

GUIDANCE ON THE TAX TREATMENT OF NON-CORE HEALTH CARE COMMERCIAL ACTIVITIES OF NHS FOUNDATION TRUSTS

Contents

1. INTRODUCTION

- Scope of guidance

2. BACKGROUND

3. KEY PRINCIPLES

4. TRADING BY NHS FOUNDATION TRUSTS

- Introduction
- What is a trade?
- Provision of goods and services for the principal purpose of healthcare
- Private Healthcare
- Non-core healthcare trading

5. TAX TREATMENT OF COMMERCIAL ACTIVITIES

- Treasury power to tax commercial activities
- What activities are taxable?
- Exploitation of IP

6. SIGNIFICANT TRADING ACTIVITIES

- What is a “significant” trading activity?
- De-minimis limit for “insignificant” trading activities

7. TRADING ABOVE SIGNIFICANT LIMITS

- What if profits from the activity are likely to exceed the de-minimis limit?
- What if significant trading activities are not placed in a company?
- Reasonable expectation test

8. CALCULATING THE PROFITS OF A TRADE

- Introduction
- Allocation of indirect overheads

9. FURTHER ACTIONS

10. OTHER GUIDANCE AVAILABLE

1. INTRODUCTION

Scope of the guidance

1.1 The purpose of this guidance is to provide assistance to NHS Foundation Trusts, created under the *Health and Social Care (Community Health and Standards) Act 2003* (the "HSCA"), on the tax treatment of any commercial activity ancillary to their principal purpose of providing goods and services for the purposes of the health service in England.

1.2 This guidance does not constitute legal advice or provide a comprehensive view of the law.

2. BACKGROUND

2.1 The Government maintains a consistent policy line that all commercial activities should be subject to taxation. This policy aims to prevent any unfair competition issues and therefore ensure a level playing field exists between public bodies and the private sector. NHS Trusts are currently subject to this requirement, subject to direction by the Secretary of State for Health.

2.2 To ensure that this policy approach is maintained in relation to the commercial non-core health care activities of Foundation Trusts, the Government introduced legislation in section 148 of the Finance Act 2004. This legislation amended section 519A Income and Corporation Taxes Act 1988 (ICTA 1988) to provide a power for the Treasury to make such commercial activities taxable.

2.3 The Financial Year 2005 is the first year for Foundation Trusts which will be subject to the tax regime described in this guidance.

3. KEY PRINCIPLES

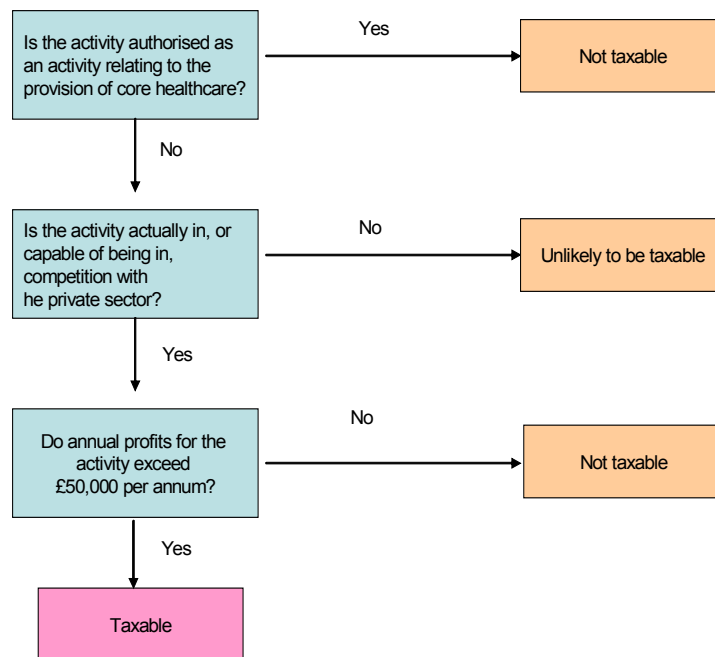
3.1 Health service bodies, including Foundation Trusts, are exempt from tax on their principal health care income under section 519A ICTA 1988. In determining whether or not an activity is likely to be taxable, a three-stage test may be employed:

