

May 2004

UK Formally Admits Mixed-use Yachts to “Capital Item” Treatment

Isle of Man (IOM) Customs have operated an extra-statutory owner-user scheme for mixed-use yachts for years. This allows the owner to recover VAT incurred on purchase of a yacht fully, subject to clear business intent. He may then use the yacht as principal “charterer” and account for output VAT on that private use.



UK Customs, on the other hand, always followed an approach that determined recovery of VAT only on a one-off basis, by reference strictly to the use to which the yacht was initially put. Thus for mixed-use yachts (i.e. business and non-business, including private use), only apportioned recovery of the proportion of VAT attributable to business use could be expected.

This all changed on 23 December 2003 when UK Customs announced a relaxing of the rules following the ECJ decision on the *Seeling* case.

The change of policy marked a large, but not complete, realignment of the UK position to that of the IOM. To the existing apportionment approach for mixed-use yachts (which ceased to be mandatory), UK Customs added a new ‘consume-payback’ mechanism.

The mechanism is a simplified capital item scheme of sorts. But it is by no means simple, particularly because of the tricky calculation of the VAT charge for private use.

Take the example of a small yacht costing £1,000,000 plus £175,000 VAT to construct. The taxpayer chooses to claim the whole £175,000 as input tax on the VAT return for the period in which the yacht was supplied. Under the mechanism, non-business use is treated as consumption and taxed over a 5-year maximum “chargeable

period”. [The IOM “owner-user” scheme may allow a chargeable period of up to 20 years].

- Therefore over this 5-year period the baseline figure each year would be £200,000 – or £50,000 per VAT period if the taxpayer is on quarterly returns.
- In the first VAT return period, the yacht is used 50% for non-business use. Output tax will be due on £25,000 in that period (i.e. 50% x £50,000). In the second VAT return period, non-business use increases to 75%. Tax will be due on £37,500 in that period. If non-business use decreases in the next period, the value for the output tax will be lower.
- Output tax is payable in each VAT return period in which non-business use occurs over the remaining 17 quarterly tax periods.
- Where the yacht remains in the business after the end of the 5-year chargeable period and it continues to be used for non-business purposes, it will no longer be necessary to account for output tax.
- However it should be noted that goods are treated as **wholly** business assets under the mechanism. Therefore on sale of the yacht or deregistration of the taxpayer, VAT will normally be due on the yacht’s full selling price.

Admittedly, the UK’s belated acceptance of this mechanism allows mixed-use yacht owners a choice of spreading their VAT liability – albeit over a rigid time scale that is three times shorter than the IOM’s. But the scheme may not always be advantageous to taxpayers, particularly where the yacht involved is likely to appreciate in value.

EU Enlargement

On 1 May 2004 the EU increased in size from 15 to 25 Member States. Any business with international dealings will need to be aware of the ramifications. We summarise the relevant implications in the June 2004 YVN.

VAT Treatment of Pontoons

Read our article in the “Caveat Section” of Issue 60 of *The Yacht Report* out in July.

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