HM Treasury

Government Response to the Technical Note on Applying VAT to Private School Fees and Removing the Business Rates Charitable Rate Relief

Summary of Responses

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Chapter 1
Background

1.1 On 29 July, the government announced that, as of 1 January 2025, all education, boarding, and vocational training provided for a charge by a private school in the UK will be subject to VAT at the standard rate of 20 per cent. Any fees paid from 29 July 2024 relating to the term starting in January 2025 onwards will be subject to VAT.

1.2 The government also announced that schools in England with charitable status would lose their eligibility to business rates charitable rate relief from April 2025, subject to Parliamentary passage of the legislation.

1.3 Together, these policies are expected to raise around **£1.8 billion a year by 2029/30,** which will help deliver the government's commitments relating to education and young people. The government has announced at Autumn Budget 2024 **a £2.3 billion increase to the core schools budget for financial year 2025/26,** increasing per pupil funding in real terms.

1.4 The government published a technical note in July setting out the details of these two tax policies and seeking views on the draft VAT legislation that was published alongside it. This consultation ran for 7 weeks until 15 September. The government received 17,502 responses ahead of the consultation closing date from a range of tax specialists, parents, schools, bodies that represent private schools (including faith schools and special schools), and others.

1.5 These written submissions were supplemented by a series of meetings with key stakeholders representing schools, local authorities (LAs) and Devolved Governments carried out by the Exchequer Secretary to the Treasury and government officials. The government is grateful to all of those who have taken the time to contribute to this consultation process.

1.6 As set out in the technical note, when designing these tax policies, the government has sought to strike the right balance between the following principles. These principles have also guided the technical amendments to the policies that have been made following this consultation:

1. Raise revenue to support the public finances and help deliver the government's commitments relating to education and young people.
2. Ensure high-quality education is available for every child.

3. Be fair, with all users of private schools paying their fair share, whilst ensuring that pupils with the most acute needs are not impacted.
4. Minimise administrative burdens for taxpayers and HMRC, whilst ensuring these policies are not open to abuse.

1.7 The amendments being made to the draft VAT legislation following this consultation can be summarised as follows:

- **Higher Education (HE)** taught at schools that are otherwise in scope of the policy (for instance, performing arts schools) will be carved out of the VAT policy.
- To ensure that education provided by **Further Education (FE) colleges** remains exempt from VAT, the second limb of the definition of a private school has been amended so that only institutions that are wholly or mainly concerned with providing education suitable for 16-19 year olds, and where the <u>majority</u> of 16-19 year old pupils are charged fees are within scope of this policy.
- **Independent Training Providers and Independent Learning Providers (ITPs and ILPs)** will be carved out of the legislation. ITPs and ILPs are defined as “an institution at which education or training suitable to the requirements of persons over compulsory school age (or, in Scotland, school age) but under 19, and where the consideration for [that provision] is payable by the relevant contracting authority under that contract”. A relevant contracting authority means the Secretary of State, Medr (Commission for Tertiary Education and Research), the Department for the Economy in Northern Ireland, or Skills Development Scotland.
- The definition of a **nursery class** will be changed to “a class that is composed <u>wholly (or almost wholly)</u> of children who are under compulsory school age or, in Scotland, school age, and would not be expected to attain that age while in that class”.
- **Teaching English as a Foreign Language (TEFL) courses** taught by private schools, or connected persons, will be carved out of the policy.
- The **connected persons test** set out at Note (2)(a) in the draft legislation will be removed. The other two connected persons tests will remain in the final legislation.
- **Non-maintained special schools (NMSS)** will be brought within scope of this policy, but will only be required to charge VAT on placements paid from 30 October pertaining to terms starting in January 2025 onwards.
- The **power to amend the anti-forestalling provisions** outlined at 2(3) in the draft legislation will be removed.

1.8 This document provides a summary of the main points raised throughout the consultation period, and the government's responses to these. Chapter 2 responds to questions 1 – 4 of the consultation and clarifies the scope of the VAT policy. Chapter 3 responds to question 5 of the consultation and provides an overview of the points raised in relation to Special Educational Needs and Disabilities (SEND), Chapter 4 summarises the feedback shared on the business rates policy, Chapter 5 outlines the expected impact of the policies, whilst Chapter 6 provides an overview of other comments that were commonly raised by respondents. Annexed is the methodology used to calculate the VAT costing, which has been certified by the independent Office for Budget Responsibility (OBR).

Chapter 2

Scope of the VAT Policy

2.1 In the draft VAT legislation published at the time of the announcement, a private school was defined as "a school at which full-time education is provided for pupils of compulsory school age or, in Scotland, school age (whether or not such education is also provided for pupils under or over that age), or an institution at which full-time education is provided for persons over compulsory school age but under 19 and which is principally concerned with providing education suitable to the requirements of such persons (for example, a sixth form college), and where fees or other consideration are payable for that provision of full-time education.

2.2 Standalone nursery schools (which were undefined in the legislation), and nursery classes attached to private schools (defined as "a class that is composed wholly of children who are under compulsory school age, or, in Scotland, school age, and who would not be expected to attain that age while in that class") were carved out of this definition. NMSS were also carved out of this definition.

2.3 The draft clauses also contained a "connected persons test" as an anti-avoidance measure to prevent schools from contracting their services out to eligible bodies in order for the education and boarding services they provide to remain exempt from VAT.

2.4 Questions 1 – 4 of the technical note sought views on the definition of a private school, and the connected persons test, used in the draft legislation:

Question 1: Does the above definition of private schools capture all private schools across the UK?

Question 2: Does this definition inadvertently capture any organisations that this policy does not intend to capture?

Question 3: Does the above "connected persons" test capture the relationships that exist between private schools and third parties?

Question 4: Does this "connected persons" test inadvertently capture any relationships that it is not intended to capture?

2.5 Of the respondents who answered questions 1 and 2, many agreed that the definition of a "private school" used in the draft clauses captured the institutions it was seeking to capture. However, some respondents raised concerns that this definition inadvertently captured institutions that either it wasn't seeking to capture, or that, in the respondent's view, should not be within scope of this policy.

2.6 For instance, a large number of respondents called for **small faith schools** to be carved out of this policy as they did not consider comparable education to be available in the state sector, and fees at some faith schools can be lower than the amount spent on pupils in the state sector. Some respondents also suggested that small faith schools do not incur as much VAT on their purchases (known as "input VAT") as other private schools, as they do not typically own their premises and aim to keep costs low. Respondents therefore argued that small faith schools did not have as much to gain by way of input VAT recovery from being VAT registered as bigger, wealthier private schools. As a result, suggestions for how to carve out small faith schools were proposed by some respondents.

2.7 A number of respondents asked that **international schools** be carved out of the policy. Respondents noted that these schools provide continuity of education for children who move to the UK for only a short period, as well as allow pupils to receive education in their first language and to learn the curriculum taught in their home country. Respondents also argued that there is no comparable state education in the UK, and that British schools in other countries are not required to charge VAT.

2.8 Concerns were raised that the definition could capture **universities** with pupils below the age of 19, and that **performing arts schools** offering both full-time education to children of compulsory school age and/or FE, as well as HE, would be within scope of both changes, whilst performing arts schools that exclusively taught HE would be out of scope.

2.9 More broadly, some respondents called for performing arts schools to be carved out of the policy, arguing that they are not typical private schools. Respondents also noted that many pupils at these institutions are in receipt of bursaries and that parents of pupils at these schools may be less able to afford higher fees.

2.10 A small number of respondents queried whether other institutions that some people may not typically regard to be private schools – namely, **online schools** and **secure accommodation** – would be within scope.

2.11 There were also concerns raised that **voluntary grammar schools (VGS) in Northern Ireland,** which are not deemed to be private schools but do charge parents fees, would be within scope of this policy.

2.12 It was also queried during stakeholder engagement whether **ITPs and ILPs**, which provide vocational education and training to 16-19 year olds and adults, would be within scope of this policy.

2.13 Concerns were also raised that some **public funds received by FE institutions** may be regarded as fees for private education and could inadvertently be captured by these changes. This is because the Upper Tribunal's judgment in *Colchester Institute Corporation (2020)*

UKUT 0368 (TCC) ("Colchester") suggested that grants provided to FE institutions should, contrary to HMRC's long standing position, be treated as consideration for the supply of education, and therefore be within scope of VAT.

2.14 Some respondents raised concerns over how **"nursery class"** was defined in the draft legislation, noting that it would only take one child being above compulsory school age to bring the whole nursery into scope of the policy. Some respondents said this was a particular issue in Scotland, where it is possible for parents to request that their child's place in a primary school be deferred for a year if they feel their child is not yet ready to attend school. It was suggested, therefore, that there could be more children above school age in a nursery attached to a private school in Scotland than elsewhere in the UK.