- *Is the activity an authorised activity related to the provision of core healthcare?* The provision of goods and services for purposes relating to the provision of healthcare authorised under Section 14(1) of the HSCA is not treated as a commercial activity and is therefore tax exempt. It is expected that private healthcare is generally likely to fall within section 14(1) and is not therefore taxable.
- *Is the activity actually or potentially in competition with the private sector?* Activities of a commercial nature and activities in competition with the private sector may potentially be subject to corporation tax. It is expected that trading activities undertaken in house by many NHS organisations which are clearly ancillary to their core healthcare objectives and are not entrepreneurial in nature will not be subject to tax, e.g. staff canteens, or **patient and hospital visitor** car parking. A trading activity that *is* capable of being in

competition with the wider private sector will be subject to tax. For example, the exploitation of intellectual property, or a commercial laundry are likely to be taxable since they represent the pursuit of business opportunities that extend beyond the physical or virtual confines of the hospital and its core healthcare activities.

- *Are the annual profits significant?* Only significant trading activity may be taxed. “Significant” for these purposes is defined as annual taxable profits in excess of £50,000 per trading activity.

The three-stage test can be summarised in the decision tree below:



3.2 It is essential that, if any doubt exists regarding the treatment of particular activities, that Finance Directors of Foundation Trusts should seek advice from HM Revenue & Customs, setting out the facts of each case.

4. TRADING BY NHS FOUNDATION TRUSTS

Introduction

4.1 In carrying on their principal purpose of providing goods and services for the purposes of the health service in England, Foundation Trusts are regarded as providing a public service. They are not carrying on a trade in a commercial sense, i.e. with a view to making profits. However, any activity of a commercial nature, carried on by a Foundation Trust to provide additional income to perform core healthcare functions better, may amount to a commercial activity and, if potentially in competition with private sector businesses, could therefore be taxable. The aim of the following sections is to explain what activities of Foundation Trusts might amount to non-core healthcare trading activities and how HM Revenue and Customs treats trading profits from these activities for tax purposes.

What is a trade?

4.2 Normally, a trade involves the sale of goods or services to customers as part of a commercial enterprise. A one-off or occasional venture may be treated as a trade for tax purposes if it involves the sale of goods or the provision of services for profit.

Provision of goods and services for the principal purpose of healthcare

4.3 The provision of goods and services for purposes relating to the provision of healthcare is authorised by Monitor under Section 14(1) of the *HSCA*. Such authorised activities are not treated as a commercial activity for the purposes of the Treasury power to make certain commercial activities taxable. Therefore, any activity, which might otherwise amount to a trade, authorised under this section will be treated as tax exempt.

Private Healthcare

4.4 The extent to which a Foundation Trust can carry on private patient work will be set out in the terms of its Authorisation to ensure that the Foundation Trust continues to focus on NHS work. Authorised private healthcare services are generally likely to fall within Section 14(1) of the *HSCA* as goods and services related to the provision of healthcare and are not therefore taxable.

Non-core healthcare trading

4.5 Under Section 14(3) of *HSCA*, Foundation Trusts are empowered to carry on other activities, subject to any restrictions specified by Monitor in their Authorisation, for the purpose of making additional income in order to carry on their principal purpose better. HM Revenue and Customs will generally treat such activities as being of a commercial nature. Where potentially in competition with the private sector, these activities are likely to be taxable if the profits arising from the activity are 'significant' (see Section 6.1 below).

5. TAX TREATMENT OF COMMERCIAL ACTIVITIES

Treasury power to tax commercial activities

5.1 NHS Foundation Trusts fall within the definition of a “company” for tax purposes. Without specific tax exemption on their income, they are within the scope of corporation tax. Section 33 of the *HSCA* paved the way for this exemption by amending the general tax exemption for health service bodies, in the Taxes Acts to include NHS Foundation Trusts as a defined health service body covered by section 519A ICTA1988.

5.2 NHS Trusts may be directed by the Secretary of State to adhere to Government policy regarding the taxation of commercial activities. However, the greater financial and operational freedoms enjoyed by NHS Foundations Trusts provide scope for activities of a commercial nature to be carried on without the strict central Government controls placed on other NHS organisations. These may be substantially different in scale and scope to those non-healthcare activities currently undertaken by NHS Trusts.

