

# The Taxing Wealth Report 2024

Every politician's guide to "How to pay for it".

## The reform of value added tax:

### Abolishing the VAT exemption for services supplied by private schools

#### Brief Summary

This note proposes that:

- The VAT exemption on the supply of education by private schools be abolished.
- This is necessary to improve the vertical equity of taxation when the current exemption for VAT charges on private school fees provides a benefit very largely enjoyed by the wealthiest in society.
- Removing this exemption might raise £1.6 billion in additional tax revenues per annum.
- This change would be administratively straightforward.
- There are likely that there will be few behavioural consequences arising from this change.

<b>The proposal</b>	To abolish VAT exemption on the supply of education by private schools.
<b>Reason for the proposal</b>	1. To increase the prospect of vertical equity of taxation when the current exemption for VAT charges on

<sup>1</sup> This note forms a part of 'The Taxing Wealth Report 2024' published by Finance for the Future LLP, which is UK LLP number OC329502, registered at 33 Kingsley Walk, Ely, Cambridgeshire, CB6 3BZ. See <https://www.financeforthefuture.com/taxing-wealth/>. This note was written by Richard Murphy FAcSS FCA FAIA (Hon), Professor of Accounting Practice, Sheffield University Management School, who is a director of Finance for the Future LLP. © Finance for the Future 2023.

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and



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	<p>private school fees provides a benefit very largely enjoyed by the wealthiest in society.</p> <p>2. To raise additional sums in additional tax revenues.</p> <p>3. To reduce wealth inequality in the UK which this exemption increases.</p>
<b>Estimated tax that might be raised as a result of the recommendation made</b>	<p>There are unlikely to be many behavioural consequences to this recommendation, as the Institute for Fiscal Studies has noted when discussing this issue<sup>2</sup>.</p> <p>The current estimated cost of this tax relief is £1.6 billion per annum. It is assumed that this revenue would be collected if this exemption was removed.</p>
<b>Ease of implementation</b>	Relatively straightforward. Most private schools are already VAT registered for some of their activities.
<b>Likely difficulties that might result from implementation</b>	Few.
<b>Likely time required to implement the change</b>	At least two years notice might be required to make this change simply to allow appropriate management of the process to take place.
<b>Consultation period required.</b>	A reasonable consultation period will be required.

## Background

Value added tax (VAT) can be applied to a supply of goods and services in the UK in one of four different ways. Three involve a charge to VAT being added to the value of the supply made at differing rates<sup>3</sup>:

Rate	Rate of tax charged	Impact
Standard rate	20%	A VAT charge of 20% is added to the charge made for the supply of goods and services e.g. if

<sup>2</sup> <https://ifs.org.uk/publications/tax-private-school-fees-and-state-school-spending>

<sup>3</sup> <https://www.gov.uk/vat-rates>

		the value of those goods and services is £100 then a VAT charge of £20 is added and the customer must pay £120 for their supply.
Reduced rate	5%	A VAT charge of 5% is added to the charge made for the supply of goods and services e.g. if the value of those goods and services is £100 then a VAT charge of £5 is added and the customer must pay £105 for their supply.
Zero rate	0%	No VAT is added to the value of a supply, but it is deemed that a charge has been made for the purposes of the administration of the tax.

Unsurprisingly the standard rate of VAT is applied to most goods and services.

The reduced rate of VAT is applied to domestic energy supplies and some other supplies deemed essential e.g. sanitary products and children’s car seats.

Zero rating applies to food, children’s clothing and some other items, mainly related to charitable activities.

A VAT registered business (which is in broad terms is one making VAT chargeable supplies of more than £85,000 a year) has to add VAT charges at the appropriate to the sums it bills its customers and pay over the sums collected to HM Revenue & Customs. It has some recompense for doing so: it is permitted to reclaim from HMRC the cost of VAT charged to it in the course of its trade. This means that, in effect, zero rated businesses and their customers are in receipt of a tax subsidy.

The fourth category of charge that can apply to the goods and services that a business might supply to its customers is VAT exemption. When a business supplies VAT exempt goods and services then there is no VAT charged added to the charge that they make. Superficially this looks similar to supplying VAT zero rate goods and services. It does, however, differ because a business making VAT exempt supplies cannot reclaim the VAT charged to it in the course of its trade.

VAT exemption applies to a range of goods and services including:

- Land, although this is a complex area. Domestic rents rate, for example, VAT exempt whereas commercial rents can be subject to VAT.
- Insurance. Almost all insurance transactions are exempt from VAT but many are subject to Insurance Premium Tax instead.
- Postal services provided by the Royal Mail are VAT exempt but others are not.
- Education and training when provided by an eligible body like a school, college or university are VAT exempt, but most that is supplied for profit e.g. professional training courses, are not.
- Finance. Most supplies of financial services are exempt from VAT but those such as book-keeping and accountancy, debt collection, management consultancy and some investment and almost all finance and taxation advice are usually not. Banking and pension services are the main beneficiaries of this exemption.
- Health and welfare. Healthcare is a complex area for VAT. Exempt supplies include those provided by a qualifying institution like a hospital, hospice or nursing home and for health services provided by registered doctors, dentists, opticians, pharmacists and other health professionals.
- Investment gold is exempt from VAT.
- Some sports activities are exempt, but like education this exemption largely applies to sport and related education services supplied by eligible bodies.
- Gaming, including betting and gaming, bingo, and lotteries are normally exempt from VAT, although the rules are complex.
- Culture. Some admission charges to public and other bodies are exempt subject to specific conditions.
- Qualifying events held by charities are VAT exempt.
- Funerals are VAT exempt, as are a range of other items of less significance.

### Recommendation

It is recommended that the VAT exemption for the supply of education services by private schools be removed.

This recommendation might not have been possible if the UK was still in the European Union, but it has left and since no major political party is recommending a return at present changes in VAT exemption rules can now be made by the UK.

In 2023 HM Revenue & Customs estimated<sup>4</sup> that the cost of the VAT exemption for education was £5.2 billion. The Institute for Fiscal Studies<sup>5</sup> has estimated that approximately £1.6 billion of this might relate to the exemption for education provide by private schools. That suggestion is accepted here.

The reason for making this suggestion is that the majority of those children educated at private schools will be the offspring of parents or grandparents with significant income and wealth and as such this subsidy is being provided to those who have no economic reason to enjoy it. The subsidy contravenes the principle of vertical tax equity by subsidising those who are already wealthy.

The Institute for Fiscal Studies has suggested that there will be little behavioural response to this change in taxation. Given that the whole purpose of most parents in sending their children to private schools is to remove them from the influence of state education whilst providing them with the well-recognised economic and social advantages that private education has, to date, supplied this conclusion is accepted here.

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<sup>4</sup> <https://www.gov.uk/government/statistics/minor-tax-expenditures-and-structural-reliefs/structural-tax-relief-statistics-january-2023>

<sup>5</sup> <https://ifs.org.uk/publications/tax-private-school-fees-and-state-school-spending>