2.15 A number of respondents also queried whether **TEFL courses** taught by a private school, or a closely connected person, would be subject to VAT, and if so, the fairness of this, given that these courses are exempt from VAT when supplied by a commercial provider.

2.16 Of those who responded to questions 3 and 4 about the **connected persons test**, most agreed that the test was sufficiently strong, and that it did not inadvertently capture any relationships between private schools and third parties that it was not seeking to capture. However, some respondents highlighted that the test set out in Note (2)(a) of the legislation (which stated that an eligible body should be treated as a private school if it is closely bound to a private school by financial, economic and organisational links) was very broad, which in turn could lead to confusion over what arrangements it would capture.

Government Response

2.17 The definition of a "private school" used in the VAT legislation is predicated on whether fees are charged for the full-time education of children of compulsory school age and/or the education of 16-19 year olds. Where there is state education available, but parents have chosen to pay for their child's education instead, VAT will apply. This is in line with the principles set out in the technical note. In particular, it ensures fairness and consistency between schools and parents.

2.18 The government has carefully considered all representations regarding the proposed scope of this policy.

2.19 The government has thoroughly assessed the impacts of the VAT policy on **small faith schools**, including considering all of the evidence submitted through the consultation process. Based on the evidence provided, it is not apparent that small faith schools will be affected more by this policy than other schools. This is because, while fees of many small faith schools are lower than average, the VAT charge will be commensurately lower, resulting in a proportional charge that is comparable to that for other schools. Indeed, some faith schools are likely to be less than proportionately impacted if their income is derived not only from fees but also from other sources, such as voluntary donations from the community, or support from religious organisations. This is because donations that are freely given and where there is no reciprocal obligation are outside the scope of VAT. As such, not all of the income that small faith schools receive will be subject to VAT. Small faith schools will, however, be able to reclaim all of the VAT they pay on goods and services used to deliver education and boarding services. Thus, they may benefit from a lower net effective rate of VAT.

2.20 This is illustrated in the simplified examples below. Small faith school A has a net effective VAT rate of 15.8 per cent, which is the same as that of the larger non-faith school, whilst small faith school B has a lower effective VAT rate of 11.6 per cent.

	Small Faith School A	Small Faith School B	Non-Faith School
Proportion of income from fees	100%	50%	100%
Average fee	£6,000	£3,000	£18,000
Number of pupils	100	100	400
Total fee income	£600,000	£300,000	£7,200,000
Total income	£600,000	£600,000	£7,200,000
VAT on fee income at 20%	£120,000	£60,000	£1,440,000
Non-staff costs as % of income	30%	30%	30%
Non-staff costs	£180,000	£180,000	£2,160,000
Average VAT rate on non-staff costs	14%	14%	14%
Input VAT reclaimable	£25,200	£25,200	£302,400
Net VAT liability	£94,800	£34,800	£1,137,000
VAT liability as % of fee income	**15.8%**	**11.6%**	**15.8%**

Figure 1: Illustrative examples of VAT liabilities for different schools

2.21 It was suggested during the consultation period that small faith schools may be less resilient, as they have little or no surpluses or reserves. The government acknowledges this point; however, for the private school sector in general, where the VAT liability is assumed to be absorbed by schools, very little of this is assumed to rely on reserves (see Annex). Thus, low reserves are not expected to directly lead to higher-than-average fee increases.

2.22 The government has also closely examined the proposals put forward for how small faith schools could be carved out of the policy, the most common of which was to carve out all schools with fees below a set threshold. The government concluded that none of the proposals put forward met the four principles of this policy. This is because any carve out would reduce the amount of revenue raised from this policy, be unfair to those schools with fees just above the threshold, and would create many tax avoidance opportunities that would be difficult for HMRC to police.

2.23 Furthermore, it is the government's position that state education is suitable for children of all faiths. All children of compulsory school age are entitled to a state-funded school place if they need one, and all schools are required to follow the Equality Act. These include fostering and promoting an environment that encourages respect and tolerance of children and families of all faiths and none. As a result of these considerations, **faith schools will remain in scope of this policy.**

2.24 The government also carefully considered representations to exclude **international schools** from the policy. The government recognises that international schools can, depending on their funding structure, be subsidised by foreign governments, and that international schools and the wider communities they support make an important cultural and economic contribution to the UK. However, many international schools still charge fees comparable to that of a lot of British private schools, and international schools will also sometimes educate British children.

2.25 The government recognises that education provided by British schools in other countries is not subject to VAT, but this is because no private schools in those countries are required to charge VAT. British international schools in other countries do not benefit from preferential treatment. Therefore, to ensure consistency of treatment between private schools whose pupils' parents are choosing to send their children to that school when there is state education available, and to protect the amount of revenue raised by this policy, **international schools will remain in scope of this policy.**

2.26 It is worth noting that, under education law, all foreign national children have a right to attend state-funded schools in England. Schools are required to ensure that all of their pupils can access the full curriculum, and schools receive funding for those pupils with a first language other than English who have started in the state-funded education system in England in the last three years. Schools also have flexibility over how they use their overall budgets to support the specific needs of pupils with limited or no proficiency in English. Comparable support is also available in the Devolved Governments.

2.27 **Performing arts schools that offer full-time education to children of compulsory school age and/or 16-19 year olds for a charge will remain in scope of this policy.** This is to ensure fairness and consistency across all schools that provide education services and vocational training for a charge. Furthermore, in addition to providing performing arts education, when educating children of compulsory school age, these institutions will also provide academic education. It is the government's position, therefore, that carving these schools out of the policy would be unfair to other private schools.

2.28 However, to ensure consistency of VAT treatment between **HE** taught at universities (which are not within scope of this policy), and HE taught at institutions that are within scope of this policy (such as performing arts schools), HE will be expressly carved out of this policy:

- In England and Wales, a HE course has the meaning given by section 83(1) of the Higher Education and Research Act 2017.
- In Scotland, HE is a course of any description mentioned in section 5(3) of the Further and Higher Education (Scotland) Act 2005.
- In Northern Ireland, HE is a course of any description mentioned in paragraph 1 of Schedule 1 to the Further Education (Northern Ireland) Order 1997 (S.I. 1997/1772 (N.I. 15)).

2.29 As set out in the technical note, education services supplied by an eligible body are exempt from VAT. **Online schools** are not recognised as schools within the meaning of the Education Act 1996, the Education Act (Scotland) 1980, the Education and Libraries (Northern Ireland) Order 1986, or the Education Reform (Northern Ireland) Order 1989. Therefore, unless an online school is a not-for-profit organisation meeting certain conditions, it will not normally meet the conditions for being an eligible body. As such, **online schools are, and will likely always have been, liable to charge VAT at the standard rate on all of the education services that they provide. This will not change.**

2.30 Where a single fee is paid for **secure accommodation** to cover all aspects of the service they provide (for instance, welfare, education, and residential care), secure accommodation will not be within scope of this policy. This is because the predominant element of the supply will not be education. A fundamental principle of VAT is that, where a single supply consists of multiple elements, the VAT treatment of the whole supply is dictated by the predominant element of the supply. However, where a separate fee, or increased amount, is paid for young people to attend a school, while they are living in secure accommodation, that education-related fee or increase will be subject to VAT (providing the institution otherwise meets the definition of a "private school" as set out in legislation and their taxable income exceeds the VAT threshold of £90,000 p.a.). If an LA is funding the education (as will be the case in most instances), they will be able to reclaim the VAT they are charged via the Section 33 VAT Refund Scheme.

2.31 The UK government recognises that, in Northern Ireland, **VGS** are not regarded as private schools because they receive grant funding from the Northern Ireland Executive. There are a number of factors considered when determining if an organisation is carrying out economic activity that is subject to VAT. Where VGS only charge a capital fee of up to £140, which is ringfenced for capital expenditure, these VGS will remain outside the scope of VAT, as there is not a strong enough link between the fees charged and the education they provide to constitute business activity.

2.32 However, where a VGS has a preparatory department and/or boarding department that it charges fees for, the preparatory and boarding fees will be within scope of VAT. This ensures fairness and consistency amongst parents across the UK who choose to pay for their children's education when there is a state-funded alternative available. This is also in line with how schools in other parts of the UK that receive government grants in addition to charging fees will be affected by this policy.

2.33 Turning to **FE institutions** – to ensure the legislation achieves the policy intention of capturing private sixth forms (both those attached to private schools and standalone sixth forms), but does not capture FE colleges, amendments have been made to the definition of a private school used in the draft legislation. The second limb of the definition of a private school now defines the FE within scope of this policy as "an institution which is wholly or mainly concerned with providing education suitable to the requirements of persons over compulsory school age (or, in Scotland, school age) but under 19, at which full-time education is provided for such persons, where the provision of [that full-time education] is wholly or mainly provision in respect of which fees or other consideration are payable, and which is not an independent training or learning provider." In practice, this means that only those institutions that are principally concerned with providing education suitable for 16-19 year olds and where the majority of their 16-19 year old pupils are charged fees are caught by this definition. The government is confident that this definition does not capture FE colleges, because such institutions are not permitted to charge domestic 16-19 year old pupils fees.

