

VAT: supplies of research between eligible bodies

1. Introduction

This Information Sheet is intended to provide some additional guidance on when the provision of research between eligible bodies may still be treated as exempt from VAT following the withdrawal of the VAT exemption for research, as explained in Revenue & Customs Brief 21/13. It also details the transitional arrangements that will apply following the withdrawal of the exemption on 1 August 2013.

1.1 Who should read this Information Sheet?

Those eligible bodies that undertake research and those that commission research.

This Information Sheet should be read in conjunction with Revenue & Customs Briefs 10/13 (VAT: withdrawal of the VAT exemption for supplies of research between eligible bodies - consultation update) and 21/13 (VAT: withdrawal of the VAT exemption for supplies of research between eligible bodies - announcement on transitional arrangements).

1.2 What are eligible bodies?

Eligible bodies are defined in Note (1) to Group 6, Schedule 9, VAT Act 1994 and include schools, UK universities or a college of a university, an institution falling within the Further and Higher Education Acts, a public body such as a government department or a local authority, or a non-profit making body such as a charity.

2. The current VAT treatment and the changes being made

A supply of 'business' research between eligible bodies is exempt from VAT and 'non-business' research is outside the scope of VAT (see below for a further explanation of the distinction between these two types of research).

The VAT exemption for business research supplied between eligible bodies will be withdrawn for all written contracts that were not entered into by 1 August 2013.

However there will be a transitional arrangement for supplies of research made under a written contract entered into before 1 August 2013 (whether or not work under these contracts has commenced by that date) which will allow the exemption to continue to apply for supplies within the scope of the contract as at 31 July 2013. There are however, certain restrictions on the scope of the transitional arrangements (see below).

2.1. Transitional arrangements and how they will work

Supplies of business research where the written contract was entered into before 1 August 2013, whether or not work has started, will continue to be exempt for the life of the contract, provided that the services performed are within the scope of the contract as it stood immediately before 1 August 2013.

This means that if the contract is extended or varied (whether or not the consideration payable is increased) on or after 1 August 2013 then payments for these new or changed supplies will be standard-rated. Supplies relating to the contract as it stood at 31 July 2013 will remain exempt.

Some minor variations will not affect the liability of the original contract. This might include one or more of:-

- Changing the supplier of a sub-contracted service,
- Changing the order the contract is performed in,
- Minor changes to the delivery time of the contract and milestones (less than three months) providing there is no additional consideration.

This list is not exhaustive but the changes involved must have only very minor impact of delivery of the contract as agreed at 31 July 2013.

However, substantial variations may include one or more of the following:-

- Increases the length of the contract (over three months),
- Payment of additional consideration,
- Requirement for new or additional tests to be performed,
- Changes to the product or topic on which research is being carried out.

Again, this list is not exhaustive as the impact needs otherwise to be determined on a case-by-case basis but the changes involved will impact on delivery of the contract as at 31 July 2013.

If a substantial variation is made to a written contract as it stood at 31 July 2013, supplies that relate to the changes will be subject to VAT at 20% and changes that remain within the scope of the contract as it stood at 31 July 2013 remain exempt.

Supplies under the contract will be a continuous supply of services. Each liability of each supply is individually determined.

- If the supply made is for a supply wholly under the contract as it was on 31 July 2013, that supply will be exempt from VAT.
- If a supply is wholly for an extended part of the contract, that supply will be standard-rated.
- If a supply relates in part for the contract as it stood as at 1 August 2013 and in part from extended parts of the contract, then that whole supply is taxable at the standard rate.

As this is a single supply, there can be no apportionment. Supplies can only be exempt if they fall wholly within the scope of the contract as at 1 August 2013, otherwise they are taxable. Research providers that want to benefit from the exemption should ensure all supplies that are within the scope of the contract as at 31 July are invoiced or paid on their own and not with any work relating to the extended supplies.

3. What is research?

Given the changes outlined above, from 1 August 2013, eligible bodies that undertake research will need to ensure that they are clear as to whether or not their research falls within the scope of VAT.

