

DBULLETIN

Changes to the VAT Zero Rate for Buildings Used for Charitable or Residential Purposes

Supplies involving the acquisition or construction of a new building (or part) intended for use solely for a relevant residential or solely for a relevant charitable purpose are zero rated for VAT provided that the supply is made to a person who both intends to use the building for such a purpose and gives the builder a certificate in a specified form before the works are carried out.

If there is a business use of the premises within a 10 year period from the date of completion of its construction then a change of use a charge arises on the person acquiring the business.

HMRC have announced in their Brief 39/09 that they have changed their interpretation of the meaning of the phrase “solely for a relevant residential purpose or solely for a relevant charitable purpose” in relation to this zero rating. Broadly, HMRC now recognise that the term “solely” as used in those phrases can incorporate a de minimis margin of up to 5%. HMRC will now accept that a building (or part) is used solely for the relevant qualifying use if the use of the building (or part) for the relevant qualifying use is 95% or more. HMRC will accept any method used to calculate the qualifying use of the building (or part) so long as it is fair and reasonable.

This will be welcome news for those involved with projects under which relevant residential use buildings are constructed because to date there has been no de minimis provision at all for these buildings. Thus if accommodation is constructed as residential accommodation for say NHS staff and

this accommodation does not qualify as dwellings, it will usually qualify as a building used solely for a relevant residential purpose and therefore zero rating will apply. However, if it is intended that some of the time some of the units may be used for hotel type uses (for example for accommodation for visitors or patients' families under “patient hotel” type arrangements) then up to now this would have prevented the zero rating of the building. However under the new rules, provided that the non-qualifying use is kept within the 5% de minimis a certificate can be given and zero rating will apply. However, the announced changes will not be so welcome to charities or those involved with projects under which relevant charitable use buildings are constructed. This is because to date there has been an extra statutory concession (ESC) in force in relation to charitable buildings under which HMRC will ignore non-qualifying use of the charitable building (or part) if that use is less than 10% of the total use. However charities using the ESC must comply with the strict provisions of the ESC which measures the 90% charitable use by one of three specific measurements.

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HMRC state that in the light of their change of view, the ESC is no longer necessary and so it is being withdrawn on 1st July 2010. From then on charities can only certify use as being solely for a relevant charitable purpose if they can bring themselves within the 5% de minimis. During a transitional period of 12 months from 1st July 2009 charities have the option of either using the existing ESC in accordance with its terms or the new interpretation of "solely" to determine whether they can take advantage of the zero rate. But the choice must be made and the certificate given before the end of the transitional period. HMRC will not consider a certificate to be valid unless (in the case of a supply of construction services) the works have actually started on site before 30 June 2010 and be expected to progress to completion and (in the case of the acquisition of a building) exchange of contracts has taken place and a deposit paid to the Vendor before 30 June 2010.

All this is likely to result in increased costs for those developing charitable use buildings. Many charitable projects in the course of procurement may run out of time for the option to be exercised and unless such projects can be brought within the new rules, they will not qualify for zero rating. This could prove extremely costly for those projects. Further, under the existing ESC if there is a change of use within the 10 year period no tax charge (as referred to above) arises. This does not apply to the new rules. Any change of use within the period of 10 years will trigger the charge.

The change of view appears to have come without any prior consultation and it is expected that charities will lobby the Government to reverse the changes.

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