2.34 The government is aware that some FE colleges may have international pupils aged 16-19 who are charged fees, because, in order to be eligible for state-funded FE, international pupils typically need to be of "settled status" and have been "ordinarily resident" in the UK for 3 years. To ensure consistency of tax treatment of all pupils at FE colleges who pay fees (i.e. adult learners and 16-19 year old international pupils), international pupils' fees at FE colleges will not be within scope of this policy. This is in line with the fairness principle set out in Chapter 1, as these pupils are not eligible for state-funded FE. It also ensures that FE colleges remain accessible to a wide range of people, thereby supporting the government's objective to increase labour market activity.

2.35 Similarly, **ITPs and ILPs**, which are akin to FE colleges in that they provide vocational training and apprenticeships to 16-19 year olds and adults, are carved out of this policy. ITPs and ILPs are defined in the VAT legislation as "an institution at which education or training suitable to the requirements of persons over compulsory school age (or, in Scotland, school age) but under 19, and where the consideration for [that provision] is payable by the relevant contracting authority under that contract". A relevant contracting authority means the Secretary of State, Medr (Commission for Tertiary Education and Research), the Department for the Economy in Northern Ireland, or Skills Development Scotland.

2.36 ITPs and ILPs are expressly carved out of the legislation, as the Department for Education (and equivalents in the Devolved Governments) fund 16-19 year olds' places in ITPs and ILPs via commercial contracts, which are deemed to be consideration for a supply of education. 16-19 year olds' places in FE colleges, on the other hand, are generally funded via block grants, which are outside the scope of VAT. As such, FE colleges funded via block grants are not caught by the definition of a private school used in this legislation, and therefore do not need to be explicitly carved out.

2.37 Regarding concerns that **public funds received by FE institutions** may be regarded as fees for private education and may be within scope of this policy as a result of *Colchester*, HMRC does not actively impose the Upper Tribunal's decision and is taking steps to test the primary decision on the treatment of public monies via a new appeal. This means that it remains open to institutions that continue to treat such education as non-business to claim reliefs, where all the relevant criteria have been met.

2.38 Institutions can, if they choose to, apply the conclusion of the Upper Tribunal in *Colchester,* which would result in them treating the public funds they receive as business income. This could bring these institutions within scope of this policy, as this income would be treated as consideration for the provision of education. However, FE institutions should carefully consider this decision and ensure they understand what their new VAT obligations would be and the financial implications of this. Providers who do this should also consider if they need to submit any error correction notices for any under or overpayment of VAT, including adjustments to previous claims for charitable reliefs.

2.39 The government has listened to feedback regarding the definition of **"nursery class"** used in the draft legislation. To ensure the legislation achieves the policy intent of keeping nursery education exempt from VAT across the UK, the definition of a nursery class has been amended to: "a class that is composed wholly (or almost wholly) of children who are under compulsory school age or, in Scotland, school age, and would not be expected to attain that age while in that class". Therefore, providing the majority of children in the nursery class are under compulsory school age and aren't expected to turn compulsory school age that year, the whole nursery class will remain exempt from VAT. Nursery schools not attached to a private school will remain exempt from VAT, regardless of the age of their pupils.

2.40 The government has also listened to concerns about **TEFL courses** taught by a private school or a connected person being subject to VAT when TEFL courses taught by a commercial provider are exempt from VAT. To ensure parity of tax treatment between comparable supplies, TEFL courses taught by a private school, or a connected person, will be carved out of the policy. For the purposes of these clauses, TEFL will take its natural meaning as it does in Group 6 of Schedule 9 of the VAT Act 1994.

2.41 The government has reviewed the **connected persons tests** contained in the draft legislation and is confident that the tests set out at Notes (2)(b) and (2)(c) in the draft legislation are sufficiently strong to guard against any potential tax avoidance. The test set out at Note (2)(a) in the draft legislation has therefore been removed to avoid uncertainty amongst taxpayers.

Chapter 3

Special Educational Needs and Disabilities

3.1 As set out in the technical note, where a pupil's place in a private school is funded by an LA or Devolved Government because the state does not deem their needs to be able to be met in the state sector, LAs and Devolved Governments will be compensated for the VAT they pay on these pupils' fees.

3.2 Question 5 of the technical consultation sought views on whether this approach to protecting pupils with the most acute SEND met the intended policy aims across all four UK nations.

3.3 Whilst not many respondents answered this question specifically, many respondents commented in general on the impact of this policy on pupils with SEND. In particular, respondents raised concerns that parents feel many pupils have needs that cannot be met in the state sector, despite not qualifying for an Education, Health and Care Plan (EHCP), or equivalent in the devolved nations. Respondents also highlighted that the smaller class sizes and more specialised provision that private schools can offer make them more suitable settings for pupils with some forms of SEND, even if their core needs could be met in the state sector.

3.4 A number of respondents also raised concerns with the current EHCP system in England, highlighting in particular that waiting lists can be long and that LAs' decisions to refuse an EHCP are frequently overturned at Tribunal. Some respondents therefore called for all children with SEND who attend a private school to be carved out of the policy.

3.5 Other respondents suggested that all private special schools should be carved out of the policy, arguing that registering for, and charging, VAT is disproportionately burdensome for schools with a high proportion of LA- or Devolved Government-funded pupils, as the VAT they charge on their pupils' fees will ultimately be recovered from HMRC. Some respondents also suggested that it would be burdensome for LAs to reclaim the VAT they pay on pupils' fees.

3.6 There were particular calls to carve out Scottish grant-aided special schools, which cater for pupils with complex needs. Some respondents also queried whether Special Post-16 Institutions (SPIs) were in scope of the changes, and called for them to be carved out if they were, as they have a high proportion of pupils with EHCPs.

3.7 Respondents who represent NMSS highlighted concerns that they were the only type of special school that would not be able to reclaim their input VAT. Moreover, other respondents questioned how carving NMSS out of the policy aligned with the broader approach to pupils with SEND – that all pupils who attend a private school (as defined in this piece of VAT legislation) are within scope of the policy, but where places are funded by an LA or Devolved Government because the child's needs cannot be met in a state school, LAs and Devolved Governments will be compensated for the VAT they are charged on those pupils' fees.

Government Response

3.8 As set out in the technical note, the government is committed to ensuring that pupils with the most acute SEND (referred to as additional support needs in Scotland and additional learning needs in Wales) are not impacted by this policy. Therefore, in England, Scotland and Wales, where a pupil's place in a private school is funded by the LA (rather than parents and carers) because the pupil's needs cannot be fully met in the state sector, or are best met elsewhere, LAs will be able to reclaim the VAT they are charged on the fees of these pupils via the Section 33 VAT Refund Scheme.

3.9 In 2023/24, £14.7 billion was reclaimed from HMRC through the Section 33 Refund Scheme, the vast majority of which was reclaimed by LAs. The government is therefore confident that LAs are already very familiar with the process of reclaiming VAT via the Section 33 scheme, something that was endorsed by bodies representing LAs that the government engaged with during the consultation process.

3.10 In Northern Ireland, it is the Education Authority, a non-departmental public body of the Department of Education that is responsible for funding placements of pupils with a statement of SEN within a private school. The Education Authority will be able to recover the VAT it is charged on pupil's fees via the Section 99 VAT Refund Scheme. In 2023/24, £640 million was reclaimed via the Section 99 Refund Scheme. Again, therefore, the government is confident that this approach will not place an additional burden on the Northern Ireland Executive.

3.11 For pupils over 16 in Wales who require a place in a private special college because their needs cannot be met in the state sector, the Welsh Government, rather than LAs, currently funds their places. In the 2028/29 financial year, this responsibility will transfer over to LAs. The Welsh Government will be given additional funding to cover the VAT they will be charged on these pupils' fees, which will be ringfenced for these purposes.

3.12 This approach ensures that parents and carers of pupils with a LA- or Devolved Government-funded place in a private school will not be impacted by this policy change. The government recognises that some parents may choose to send their child to a private school because they feel that school is better able to meet their child's needs than the state sector, even if their child doesn't have an EHCP or equivalent. **However, in line with the third principle (be fair, with all users of private schools paying their fair share, whilst ensuring that pupils with the most acute needs are not impacted), VAT will apply to these pupils' fees.** This is because, both for fairness reasons and to protect Exchequer revenue, the government deems it important for preferential VAT treatment to be tied to a formal, independent assessment that a child's needs cannot be met in the state sector. Carving all children with SEND out of this policy would carry a significant cost, and therefore undermine the government's ability to improve education for the 94 per cent of school children in the UK that attend state schools, including for the over 1 million children in the state sector with SEND.

