

FINANCE ACT 2012

EXPLANATORY NOTES

INTRODUCTION

Section 198: Supply of Goods Or Services by Public Bodies

Summary

1. [Section 198](#) implements Article 13(1) of the Principal VAT Directive ([2006/112/EC](#)) ("the PVD") by inserting a new section, 41A, into the Value Added Tax Act 1994 (VATA).
2. It applies to Government departments, local authorities and analogous public bodies who supply goods and services when acting within a legal framework, such as a statute, which applies only to them and not to private individuals.
3. Such bodies are not to be treated as taxable persons unless their exemption would lead to distortion of competition.
4. The exemption does not however apply to their engagement in activities described in Annex 1 of the PVD ("Annex 1") unless those activities are carried out on such a small scale as to be negligible.

Details of the Section

5. Subsection (2) amends section 41 VATA ("section 41"). Section 41 applies VATA to the Crown. Section 42(2) provides for the taxation of goods and services supplied by Government departments in certain circumstances where such supplies are not taxed under general VATA provisions. Sub section (2) deletes section 41(2) and makes a consequential amendment to section 41(3)(b) so that reference is made to the new section 41A of VATA which will determine when supplies by Government departments are taxed.
6. Subsection (3) inserts a new section 41A which provides as follows:
 - New section 41A(1) provides that the section will apply to supplies of goods and services made by a public body (being a body within the ambit of Article 13(1) PVD) which is acting in its capacity as a public authority;
 - New section 41A(2) provides that (where the new section 41 applies) a supply in respect of an activity listed in Annex 1 of the PVD is to be treated as a supply in the course or furtherance of business (and therefore taxable in accordance with section 4 of VATA) unless the activity is on such a small scale as to be negligible;
 - New section 41A(3) provides that (where the new section 41 applies) a supply which is not in respect of an Annex 1 activity is only to be treated as a supply in the course or furtherance of a business if relieving it from VAT would lead to a significant distortion of competition

Background Note

7. [Article 13\(1\)](#) provides that public bodies (Government departments, local authorities and analogous institutions) should not be taxed when making supplies of goods and services unless those supplies arise out of Annex 1 activities (which are not negligible) or relief from VAT would cause significant distortions of competition.
8. There is no explicit transposition of Article 13(1) into UK legislation. HMRC has given effect to the Article by interpreting existing legislation in a way that achieves the correct result for the Article's purposes. However recent litigation has cast significant doubt on whether this approach amounts to an effective implementation of Article 13(1).
9. This provision puts the effective implementation of the article beyond doubt and therefore precludes the possibility of infraction proceedings being taken against the UK. In practice public bodies should see no change to their existing tax treatment as a result of the legislative changes. It also provides a clear legislative base for applying the appropriate test to determine whether a particular supply is taxable in an environment where public and private sector provision is constantly evolving.