

Novation of construction contract

Grimsby College Enterprises Limited

Background

Grimsby College (the College) is a body regulated by the Further and Higher Education Act 1992. Like many similar institutions, the College moved from local authority control to being a self governed body regulated by the Further Education Funding Council. As a result, such institutions needed to generate further income from commercial activities and set up wholly owned subsidiaries to undertake commercial activities. Grimsby College created Grimsby College Enterprises Limited (Enterprises). This entity makes taxable supplies of engineering and vocational courses to third parties and is fully taxable. The college by comparison is an eligible body within the meaning of Schedule 9 Group 6 item 1. Therefore its supplies are primarily exempt or outside the scope.

In 2001 the College's governing body decided to build and equip a new engineering facility. The taxpayer argued the main motive for this was to increase the ability to provide taxable fee paying courses. The College entered into two building contracts. However after taking tax advice it was decided that the costs should be charged to Enterprises in order to achieve VAT recovery. It was agreed the contracts would be novated but agreements to this effect were never signed. All building contract invoices were made out to Enterprises and it was Enterprises that paid those invoices, albeit with money loaned from the College. To confuse matters the College received and paid some of the early architectural and surveying invoices. It was claimed these were subsequently recharged. Other agreements were entered into. These included a lease by the College to Enterprises for use of the site. The rent was very low and in the opinion of the Tribunal more of a ground rent rather than a fair rent. At the same time Enterprises entered into a licence to use facilities agreement. According to the agreement this entitled the College to share the facilities on a non-exclusive basis jointly with Enterprises.

Held

Input tax on construction costs

The first issue was whether the input tax incurred in building the new block was Enterprises' input tax. The taxpayer argued the contracts were novated orally and that it had bought and paid for the supplies in question and the VAT charged was its input tax. The Tribunal however agreed with HMRC finding as a matter of fact the contracts had not been novated. The mere changing of the invoices to Enterprises fell short of demonstrating novation. Whilst the costs had been invoiced to Enterprises they were essentially paid using the College's money. The Tribunal found in reality the supplies were made to the college.

**WE HOPE YOU FIND THIS NEWS ARTICLE HELPFUL. IF YOU WOULD LIKE TO REGISTER TO RECEIVE
FUTURE UPDATES BY EMAIL THEN PLEASE SEND A REQUEST TO**

info@4eyesltd.co.uk

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.

Input tax on equipment costs

The Tribunal went on to examine the input tax paid on the equipment for the building. Here the Tribunal found the input tax was Enterprises. The Chairman noted it was not possible to displace the fact that Enterprises contracted for the acquisition of the equipment which was to be installed in a building it was about to use to make supplies.

Was this input tax recoverable by Enterprises?

The key question is: what supply Enterprises was making in order to determine if the input tax was recoverable? Enterprises argued its licence to use facilities agreement was not an exempt supply of immovable property and was therefore taxable. However, the Tribunal Chairman agreed with HMRC. Enterprises was wholly dependant on the College and in reality allowed the College access to the building so it could make the entire supply of education to its own students and some to Enterprises for onward supply. Enterprises had no physical presence such as employees and was incapable of delivering courses to students. All Enterprises did was buy in supplies made to it and sell them on. The Chairman concluded the true nature of the licence was a letting of immovable property. That supply was exempt and therefore the input tax is irrecoverable.

[To read the case in full click here.](#)

Comment

This case shows the potential pitfalls with VAT planning. It is essential that when a VAT efficient arrangement is put in place, great care is taken with the implementation in order to make the arrangement resilient to subsequent challenge by HMRC.

**WE HOPE YOU FIND THIS NEWS ARTICLE HELPFUL. IF YOU WOULD LIKE TO REGISTER TO RECEIVE
FUTURE UPDATES BY EMAIL THEN PLEASE SEND A REQUEST TO**

info@4eyesltd.co.uk

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.