3.13 The government will take a community-wide approach, improving SEND provision in mainstream state schools, as well as ensuring state special schools cater to those with the most complex needs. **The government is committed to reforming England's SEND provision to improve outcomes and return the system to financial sustainability, and will provide a £1 billion uplift in high needs funding for financial year 2025/26.**

3.14 The Government has also carefully considered proposals to carve all special schools out of this policy. However, this approach would result in the fees of privately-funded pupils in attendance of private special schools being exempt from VAT, whilst the fees of pupils attending mainstream private schools (including those with SEND) would be subject to VAT. The government deems this to be unfair, given that, in both cases, parents have made a choice to send their children to private schools when the state deems there to be appropriate provision in the state sector for these pupils.

3.15 Furthermore, the ability to recover input VAT will outweigh the administrative burden of being a VAT-registered business for the vast majority of special schools. Indeed, as demonstrated in Figure 2, government analysis suggests that, even where a high proportion of special schools' costs are spent on staffing, on average, they are expected to be able to reclaim a significant amount of money each year. **As such, it is more financially advantageous for schools that have a high proportion of their fees paid by LAs or a Devolved Government to be within scope of VAT, rather than exempt, as the amount of input VAT they are able to recover will outweigh the VAT they charge on fees that is not refunded under Sections 33 or Section 99 discussed above. Even special schools with a less high proportion of fees funded by bodies eligible for VAT refunds will see their VAT liability significantly mitigated by their ability to reclaim**

input VAT on all their educational services, including those supplied to the bodies receiving refunds of VAT.

Number of pupils	35
Average fee per pupil	£65,000
Income	£2,275,000
Non-staff costs as % of fee income [1]	20%
Non-staff costs	£455,000
Average VAT rate on non-staff costs	14%
Input VAT reclaimable	**£63,700**

Figure 2: Illustrative example of private special schools' annual VAT recovery

3.16 In line with the approach taken with special schools in the rest of the UK, **grant-aided special schools in Scotland will remain in scope of this policy.** The block grants that the Scottish Government provide to grant-aided special schools fall outside the scope of VAT, as they are not pupil specific. The funding that LAs pay for individual pupils will be subject to VAT, but LAs will be able to reclaim this VAT via the Section 33 VAT Refund Scheme.

3.17 Similarly, in line with the approach taken with private FE institutions and special schools, **where SPIs are principally concerned with providing education suitable for 16-19 year olds and where the majority of 16-19 year old pupils are charged fees, they will be within scope of this policy**. The vast majority of young people at SPIs have their places funded by LAs or a Devolved Government, because the SPI is named in their EHCP, or equivalent. SPIs within scope of this policy will be able to recover all of their input VAT that relates to their taxable supplies. Any grant funding that SPIs receive from the Education, Skills and Funding Agency (ESFA) will not be subject to VAT.

3.18 **The government has listened to calls for NMSS to be able to recover their input VAT and has taken the decision to bring them within scope of this policy to provide consistency with other non-state-funded special schools**. NMSS are funded via block grants from the ESFA, which are outside the scope of VAT, and top-up funding from

[1] Stakeholders suggested during the consultation period that, on average, 80 per cent of special schools' expenditure is spent on staff costs due to their high staff to pupil ratios. This is slightly above the expected average for other types of private schools.

LAs based on the needs of individual pupils. The LA funding will attract VAT because it is pupil specific. However, as set out above, LAs will be able to recover that VAT. As NMSS were not within scope of this policy at the time it was announced, they will not be subject to the anti-forestalling provisions contained within the legislation. This means that **only placements for NMSS paid from 30 October pertaining to the term starting in January 2025 onwards will be subject to VAT**.

Chapter 4
Business Rates

4.1 Business rates are a tax that apply to all non-domestic properties in England, unless specifically exempt from rating. The revenue is a vital source of local government funding, used to fund local services, such as adult social care, and for broader government priorities, including education.

4.2 Where a school in England has charitable status, it is currently eligible for mandatory charitable rate relief of 80 per cent. LAs have the additional flexibility to provide a further discretionary relief of 20 per cent. The business rates system also includes a full exemption for property, or parts of a property, used wholly for disabled persons. This is applied by the Valuation Office Agency (VOA) and such property is excluded entirely from business rates. The exemption applies across both state and private schools.

4.3 As set out in July, **the government is removing the business rates relief that private schools that are charities benefit from.** The Ministry of Housing, Communities and Local Government (MHCLG) will bring forward primary legislation to amend the Local Government Finance Act 1988 to end relief eligibility for private schools intended to take effect from April 2025, subject to Parliamentary process.

4.4 The technical note published in July provided an overview of the scope and design of the two tax policy changes. Though the technical note did not include specific questions on the business rates policy, it invited comments on technical elements of the policies and noted the government's intention to consider how best to address impacts of the policy change, where a pupil's placement at a private school was specified in their EHCP. As a result, responses to the technical note focused largely on the VAT policy. Responses that engaged with the business rates changes were more limited and focused largely on expressing concerns over the impacts of the policy, and on seeking clarity on scope of the measure and its impact on specific types of education provider.

4.5 On points of concern, a number of respondents raised concerns on the cumulative impact of both policy changes on small faith schools. On points of clarity, respondents sought clarification on the treatment of FE colleges, SPIs, performing arts schools, and LAs' ongoing ability to award discretionary relief.

4.6 In developing the policy and considering responses to the technical note, the government has sought consistency between the

VAT and business rates changes. Recognising, however, that business rates is a tax on non-domestic properties rather than the individual supply of education, there are some areas where a different approach has been taken on business rates.

Government Response

4.7 As stated above, the government committed to consider the impact of this change on children with SEND. The government has carefully considered the distribution of EHCP pupils in private schools in England, noting that the vast majority either have a low or very high proportion of EHCP pupils. To ensure that schools focused on provision for pupils with an EHCP are not impacted by this policy change, the government will ensure that **charitable rate relief is retained for private schools that are "wholly or mainly" concerned with providing full-time education to pupils for whom an EHCP is maintained**. For mainstream private schools that have some low level of pupils with an EHCP, the government does not consider these schools as distinguishable from other private schools and, as such, subject to the passing of legislation, will withdraw their eligibility to charitable rate relief.

4.8 On concerns about the cumulative impact of both policies on small faith schools, the government has carefully considered the impact this policy would have on **small faith schools.** As outlined in Chapter 2, there are significant challenges with carving out these types of schools. On business rates specifically, evidencing eligibility for a low fee-based carve out would create substantial new administrative burdens for schools and LAs. Moreover, there are 296 LAs in England responsible for business rates collection who would be required to monitor fees of all relevant private schools, adding complexity and risking inconsistency of treatment, which would not be in line with the third principle guiding these changes (be fair, with all users of private schools paying their fair share).

4.9 As also stated in Chapter 2, all children of compulsory school age are entitled to a state-funded school place if they need one, and all state funded schools are required to follow the Equality Act. As a result of the above, **faith schools will also remain in scope of the business rates policy.**

4.10 On points of clarity, the government has considered questions and representations on the treatment of FE colleges, performing arts schools, and SPIs. In respect of FE, the government has considered how best to deliver the policy intent of removing charitable rate relief for private schools providing education to pupils of compulsory school age and/or FE for a fee. Institutions **that are "wholly or mainly" concerned with full-time education suitable for persons over compulsory school age but under 19, where fees or other considerations are**

payable for that education will lose their eligibility to charitable rate relief. Conversely, those **16 to 19 institutions not "wholly or mainly" concerned with such pupils funded by fees or other consideration will retain their charitable rates relief** – this is most notably the case for publicly funded FE colleges. The same rules will apply equally to performing arts schools.

4.11 **ITPs** and **ILPs** are also carved out of this policy, given they are akin to FE colleges. For business rates, ITPs and ILPs are defined as "an institution at which education or training is provided for persons over compulsory school age but under 19, under a contract with the Secretary of State. And where the consideration for the provision is payable by the Secretary of State under that contract."

4.12 With regards to SPIs, as set out above, the business rates system already provides an exemption for property, or parts of a property, used wholly for disabled persons. As is also set out above, private schools that are "wholly or mainly" concerned with providing full-time education to pupils with an EHCP will retain eligibility for relief. The government expects that, taken together, these measures will ensure that most special schools and SPIs run by charities will be exempt from business rates or, where they are liable for business rates, retain their charitable rate relief.

4.13 With regards to the ability of LAs to continue awarding discretionary rates relief, the government can confirm that existing discretionary relief powers provided by the Local Government Finance Act 1988 will be unaffected by the ending of charitable rate relief for private schools.

4.14 Finally, with respect to respondents' requests for greater clarity on the scope of these policy changes, schools that satisfy the definition of a private school will lose any entitlement to charitable rate relief entirely. This may include private schools with some nursery classes, which, despite the presence of some nursery provision will still be, by their nature, private schools. Standalone nursery schools, where they have their own business rates assessments, will be excluded from the legislation and, where applicable, retain their charitable rate relief. This approach best ensures consistency with the underlying policy intent.