5.3 Where NHS Foundation Trusts are carrying on activities of a commercial nature, and those activities are potentially in competition with the private sector, the Government is committed to maintaining its level playing field policy towards the tax treatment of such activities. The Government therefore introduced legislation in the 2004 Finance Act to ensure that significant commercial non-core health care activities of NHS Foundation Trusts are taxable. The legislation provides the Treasury with a power to disapply the general tax exemption at Section 519A ICTA 1988 and make an order to determine the amount of profits of any commercial activity that appears to be in competition with the private sector that are charged to corporation tax.

What activities are taxable?

5.4 As a rough guide, any activities falling within Section 14(3) of the *HSCA* will have the **potential** to be taxable. The examples quoted below are not intended to be exhaustive or prescriptive and guidance from HM Revenue & Customs should be sought where a Foundation Trust is in any doubt. Whether or not a Treasury Order will be necessary to determine the profits to be brought into the charge to corporation tax will depend on a number of factors, including:

- Whether the activities are above and beyond those ancillary to core healthcare provision. An indication that an income generating activity is unlikely to be taxable is if it is focused inwardly on the delivery of services to patients, staff and visitors on the Trust’s premises;
- Whether the activities are capable of being in competition with private sector businesses. These income-generating activities will, for the most part, be externally focused in terms of where and with whom services will be delivered. For example: a laundry, selling services to other organisations; a laser clinic; or the sale of consultancy services;
- Whether the activities are carried on within the Foundation Trust itself or whether they are placed in a separate company, wholly or partly owned by the NHS Foundation Trust.

- The level of profits from the activity (see Section 6.1 below).

5.5 Any activity authorised by the Monitor under Section 14(1) of the HSCA as goods and services relating to the provision of healthcare will not be treated as a commercial activity for tax purposes and will therefore remain tax exempt.

Exploitation of IP

5.6 The NHS is allowed to develop as an innovative organisation and create income generation by exploiting its intellectual property rights (IPRs). There are a number of ways the NHS can exploit its IPRs, for example by issuing licences or transferring the IP to spin out companies. These are covered in the Department of Health's *The NHS as an Innovative Organisation – A Framework and Guidance on the Management of Intellectual Property in the NHS*.

5.7 The exploitation of IP by NHS Foundation Trusts is an activity for the purpose of making additional income available in order to carry on its principal purpose better. As such, any income or gains from the exploitation of IPR may be taxable if the resulting income arises from a commercial activity potentially in competition with the private sector.

6. “SIGNIFICANT” TRADING ACTIVITIES

What is a “significant” trading activity?

6.1 A non-core health care commercial trading activity carried on by a Foundation Trust will be treated as being “significant” for tax purposes if the annual profits of the activity exceed £50,000. Accordingly, if it is clear that the activity is significant (or is likely to become significant) it will be necessary for Foundation Trusts to identify the income and expenditure relating to the activity. This might, for example, be achieved through the application of controls and procedures within an existing accounting system, or through the operation of a separate accounting system more suitable for the preparation of commercial financial information and the computation of taxable profits. In any doubt or difficulty as to whether a trading activity is significant, Finance Directors of Foundation Trusts should seek advice from their HM Revenue and Customs office.

De-minimis limit for “insignificant” trading activities

6.2 Where the annual profits of a particular non-core health care activity are £50,000 or less the Treasury would not seek to make an order to tax the activity. The application of this de-minimis limit is a de-regulatory measure in place to ensure that relatively small transaction streams, which might in themselves constitute a trading activity, are not brought into the scope of tax, thereby preventing unnecessary administrative burdens. The intention of this provision is that the small-scale commercial activities undertaken in-house by many NHS Trusts should not become subject to corporation tax simply as a result of their transition to Foundation status.

7. TRADING ABOVE SIGNIFICANT LIMITS

What if profits from the activity are likely to exceed the de-minimis limit?

7.1 Where it is clear that the profits of a particular activity are likely to exceed the £50,000 de-minimis limit they will be taxable if the activity is a commercial one (i.e. they fall within Section 14(3) of the HSCA) and potentially in competition with the private sector.

