

VAT - the unfortunate demise of *Lennartz* Accounting for charities?

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HMRC have recently given their views following a decision of the European Court of Justice (ECJ) last year regarding the availability of *Lennartz* treatment for assets used for both business and non-business purposes.

***Lennartz* - a quick recap**

Herr *Lennartz* was a German Tax Adviser. He purchased an asset for both private and business use and reclaimed all of the VAT "up front". He then accounted for VAT on the private use of the asset each VAT quarter and thus gained a substantial cash flow benefit. The ECJ confirmed his entitlement to do so.

In the UK, charities and HMRC have long assumed that the same treatment could be applied when a capital asset was purchased for both "business" and "non-business" purposes.

What's changed?

A Dutch cooperative went to the ECJ seeking clarification on a technical point regarding the operation of *Lennartz*. The judgment was more far reaching. The Court said that *Lennartz* is available for private use of a business asset because private use is something that happens outside a business. Where a charity uses an asset in pursuit of its own charitable objects *Lennartz* isn't available. The asset is used "internally."

What is not clear is what happens if the charity has an asset that (in accordance with its objects) it allows other organisations to use for free. A charitable trust owning property, for example.

What does this mean for charities?

From 22 January 2010 charities may not use *Lennartz* for any new capital projects to be used for their own non-business activities. VAT suffered must be apportioned. Exceptionally, HMRC will consider claims from taxpayers who have already entered into binding commitments for projects on the understanding that *Lennartz* accounting will be available.

Charities with assets subject to existing *Lennartz* accounting arrangements are offered a choice:

- unwind existing arrangements (but see below); or
- opt to continue using *Lennartz* accounting in respect of the assets concerned, honouring the full, ongoing commitment to account for output tax under *Lennartz* accounting.

Although this would seem equitable, it is difficult to see how HMRC could prevent a charity from withdrawing from *Lennartz* treatment. HMRC are adamant that they will not accept one-sided claims for repayment of the output tax only. What isn't clear is how they intend to enforce this in circumstances where the original input tax claim is now out of time to adjust.

If you would like to discuss either the above, or any other VAT issues with an experienced, commercially focused VAT adviser, please contact Steve Chamberlain or Julian Borley of our VAT department on 01865 261100.