4.15 Similarly, FE institutions teaching some HE that nevertheless satisfy the definition of a private school will lose any entitlement to charitable rate relief.

Chapter 5

Impacts Analysis

5.1 The majority of consultation respondents raised concerns over the impact these policies would have on pupils and their families across both the state and private sector, as well as the impact they would have on state and private schools. The government always wants to understand the impact of policies, and is grateful to all those who took the time to contribute views and evidence around the impact these policies may have.

5.2 In particular, respondents highlighted that these polices could lead to private school fees increasing, and that not all families who send their children to private schools would be able to afford higher fees. Some respondents suggested this could put families under financial strain, and ultimately, lead to family breakdown.

5.3 Respondents noted concerns that higher fees could also lead to some pupils from less wealthy families having to move into the state sector, arguing this would make private schools more exclusive. Respondents commented on the fact that this pupil movement could place pressure on state schools, and ultimately lead to overcrowding in state schools. Indeed, some respondents questioned whether these policies would raise any money, given that the government would have to pay for the pupils moving out of private schools to receive state education.

5.4 Many respondents argued that the mid-academic year VAT implementation date was disruptive for pupils who would have to move into the state sector, and that it could negatively impact their mental health. For instance, concerns were raised that it could be challenging to find state schools that would accept pupils mid-academic year, and it was noted that private schools typically require a term's notice to withdraw pupils. It was highlighted that it could be particularly challenging for those midway through GCSEs or A Levels to find local state schools offering the same syllabus and exam board as they had been studying at a private school.

5.5 It was claimed by some respondents that state education can be poor quality, and that parents taking their children out of private school would likely seek to send their children to the best state schools, thereby exacerbating socio-economic divides. Respondents highlighted that a potential knock-on consequence of this could be house prices within the catchment areas of good state schools increasing.

5.6 Some respondents raised concerns that military and diplomatic families who send their children to a UK boarding school to prevent them from having to move schools every time their parents are posted in a different country would not be able to afford to keep their children in boarding schools, unless the Continuity of Education Allowance (CEA) was increased. It was also suggested that fewer overseas families may opt to send their children to study in British private schools owing to fee increases.

5.7 Respondents noted that private schools are heterogeneous, with some having a greater ability to absorb their new tax liability than others. Some respondents remarked that these policies could impact on the amount of charity work schools are able to carry out, as well as the number of bursaries and scholarships they are able to offer students. Furthermore, it was highlighted that these policies could impact the quality and variety of education that private schools can offer, as schools may need to find cost savings to fund their new tax liabilities. It was suggested by some respondents that a higher quality of education can open up more career opportunities later in life, which can subsequently result in the Exchequer collecting higher personal tax revenues in future years.

5.8 Respondents commented that these policies may cause schools – particularly those that are small and/or in rural locations – to close. As well as creating acute pressures on surrounding state schools, it was suggested that this could have wider ramifications on the local community. For instance, teachers would lose their jobs and the school would stop contributing to the local economy.

Government Response

5.9 Whilst developing these policies, the government has carefully considered the impact they will have on pupils and their families across both the state and private sector, as well as the impact they will have on state and private schools. The government is grateful to those who provided data and insights throughout the consultation period, which has helped to refine this analysis. Further details on the impacts analysis contained within this chapter can be found in the Tax Information and Impact Note published alongside the Budget document. The methodologies for calculating the costings for the VAT and business rates measures have been certified by the independent OBR. The methodology for the VAT costing is set out in the Annex. The estimation of impacts, such as pupil movements, follows from the costing methodology.

5.10 As stated in the technical note, after recovery of VAT on their costs, on average, the government expects schools to be liable for VAT amounting to around 15 per cent of their fee income. It will be a commercial decision for individual schools how they fund this additional cost. As demonstrated in Figure 3, it is expected that many schools will be able to absorb a significant portion of their new VAT liability through drawing on reserves, recovering input VAT, and reducing costs. **On average, the Government expects private school fees to go up by around 10 per cent as a result of the introduction of VAT.** It is worth noting, however, that some schools have already said publicly that they are going to cap fee increases at 5 per cent, or indeed, absorb the full VAT cost themselves.

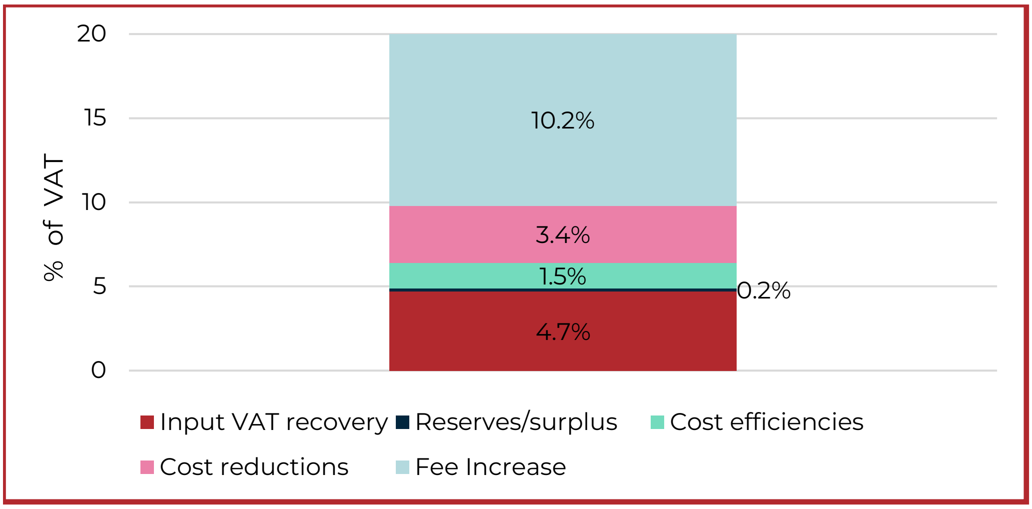

Figure 3: Average expected passthrough of VAT to school fees

5.11 A 10 per cent increase in fees (in addition to underlying growth) is not on an unprecedented scale: in the two years to 2004, average fees of member schools of the Independent Schools Council (ISC) increased by nearly 15 per cent above inflation, and the number of pupils in private schools has remained steady despite a 75 per cent real terms increase in average private school fees since 2000. **The government is confident that the vast majority of parents will be able to keep their child in private school, even if fees increase**. This view is strengthened by the fact that the majority of children attending a private school come from households that sit in the top two income deciles. Indeed, 40 per cent of children attending private schools come from the top income decile.

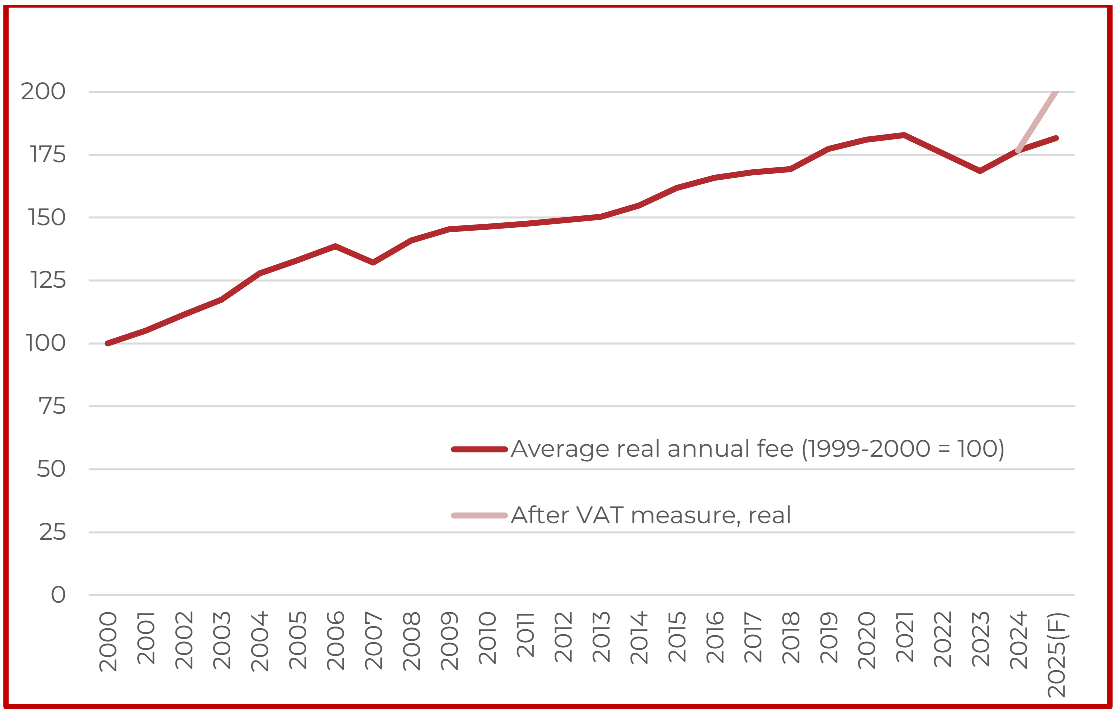

Figure 4: Historic and projected fee growth

Notes: Average fee growth for 2000 to 2024 based on ISC Census data, which represents around 80 per cent of private school pupils. Fee growth in 2025 before VAT based on projection used for costing. Fee growth in 2025 after VAT based on passthrough to fees of 10 per cent as assumed in costing (see paragraph 5.10). Real fee adjusted for Consumer Price Index in first quarter of calendar year (forecast for 2025).

