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VAT TRAP FOR CHARITIES

Introduction

A change in interpretation announced by HM Revenue & Customs (HMRC) in July 2009 will further restrict the ability of charities to obtain the benefit of zero rating where there is some business use of a new building.

Where the change has been overlooked, or a project has been delayed, urgent action is required as there is only three months or so before the previous more generous concessionary treatment is withdrawn. The addition of a VAT charge where none was anticipated, unless it is possible to change or amend the planned use of the building, could result in the entire project being cancelled.

Charities with a mix of business and non-business activities have for many years obtained zero rating for new buildings by relying on the 'charitable building' concession. The concession (ESC3.29) disregards non-qualifying use that is less than 10 per cent of total use when considering whether the intended use of a building meets the legal test of being used 'solely for a relevant charitable purpose' (RCP).

Last year HMRC announced that the concession would be withdrawn from 1 July 2010, after a 12 month transitional period. After that date charities will have to comply with the new HMRC interpretation of the law, requiring that the building concerned is intended to be used 95 per cent or more for 'RCP'.

On the plus side a charity can now use any fair and reasonable method to measure use, rather than one of the four specified in the concession (three of which require permission in any case). Notwithstanding that there is now freedom as to the method of measurement; we believe the reduction from 10 to 5 per cent will make it very difficult for a charity to accommodate any meaningful business activity within the building.

In addition, the 'change of use' charge will again apply, whereas it has not applied since 2007 where the concession has been utilised. The charge applies if the building begins to be used for less than 95 per cent for RCP within a ten year period and is equal to the VAT that was originally saved through zero rating, reduced by 10 per cent for each year of RCP use.

Should a charity be planning to rely on the concession at some point during the remainder of the transitional period and issue a zero rating certificate to the builder, then HMRC will only accept that the certificate is valid if there has been a meaningful start on site of the construction of the building before 30 June 2010, which will continue without interruption to completion; or in the case of the acquisition of a property contracts, have been exchanged before 30 June 2010.



Recent experience indicates that it can take three to four months to obtain a clearance from HMRC charities. Given the inherent uncertainties and ambiguities, any charity and advisers involved with a new construction project where some business use is anticipated, but at the same time it is expected to take advantage of the benefit of zero rating are recommended to review their plans now to mitigate the risk of a potential VAT liability.

For more information see Revenue & Customs Brief 39/2009 and VAT Information Sheet 8/2009.

For further advice concerning any of the issues raised in this briefing, please contact one of our key individuals detailed overpage, or alternatively call our helpline on 0800 526262. Information on other property tax related topics can also be found on our website at <http://bankingtaxfinance.davislangdon.com>.