7.2 If a Foundation Trust considers that this provision applies to a particular activity, they should think about placing that activity in a separate wholly or partly owned company. Normal corporation tax rules will then apply to the taxable profits generated, whether or not they actually breach the £50,000 de-minimis limit.

7.3 Finance Directors of Foundation Trusts requiring advice on setting up a company to carry on commercial non-core healthcare activities should consult professional advisers. They may also contact their HM Revenue and Customs office for advice on the corporation tax issues associated with setting up such a company.

What if significant trading activities are not placed in a company?

7.4 Where an activity falling within Section 14(3) of the HSCA with significant profits is being carried on by a Foundation Trust but not through a separate company, the Foundation Trust should notify HM Revenue and Customs when it first becomes aware that trading is likely to be significant.

7.5 HM Revenue and Customs, upon notification or discovery that a particular activity being carried on by a Foundation Trust should be taxable may seek a Treasury Order to determine the amount of the profits subject to corporation tax. Finance Directors should be aware that failure to notify HM Revenue and Customs of potentially taxable activities could result in the Trust becoming liable to interest and, exceptionally, penalties.

7.6 If a Foundation Trust is unsure about whether a particular activity, which is not carried on within a company, falls outside Section 14(1) of the HSCA (and is therefore potentially taxable) they should seek advice from their financial adviser.

Reasonable expectation test

7.7 It may be the case that the profits of a particular non-core health care activity were anticipated to be within the £50,000 de-minimis limit but unexpectedly exceeded the limit. Where this is the case, HM Revenue and Customs may not seek a Treasury Order to tax the resulting profits providing the Foundation Trust can show that, at the start of the accounting period in question, it was reasonable for it to expect that the profit would not exceed the limit.

7.8 HM Revenue and Customs will consider any evidence the Foundation Trust may have to satisfy the reasonable expectation test.

7.9 For example, it may be the case that the Foundation Trust had carried on the activity for a number of years and might be able to show that the turnover increased unexpectedly

compared with earlier years. Alternatively, the Foundation Trust might have started carrying out the activity in the year in question and might be able to show that the profit was higher than it forecast when it decided to start the activity.

7.10 The type of evidence needed to demonstrate the levels of turnover and income which were expected might include minutes of meetings at which such matters were discussed, copies of cash flow forecasts, business plans and the previous years' accounts.

7.11 If the Foundation Trust expects to be regularly trading at or around the £50,000 limit, it would be advisable to use a trading subsidiary (see [Section 6](#)).

8. CALCULATING THE PROFITS OF A TRADE

Introduction

8.1 The profits of non-core health care activities carried on by Foundation Trusts, including capital allowances if applicable, should be calculated in the same way as for any other trader. However, there are some factors that may be particularly relevant when calculating the profits of a trade carried on by a Foundation Trust.

Allocation of Indirect Overheads

8.2 As well as deducting direct expenditure of the trade when calculating the profits, the Foundation Trust should deduct indirect expenditure that it has incurred and which is attributable to the trade. For example, if the trade is carried on in the Trust's premises it will normally be proper to allocate to the trade part of the costs of the premises such as:

- heat and light
- rent
- building repairs and maintenance.

8.3 Apart from the use of premises, other indirect overheads that may be partly attributable to the trade are:

- employee salaries
- computer costs
- telephone charges
- postage costs
- accountancy and legal fees
- general administration.

8.4 The proper basis of apportionment of indirect costs will depend on the facts. In the case of the use of premises, the apportionment might be based on the size of floor space allocated to the trade. In the case of employee salaries, the apportionment might be based on the amount of employee time devoted to the trade compared to total employee time.

9. FURTHER ACTIONS

9.1 The guidance contained in this note is indicative. The tax status of particular trading activities is determined on the facts of each case and may require specialist judgement to be exercised.

9.2 In the event that a Foundation Trust considers that existing or proposed activities are likely to be subject to corporation tax, further guidance may be sought from HM Revenue and Customs. Foundation Trusts should contact their HM Revenue & Customs office direct.

10. OTHER GUIDANCE AVAILABLE

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