5.12 The government recognises, however, that some parents may not be able or willing to pay higher fees. **The government estimates that, in the long-term steady state, 37,000 pupils will leave or never enter the UK private school sector as a result of the VAT policy. This represents around 6 per cent of the current private school population.** This estimate is within the Institute for Fiscal Studies' (IFS) estimated range of 20,000 to 40,000, and is significantly lower than some other public estimates. The government estimates that **approximately 3,100 additional pupils in England will leave or never enter the private school sector in England as a result of the business rates policy.**

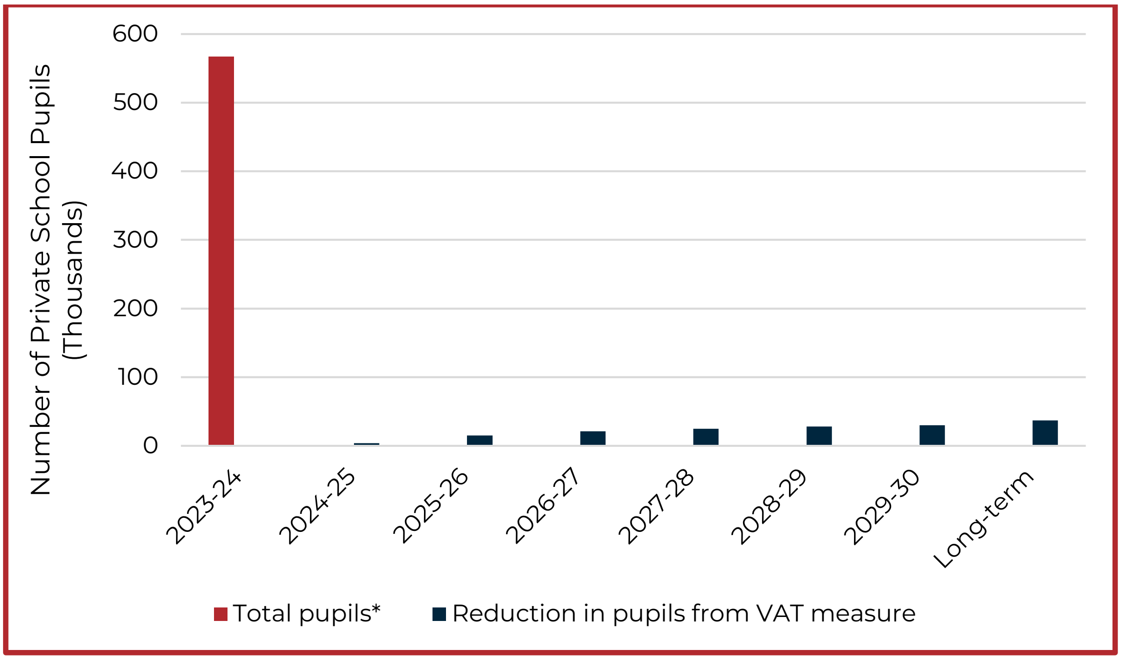

Figure 5: Expected decrease in pupils in private schools

*Excluding LA-funded pupils, where demand is not expected to be affected.

5.13 Of those leaving or never entering the private sector, **the government predicts that 35,000 pupils will move into UK state schools in the long-term steady state following the VAT policy taking effect in January,** with the other 2,000 either being international pupils who do not move into the UK state system, or pupils who move into homeschooling. This represents less than 0.5 per cent of total UK state school pupils, of which there are over 9 million. **The government expects approximately 2,900 pupils will move into state schools in England following the business rates policy taking effect. As such, the impact on the state education system as a whole is expected to be very small.**

5.14 Many of these moves are expected to take place at natural transition points, such as when a child moves from primary to secondary school, or at the beginning of exam courses. Furthermore, some parents will be opting not to send their child to private school when they otherwise might have done, rather than removing their child from a private school. The number expected to move before the end of the 2024/25 academic year is around 3,000.

5.15 This policy will result in some additional costs on state schools. Based on average 2024/25 per-pupil funding in England, the government expects the revenue costs of pupils entering the state sector as a result of the VAT policy across the UK and business rates policy in England to steadily increase to a peak of around £0.3 billion per annum after several years.[2] However, to put this in context, the UK Government expects to raise around £1.8 billion per annum from these policies by 2029/30. **Therefore, this policy is expected to have a very significant positive net impact on the Exchequer.**

5.16 Pupil numbers in schools fluctuate regularly for a number of reasons, and the school funding system in England is already set up to manage that. Education funding is a devolved matter; however, the Barnett formula will apply in the normal way for the Devolved Governments. For individual schools, the government therefore expects changes in pupil numbers caused by changes in VAT to be managed in the usual way.

5.17 Any pressure created by fewer pupils attending private schools will vary from area to area and will interact with other factors impacting state school capacity (such as an anticipated national-level decline in total pupil numbers in the coming years). All children of compulsory school age are entitled to a state-funded school place if they need one, and funding is also provided for post-16 education in all parts of the UK. LAs are responsible for ensuring sufficient state school places. The Department for Education and Devolved Governments already work with LAs to identify pressures and take action where necessary. For instance, the government provides capital funding through the Basic Need grant to support LAs in England to provide school places. The government has already announced over £700 million worth of Basic Need grant funding to support LAs in creating school places over this academic year and next. This funding can be used to provide places in new schools, as well as to expand existing schools, including academies and free schools.

5.18 The predicted increase in pupil numbers in state schools following this policy is expected to take place over several years and represents a very small proportion of overall pupil numbers in the state sector. For individual schools, the government expects changes in pupil numbers caused by the VAT policy to be managed in the same way as other pupil number changes. The majority of school funding in England is distributed on a per-pupil basis. This means that schools whose pupil numbers are increasing will see a commensurate increase in their funding the following year, as per the standard process. The Barnett formula will apply in the normal way for the Devolved Governments.

5.19 The government understands that moving schools can feel challenging. However, LAs and schools do already have processes in place to support pupils moving between schools, and children move between the private sector and the state-funded sector every year. Analysis published by the Department for Education in 2022 followed six cohorts of secondary school pupils in state-funded schools in

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[2] Average 2024/25 per-pupil funding in England has been estimated to be £7,690, as set out in the Department for Education's School Funding Statistics.

England who started Year 7 between 2010/11 and 2015/16 and were expected to reach Year 11 between 2014/15 and 2019/20 respectively. For each cohort, the number of pupils who moved school during secondary school was considerably higher than the total number of private school pupils expected to move into state schools as a result of this policy. Indeed, around 1 in 6 of the pupils who reached Year 11 in the 2018/19 academic year moved secondary school (107,900 moves by 86,700 pupils).

5.20 The government greatly values the contribution of our diplomatic staff and serving military personnel. The CEA provides clearly defined financial support to ensure that the need for frequent mobility, which often involves an overseas posting, does not interfere with the education of their children. Ahead of the VAT policy coming into effect on 1 January, the Ministry of Defence (MoD) and the Foreign, Commonwealth and Development Office (FCDO) will increase the funding allocated to the CEA to account for the impact of any private school fee increases on the proportion of fees covered by the CEA in line with how the allowance normally operates. The MoD and FCDO will set out further details shortly.

5.21 Turning to business rates, of the approximately 2,440 private schools in England, around 1,140 are charities. As set out above, the business rates system already provides an exemption for certain properties being used for the disabled. As is also set out above, the government will legislate such that schools providing "wholly or mainly" for pupils with an EHCP will retain their relief. Taken together, the government expects that around 1,040 private schools will lose their charitable rate relief.

5.22 The government expects many schools will absorb a significant portion of their new VAT liability through various means. Assuming, therefore, that 100 per cent of the business rates bill increases will be passed through to school fees, the average increase in business rates per pupil is estimated to be 1.3% of forecast average English private school fees in 2025/26. In practice, the impact of this change will vary depending on the size of school, the fees they charge, and the region in which they operate.

Chapter 6

Other Comments

6.1 The majority of respondents made general comments on the VAT policy and its implementation that went beyond the scope of the questions posed in the technical consultation. This chapter summarises the main points raised by respondents.

6.2 Many respondents **supported the overall aims of the policies**. A small number of respondents also **supported the policies themselves**, with some respondents arguing that private schools are businesses and should not, therefore, receive preferential tax treatment.

