a) otherwise than in the course or furtherance of a business;".

HMRC's decision, the subject of the appeal, was that the development was not for a relevant charitable purpose because the supplies to be made by the Appellant would constitute supplies in the course or furtherance of business.

HMRC argued:

This VAT update is published for the general information of 4 Eyes Ltd personnel, clients and contacts. It provides only an overview of the rules and regulations in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material contained in this e-mail will be accepted by the authors or the firm.

An 'economic' (i.e. business) activity existed where services were supplied for a consideration, and there was a link between the services supplied by the Appellant and the invoices raised to funding bodies.

Goods or services were supplied in the course or furtherance of a business when a taxpayer engaged in the market place by offering to make supplies, setting a price, acting for his own benefit and purposes and making supplies on his own account. This contrasted with non-business activities such as personal use, acting in a public law capacity, 'passive' investment in and exploitation of assets and operating a 'concession' such as letting a property at an artificially low rent in order to 'subsidise' the establishment of an activity.

The Appellant had engaged in the market place, with a defined customer base. It was not carrying on an NHS activity but was filling a gap in the NHS's activities, was acting in a business-like manner and was not in competition due to being first in the marketplace.

The High Court had erred in *Customs and Excise Commissioners v St Paul's Community Project Ltd* by concluding that a non-business activity took place where fees were charged at lower levels than commercial providers and intended only to cover costs in circumstances where distribution of profit was prevented.

Yarburgh Children's Trust, where a playgroup activity was carried on by a cooperative and held to be non-business because it was predominantly concerned with carrying out the trust's objectives, could be distinguished on the basis that the supplies made by that trust had been to parents who controlled the trust.

The Appellant argued:

The payment of money did not necessarily indicate that a business was being carried on. There was no direct link between the cost of the services provided to a particular individual and the charges made to the funding bodies.

The 'predominant concern' test where it was held that it was not the profit motive which defined a business activity but whether the predominant concern was to make taxable supplies) was the correct test, rather than HMRC's 'engaging in the marketplace' test and, notwithstanding, there was no marketplace in the Appellant's case.

The 'predominant concern' of the activities carried on by the Appellant was not economic; it supplied a unique service which it subsidised in furtherance of its charitable objects.

Decision

The Tribunal decided that it was difficult to classify the intended use of the proposed epilepsy centre as a trading or commercial activity which might justify it being described as 'economic'. In particular:

- the issue of whether a person is carrying on a business would often ultimately depend upon whether its predominant concern was making taxable or exempt supplies to consumers for a consideration;
- the ascertainment of the 'predominant concern' required the examination of the full facts and circumstances;
- these activities were predominantly, if not exclusively, concerned with the Appellant's charitable purposes;
- the Appellant provided specialist services which were not carried out commercially by anybody else for profit in Scotland and so filled a gap in the provision of NHS in Scotland and fulfilled a national need;
- the activities in question were not in any real sense a trading or commercial activity which might justify them being described as 'economic';

This VAT update is published for the general information of 4 Eyes Ltd personnel, clients and contacts. It provides only an overview of the rules and regulations in force at the date of publication, and no action should be taken without consulting the detailed legislation or seeking professional advice. Therefore no responsibility for loss occasioned by any person acting or refraining from action as a result of the material contained in this e-mail will be accepted by the authors or the firm.

- this was not a case of an undertaking being first to enter the market one step ahead of everyone else in the business community;
- the sums received for the services provided made a contribution towards the cost of providing those services and were not determined by reference to going rates in the marketplace (as there was no marketplace as such);
- there was no consistent direct link between the cost of providing services to a particular individual and the charge made to the funding bodies;
- the fact that charges were made to defray, in part, the cost of providing the services did not convert the activities into a business for the purposes of VAT any more than it deprived the Appellant of its charitable status;
- in essence, as in *Yarburgh*, the intended use of the proposed new epilepsy centre by the Appellant could not be regarded as the Appellant doing anything more than the carrying out of its charitable functions;
- as the Appellant was not in competition, there could be no distortion of competition or breach of the principles of fiscal neutrality if its activity were deemed to be non-business; and
- in light of the foregoing circumstances, the intended use of the proposed epilepsy centre would not in any real sense be a trading or commercial activity which might justify it being described as 'economic' or a use in the course or furtherance of a business.

Consequently, the appeal was allowed.

Implications

This decision may be significant for charities seeking relief from VAT for the development of buildings.

It should also be borne in mind that, based on this decision, the Appellant should also be entitled to receive supplies of fuel and power for use in the building at the reduced rate of VAT. So even if a charity which has suffered VAT on a similar development is not able to secure retrospective zero-rating, it may still be entitled to relief from VAT on fuel and power supplies.

One of the principal points considered in this case was whether the funding received from the funding bodies constituted consideration for a contract for supplies of services or non-business funding. This can be a contentious area and, as in this case, HMRC may not always be correct in its analysis of the correct treatment of this income. Charitable bodies should be careful to consider this aspect of their funding, and should seek specialist VAT advice.