If it falls within the scope of VAT then they will need to consider whether it falls within the transitional provisions which apply to existing contracts.

Although there is no legal definition of “research” in VAT law it is generally considered that research means original investigation undertaken in order to enhance knowledge and understanding.

It is the intention of the parties at the beginning of a project that will determine whether the services supplied qualify as research for VAT purposes. If the intention is to advance knowledge and understanding, the supply is one of research.

Research does **not** include supplies such as merely confirming existing knowledge or understanding, consultancy, business efficiency advice, market research or opinion polling.

The fact that a particular project may have a specific commercial application does not prevent it from being research. Indeed much research funded by the Department of Business, Innovation and Skills and by Research Councils is aimed at developing improved equipment or techniques for use in industry.

4. Research that is within the scope of VAT

For a supply to come within the scope of VAT there have to be at least two parties and a written agreement between them under which something is done for a consideration and by way of business. This means that there must be a direct link between the service supplied (in this case research) and the consideration received such that the relationship can be established between the level of benefits the customer gets and the amount they pay.

Consequently, where research is supplied by way of business and under a contract (or other agreement) in return for consideration, this will be within the scope of VAT and from 1st August 2013, new contracts will no longer qualify for the exemption. The supply will therefore be taxed at the standard rate.

5. Research that is Outside the Scope of VAT

Generally research is outside the scope of VAT when it is funded, either by the public sector or by the charitable sector, for the wider public benefit. However, this is only a general rule of thumb and each case must be considered on its own merits.

The Advocate General in 'Keeping Newcastle Warm (C353/00)' said that if the funding is provided by the public sector (eg, government departments and research councils) 'for the public good' then this is an indicator that the funding is not consideration for any supply by the person who receives the funding.

The main question to ascertain whether the research is outside the scope of VAT is whether the funding is part of the consideration for any specific supply: does the funder receive anything for the consideration that is paid? If not, then service is outside the scope of VAT.

6. Collaborative research

It is common practice for several bodies (typically universities or other eligible bodies) to apply jointly for grant funding to undertake a research project. It is not uncommon for one of the applicants to be shown as the head or lead body which deals primarily with the funding body including receiving funding which is passed to other applicant bodies for their contribution to the project. For ease, contracts are often concluded only in the name of the funding body and the lead research body even though this is a collaborative project.

Provided HMRC is satisfied that the collaborative arrangement is genuinely non-business ie, does not involve supplies for consideration, then it will accept that all research services provided by each of the collaborating bodies involved in the project are outside the scope of VAT, even if the funding may be passed on by the lead research body to others and that only the lead research body is party to the contract with the funding body.

In order to evidence that a project is collaborative and that the funds passing between eligible bodies are not consideration for any supply for VAT purposes, HMRC may ask for evidence that research bodies are participating in collaborative research; the best evidence of that will be the original application for funding which would, in many cases, show who all the collaborative partners are. However, HMRC will accept any alternative evidence that clearly demonstrates that the bodies concerned were participating in collaborative research.

6.1 Changes in collaborative parties

If research bodies are added to or are substituted in a collaborative research project once it has commenced (and so are not mentioned in the funding contract) HMRC would still see them as parties to the collaborative project so that their supplies remain outside the scope of VAT.

7. Partial exemption and business/non-business methods

Research bodies may have existing agreements as to how they establish their recoverable input tax covering how partial exemption and business/non-business calculations must be carried out. Such agreements may combine the two. Those agreements will remain in place spanning the changes in how research is treated for VAT. If any supplies made are treated as non-business or business taxable instead of business exempt then any method in place will reflect this change.

If research bodies feel that their existing methods will no longer produce a fair attribution of input tax to making business taxable supplies after the changes to VAT law and any contractual changes they may make as a result then they should contact HMRC.

8. Who can I contact for further information?

If you have a query for which you have been unable to find the answer within this VAT Information Sheet please contact the VAT Helpline on Tel 0845 010 9000. The Helpline is available from 8.00 am to 6.00 pm, Monday to Friday. If you have hearing difficulties, please ring the Textphone service on 0845 000 0200.