6.3 A number of respondents raised concerns, however, **over the time between the policy's announcement and its introduction, and the negative impact this could have on the wellbeing of headteachers and school governors.** In particular, respondents highlighted concerns about private schools not having enough time to register for VAT, and having insufficient time to update accounting systems. Schools, their representative bodies, and tax specialists also highlighted uncertainty around a number of areas concerning how schools should charge and recover VAT. These included but were not limited to: single and multiple supply rules, what constitutes closely related goods and services, rules around charging VAT on bursaries and recovering VAT on goods and services used to deliver education to bursary recipients, input VAT recovery (including use of the Capital Goods Scheme), partial exemption calculations, and the VAT treatment of services provided by self-employed teachers. One area of particular uncertainty was the VAT treatment of school meals, and whether this would vary depending on whether a pupil was a boarder or a day pupil.

6.4 Respondents also noted that **schools were likely to have already set their fees for the next academic year** at the time this policy was announced, and noted that there was insufficient time to make adjustments to budgets and find cost savings. It was suggested that this could lead to more of the VAT cost being passed on in the form of higher fees.

6.5 Some respondents also queried **the legality of the VAT policy**; in particular, its compatibility with Human Rights law, the Equality Act 2010, the Children and Young Person's Act 2008, and the UK's obligations under the United Nations Convention on the Rights of the Child.

6.6 Furthermore, a number of respondents suggested that this VAT policy was **out of step with broader VAT policy**. For instance, some respondents questioned why nurseries and university education were retaining their VAT exemption, and suggested that only charging VAT on education provided by private schools constituted age discrimination. Other respondents questioned why VAT was being applied to private school fees when other goods and services consumed by children (such as books and children's clothing) are zero-rated for VAT purposes.

6.7 Many respondents also argued that it was unfair for **the income of parents who send their children to private school to be subject to personal taxes, and for parents to also have to pay VAT on their child's school fees.** Respondents argued this was particularly unfair given that these parents were not making use of the state education sector, which their taxes were contributing to.

6.8 Some respondents raised concerns that those parents who had **pre-paid fees** for terms starting in January 2025 onwards ahead of the date this policy was formally announced on 29 July would avoid paying VAT on those fees, whilst those parents who paid later would have to pay VAT on fees for the same terms.

Government Response

6.9 The government welcomes the support it has received for these policies and believes it is right that they come in as soon as possible to raise the funding needed to deliver education priorities. Indeed, as a result of coming into effect in January, **the VAT policy is forecast to raise £460 million in 2024/25**. As set out at the end of July, the Chancellor of the Exchequer has pledged to restore economic stability after revealing £22 billion of unfunded pressures in 2024/25 inherited from the previous Government. Restoring fiscal responsibility and economic stability are critical to getting our economy growing.

6.10 A **start date** of January 2025 gives schools and parents 5 months to prepare from the date of the announcement. Exactly when individual schools will need to register for VAT and submit their first VAT return will be influenced by when they exceed the VAT threshold, whether they exceed it via the future or historic test, and which stagger group they are in once they are registered.[3]

6.11 Nevertheless, the government recognises that, for many schools, this will be the first time they have needed to register for VAT. The government is committed to supporting these schools to ensure that the VAT registration process is as smooth as possible for them, and to ensuring they have the necessary support in order to be able to correctly charge VAT and remit it to HMRC. That is why HMRC has put

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[3] Once VAT-registered, a business will be assigned a "VAT stagger group", which determines when they need to submit VAT returns and make payments to HMRC.

in place additional resource to process VAT registrations and, on 10 October, published bespoke guidance for schools, which can be found online here: Registering for VAT and Charging & Reclaiming VAT. HMRC published initial guidance ahead of the Budget to maximise the amount of time schools had to prepare for this policy taking effect. This guidance will be updated shortly to reflect the final policy design. HMRC is also holding support sessions for schools, and is available to answer any queries that schools may have. HMRC can be contacted by schools, their representative bodies, and tax advisors via the following email address in the event of any technical queries about registering for, charging, and remitting VAT: vatonprivateschoolfees@hmrc.gov.uk.

6.12 The **VAT treatment of school meals** will be dictated by normal single and multiple supply rules. In Schedule 9 of the VAT Act, there is an exemption for education provided by an eligible body and a separate exemption for goods and services closely related to that education. The exemption for closely related goods and services is being retained, including for private schools. This means that, when private schools sell school meals as a separate supply to the education (i.e. they are itemised separately on invoices and parents have a choice as to whether or not they purchase them), they will remain exempt from VAT.

6.13 However, a general principle of VAT is that when a bundle of goods and/or services are supplied as a single supply, a single rate of VAT is charged, even if different rates of VAT would apply to each of the components when supplied separately. The VAT rate for the whole supply is determined by the predominant element of the supply. This is an important principle that runs throughout the whole VAT system to prevent the need for businesses to artificially separate out single supplies, which would be disproportionately burdensome, and would also be very complex, as it will not always be clear where the boundaries lie between the different goods and services within a package. This means that, where private schools sell meals as part of a single supply, the predominant element of which is education or boarding, the whole supply (including the meals) will be subject to 20 per cent VAT.

6.14 When developing this policy, the government has carefully considered its interactions with existing legislation, and is **confident that the policy is consistent with all of the UK's human rights obligations, the Equality Act 2010, the Children and Young Person's Act 2008, and the UK's obligations under the United Nations Convention on the Rights of the Child.**

6.15 In relation to **age discrimination**, the government's view is that universities should retain their VAT exemption in recognition of the fact that, unlike with schooling, there is no fully state-funded university education. Keeping university education exempt from VAT ensures that it remains accessible to a wide range of people, thereby supporting the government's aim to increase labour market activity. Similarly, not all parents are entitled to free full-time nursery provision. Therefore, keeping nursery provision exempt from VAT helps keep it affordable for parents, thereby supporting them in returning to work after having children.

6.16 When thinking about the VAT treatment of **other goods and services used by children**, it is worth noting that there is not, and has never been, equivalent treatment between VAT on education (which is exempt, meaning suppliers do not charge VAT but cannot reclaim input VAT) and VAT on books and children's clothes (which are zero-rated, meaning suppliers can reclaim input VAT). Some of these items (such as books) are not exclusively consumed by children. And it is also not the case that all goods consumed by children are either exempt or zero-rated for VAT purposes. The government does not accept that there should be equivalent VAT treatments for all goods consumed by children.

6.17 Finally, VAT is a broad-based tax on consumption and the 20 per cent standard rate applies to most goods and services. Parents of pupils at private schools will therefore pay VAT on a range of goods and services with income on which they also pay personal taxes. Moreover, as a general rule, UK taxes are not formally hypothecated, meaning all tax revenue is pooled together and used to fund vital public services, not all of which individual taxpayers will necessarily use directly.

6.18 As set out in the technical note, **the government will legislate in the Finance Bill with retrospective effect to provide that fees paid from 29 July 2024 pertaining to the term starting in January 2025 onwards to be subject to VAT**. This will protect Exchequer revenue by allowing HMRC to collect VAT incurred on fees paid in the period between the date this policy was announced and the Finance Bill receiving Royal Assent. It will also help to ensure parity of treatment between parents and carers who may otherwise seek to pay multiple years' worth of fees upfront in the period between this policy being announced and it taking effect, and those parents and carers for whom that is not a viable option. The government judges the date this policy was formally announced to be a fair point from which to subject fees to VAT, given that it is on this date that the details of this policy change were made clear to taxpayers, and draft legislation was published.

6.19 The government is aware that, whilst many schools have always offered schemes enabling pre-payment of fees, there were reports of increased numbers of parents utilising such schemes ahead of this policy being formally announced in July, in an attempt to avoid these fees being subject to VAT. In many cases, the structure of these schemes means that the tax point – which governs the tax treatment – has not yet been passed. For instance, if the scheme involved paying a lump sum to the school in advance, but the details of the supplies that the money was buying were not determined at the time it was paid (i.e. if the money paid did not relate to specific terms' fees that had already been set), the tax point is unlikely to have passed. HMRC stands ready to challenge the validity of such payments and will seek to collect VAT on those fees where it is due. Indeed, the government is committed to tackling tax avoidance, and, in line with the principle to ensure that the policies are fair and that all users of private schools pay their fair share, HMRC will be carefully scrutinising the detail of pre-payment schemes to ensure that schools pay the correct VAT where it is due.

6.20 No concerns were raised about the way the anti-forestalling provisions were drafted in the draft legislation. The power to amend the anti-forestalling provisions outlined at 2(3) in the draft legislation will therefore be removed from the final clauses.

