

VAT recovery on cars and other assets (Lecture B1445 – 15.27 minutes)

Input tax recovery is normally very simple. If the input tax properly incurred relates wholly to taxable activity it is recoverable unless it relates to:

- cars for private use;
- customer entertaining;
- building materials not ordinarily incorporated.

If you have exempt income then it gets trickier in that you must ascertain whether the input tax incurred is directly taxable, directly exempt or residual.

Charities have the added complication of non-business activity and they will be very aware that they have no input tax deduction for their non-business activity.

Attribution of input tax is key for partially exempt businesses and charities.

Cars available for private use

Cars that are available for private use when purchased are blocked from input tax recovery. Some garages are telling customers that electric cars do not fall within the blocking order – this is incorrect as input tax will be blocked if electric cars are available for private use.

Pool cars would be outside of the blocking provisions providing you have evidence that the pool cars are not available for private use.

Other assets available for private use

Sole trader/Partnerships

When sole traders or partnerships incur VAT on a business cost they will recover the VAT incurred if they are a fully taxable business. Where that cost has an element of private use they have two choices:

1. Deduct the business proportion only;
2. Deduct input VAT on the full cost and account for output tax on private use in each quarter (Lennartz).

If for example a sole trader bought a £3,000 plus VAT laptop through his business it looks like it is fully deductible. On closer examination the laptop has significant gaming attributes and will be used 40% for private purposes. The sole trader could recover £360 (£600 x 60%) in the quarter of purchase and have no further input tax restrictions. Alternatively, he could recover £600 and account for private use each quarter. If the 40% is a reasonable estimate of the private use this could equate to £12 per quarter over the next five years. In reality the output tax calculation is more involved as you need to look at the actual private use in each quarter – probably easier just to recover £360 in quarter of purchase and be done.

It should also be noted that if he were to sell the laptop at any stage he will only have to account for VAT on 60% of the net proceeds (assuming he recovered 60% VAT when purchasing the laptop).

It should be noted that Lennartz cannot be used for property, ships and aircraft so option 1 would be the only option for those assets.

Corporates

Corporates have the same options as above but option 2 tends to be used more.

For example, a new car dealer would recover VAT in full on cars purchased new and for resale. Some of these new cars would be used as demonstrators (demo cars) for test drives etc. These demo cars are normally available for staff to take home in the evenings and at the weekend.

HMRC and the Retail Motor Industry Federation have agreed a simplified method by which the motor dealers may calculate the VAT due on the private use of demo cars.

If these demo cars are still held as demos after 12 months there will be a self supply charge on the business i.e. output VAT due. Input tax would not be deductible as the cars would no longer be regarded as new and for resale after 12 months.

As a result, new car dealers are very keen to sell their demo stock before the 12 month point so as to avoid the self supply charge.

Commercial vehicles v cars

The normal rules on when to claim VAT back apply to the purchase of any road vehicle other than a car e.g. vans. So the business proportion is deductible on purchase or the taxpayer can adopt Lennartz. Generally HMRC views any incidental private use of most types of commercial vehicle as de minimis and input tax would not be restricted in that case.

The intended use of commercial vehicles that are suitable for private use are more likely to involve private use implications. Commercial vehicles suitable for private use include motor caravans, motorcycles and double cab pick ups. .

It should also be noted that where a business converts a commercial vehicle into a car it will become liable to an output tax charge on a self-supply of the vehicle to itself. And if it is converted into a car available for private use the self supply output VAT will not be deductible. The purpose of the self supply is to put the taxpayer in the same position as if they had bought a car.

Vehicles are not treated as cars for VAT purposes if they have a payload of one tonne or more. Payload is the difference between a vehicle's maximum gross weight and its kerbside weight. Given the different treatment of cars and commercial vehicles it is important for manufacturers, distributors, dealers and business customers to know the payload of any double cab vehicle they sell or buy. It is especially important to be aware that by adding accessories to the ex-works model they may, by lowering the payload of the vehicle, convert it into a car. This would make the vehicle liable to the self-supply charge. Such conversions are most likely to occur with double cabs that have an ex-works payload of 1000 to 1050 kg.