Chapter 7

Next Steps

7.1 The government would like to reiterate its thanks to those who contributed to this consultation process. To summarise, the following amendments will be made to the draft VAT legislation that was published in July. HMRC guidance will be updated to reflect these changes shortly:

- **HE** taught at schools that are otherwise in scope of the policy (for instance, performing arts schools) will be carved out of the VAT policy.
- To ensure that education provided by **FE colleges** remains exempt from VAT, the second limb of the definition of a private school has been amended so that only institutions that are wholly or mainly concerned with providing education suitable for 16-19 year olds, and where the majority of 16-19 year old pupils are charged fees are within scope of this policy.
- **ITPs and ILPs** will be carved out of the legislation. ITPs and ILPs are defined as "an institution at which education or training suitable to the requirements of persons over compulsory school age (or, in Scotland, school age) but under 19, and where the consideration for [that provision] is payable by the relevant contracting authority under that contract". A relevant contracting authority means the Secretary of State, Medr (Commission for Tertiary Education and Research), the Department for the Economy in Northern Ireland, or Skills Development Scotland.
- The definition of a **nursery class** will be changed to "a class composed wholly (or almost wholly) of children under compulsory school age (or, in Scotland, school age) and who would not be expected to attain that age while in that class".
- **TEFL courses** taught by private schools, or connected persons, will be carved out of the policy.
- The **connected persons test** set out at Note (2)(a) in the draft legislation will be removed. The other two connected persons tests will remain in the final legislation.
- **NMSS** will be brought within scope of this policy, but will only be required to charge VAT on placements paid from 30 October pertaining to terms starting in January 2025 onwards.

- The **power to amend the anti-forestalling provisions** outlined at 2(3) in the draft legislation will be removed.

7.2 The VAT policy change will be legislated for in the Finance Bill and will take effect from 1 January 2025. This Finance Bill measure will make an amendment to the Value Added Tax Act 1994.

7.3 Schools within scope of this policy can now register for VAT. They can register online here: HMRC Guidance: Register for VAT. Bespoke guidance for schools can be found online here: Registering for VAT and Charging & Reclaiming VAT. Should schools, their representative bodies, and tax advisors have any technical queries around this policy, they can contact HMRC via: vatonprivateschoolfees@hmrc.gov.uk.

7.4 The business rates policy change will be legislated for through a Local Government Finance Bill led by the MHCLG and will take effect from April 2025, subject to Parliamentary process. The Bill will make an amendment to the Local Government Finance Act 1988.

Annex: VAT Costing Methodology

Introduction

This annex sets out detailed information on the assumptions, methodology and calculations underlying the costing of the Exchequer impact of the VAT measure, including relevant adjustments for behavioural effects. The estimation of pupil movements resulting from the policy is also set out. The final section highlights main areas of uncertainty and sensitivity analysis to the key assumptions.

The costing has been scrutinised by the independent OBR and has been certified by them.

The Tax Base

Fee income is estimated by multiplying numbers of pupils at private schools by average fees per pupil.

Pupil numbers are taken from the Department for Education's school census and Devolved Governments' data. Average fees for member schools of the ISC are taken from the ISC's 2024 Census, and for other schools, are estimated using data from sampling. Adjustments are made to allow for fee assistance provided by schools. The tax base is projected over the forecast period by applying forecast growth in average earnings plus an uplift of 1 per cent per year, this being based on observed average growth in fees since 2010. An adjustment is made for the entitlement of LAs to VAT refunds. The resulting tax base is £11,500 million for the 2024/25 financial year, rising to £13,600 million in 2029/20.

Static Costing

Additional output VAT is calculated at 20 per cent of the tax base above.

The VAT liability will be reduced by input VAT on purchases. Non-staff costs are estimated to be around 30 per cent of fee income on average, based on analysis published by the ISC. The average VAT rate on non-staff costs is estimated to be 14 per cent, based on HMRC data on comparable sectors of the economy. The resulting estimate of input VAT on current purchases is £470 million in 2024/25, rising to £560 million in 2029/30. An allowance is then made for the effect of the Capital Goods Scheme, which adjusts input tax recovery on certain (mainly property) assets acquired over the previous 10 years over the remainder of the 10-year period since their acquisition, aligning it with the business's current input tax recovery status. This adds £60 million to input tax recovery in the first year, reducing to around £30 million by 2029/30.

The static yield is calculated by subtracting the input tax from the output tax, and time apportioning the resulting liability in 2024/25 for the implementation date of 1 January 2025.

The resulting estimated tax liability is 15.5 per cent of the tax base on average over the forecast period.

A reduction in projected revenue is made to allow for the tax gap (the difference between theoretical tax liabilities and actual tax receipts due to non-compliance) at a rate moderately below the overall average VAT tax gap (approximately 4 per cent).

Behavioural Effects

Passthrough

It is predicted that schools will absorb some of the VAT liabilities through surpluses or reserves, and some through cost efficiencies that do not affect quality of service and hence have no impact on demand; the assumed proportions are 1 per cent and 10 per cent respectively. Of the remaining 89 per cent of the VAT liability, it is assumed that, on average, one-quarter will be absorbed from cost reductions that do affect service provision, and hence may affect demand, while the remaining three-quarters will be passed on as fee increases. Thus, the central case expectation of fee increases is just over 10 per cent (15.5 per cent x 89 per cent x 75 per cent). It is expected that there will be considerable variation around this average in practice.

Demand

An elasticity of demand with respect to quality-adjusted price of -0.5 is assumed, which is applied to both the reduction in service provision and the fee increase as estimated above. In arriving at this estimate of the responsiveness of demand, the government has reviewed a wide range of evidence, including a report by the IFS in 2023, survey research by the ISC, and international academic studies. The chosen elasticity of -0.5 is towards the most responsive end of the range estimated by the IFS (allowing for slight differences in the methodology in how the elasticity is applied). The use of the high end of the IFS's range balances the estimate with the other evidence, some of which suggests that demand may be more responsive.

The expected demand reduction is therefore around 7 per cent (15.5 per cent x 89 per cent x -0.5).

Substitution to Other Expenditure

The costing further assumes that 50 per cent of expenditure displaced to or from spending on school fees, from fee increases or departures from private schools, will be displaced from or to other standard rated expenditure. This is line with the overall proportion of consumer expenditure that is standard rated. For this group of consumers, it is expected that the proportion of standard rated expenditure is likely to be higher than average, but against this, some displaced expenditure will offset savings, which are outside the scope of VAT, so that 50 per cent remains a reasonable assumption.

Phasing

The demand response discussed above is the effect expected in the steady state after a period of a number of years. The timing of the demand response is expected to differ between parents whose children are already at private schools and those who have yet to send their children to private schools who would replace current pupils through natural turnover. Among the first group, the demand response is phased over the forecast period by assuming a greater likelihood of movement after key course completions such as GCSEs or Independent Schools Examination Board Common Entrance. The second group is phased using data on school joiners. Around 10 per cent of the total demand response is projected to occur in 2024/25, and cumulatively about 80 per cent by 2029/30.

Exchequer Impact

	2024/25	2025/26	2026/27	2027/28	2028/29	2029/30
Exchequer impact (£mns)	+460	+1,505	+1,560	+1,610	+1,665	+1,725

Pupil Movement Impacts

It is assumed that 10 per cent of the demand reduction in response to higher fees (by value, not number of pupils) will occur through substitution to other private schools with lower fees, rather than through substitution to state schools. The reduction in the number of pupils in private schools resulting from the policy can then be derived from the costing by multiplying the demand reduction of 7 per cent by the affected pupil population and applying the 10 per cent factor to the 75 per cent of the demand reduction that occurs in response to higher fees, rather than service reductions. There are estimated to be 567,000 pupils currently at private schools in the UK, excluding those funded by LAs (for which no demand effect is expected). The expected steady-state reduction in private sector pupil numbers is therefore 37,000 (567,000 x 7 per cent x (100 per cent – 10 per cent x 75 per cent)).

In some cases, such as where parents are overseas, pupils leaving private schools in response to the measure may not join UK state schools. To project the increase in state school numbers, the proportion with overseas parents (around 5.5 per cent) are excluded. This gives a steady-state increase in the number of state school pupils resulting from the VAT policy of 35,000.

Applying the phasing discussed above, the projected increase in the cumulative number of state school pupils in the UK by school year is as follows:

	2024/25	**2025/26**	**2026/27**	**2027/28**	**2028/29**	**2029/30**	**Long-term**
Number of pupils	3,000	14,000	20,000	24,000	27,000	29,000	35,000

Areas of Uncertainty

The costing is relatively insensitive to the demand elasticity. Changing the -0.5 elasticity assumption to -0.25 or -0.75 would change the yield by £10 million in 2025/26 and £30 million in 2029/30. The costing is also relatively insensitive to other assumptions in the costing.

The pupil displacement impacts are proportional to the demand elasticity. Changing the -0.5 elasticity assumption to -0.25 or -0.75 would change the steady state number of pupils in state schools by 17,000.

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This document can be downloaded from www.gov.uk

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