Understanding VAT rules

The VAT rules that apply to building and development projects are complex, but it’s important to have a grasp of their implications. Understanding the appropriate treatment of VAT could have a significant impact on the budgeted costs of your charity’s project, potentially making it less (or more) financially viable.

This guide explains which types of projects may benefit from VAT relief. It aims to help trustees, treasurers and project managers consider the impact of the potential VAT cost for a planned project.

It is easy to misjudge VAT impacts, especially if you have limited experience of making these assessments for building projects. Legislation is complicated and the VAT position of each individual project must be considered case-by-case.

**Considering potential VAT implications early in the planning process will help you to:**
- assess whether the works should be structured differently
- evaluate VAT costs and how these might be mitigated
- take advantage of professional advice, before entering into contractual commitments

It is much better to evaluate in advance what the VAT cost will be. You can then ensure that adequate funding is available to meet the total project costs.

Don’t assume that you won’t pay VAT because you are a charity - it’s not that simple!

Keep in mind that you are likely to need the co-operation of your contractor and professional team (providers of architectural, surveying, consultancy or supervisory services) to ensure that VAT reliefs are maximised and applied legitimately. Submitting incorrect or inaccurate details when seeking VAT relief, can result not only in an unexpected VAT cost, but also a financial penalty and reputational damage.
What VAT rate will apply?

The VAT rate that applies will depend upon the:
- nature of the project
- building’s intended use
- project customer’s organisational status

Some charities are registered for VAT and are able to recover VAT incurred from HMRC. However, this should not be assumed. There is no right to recover from HMRC any VAT that has been incorrectly charged (i.e., VAT charged at 20%, when it should be at 5% or 0%). So it’s crucial to ensure that any VAT incurred has been correctly charged from the outset.

If no VAT reliefs are relevant, the 20% standard rate VAT will apply.

What qualifies for VAT relief?

Is it a new build?

Depending on the building’s intended use, some types of construction services for a ‘New build’ can qualify for zero rating (0% VAT). Examples of services that potentially qualify for VAT relief include: groundworks, construction, plumbing, electrical works and demolition of an existing building.

The construction must be a qualifying building. This includes buildings:

- designed as a ‘Dwelling’ or number of dwellings
- intended for use solely for a ‘Relevant Charitable Purpose’, or
- intended solely for a ‘Relevant Residential Purpose’

Remember to ensure that the work is completed in accordance with the terms of the planning consent.

There are very strict definitions of the terms ‘Dwelling’, ‘Relevant Charitable Purpose’ and ‘Relevant Residential Purpose’. See our handy glossary. It is important to ensure that all the necessary conditions are satisfied.

If your project is to construct a new ‘Relevant Charitable Purpose’ or ‘Relevant Residential Purpose’ building, you must issue the contractor with a ‘Specific eligibility certificate’.
Work on existing buildings

Works of repair or maintenance carried out to an existing building are generally standard rated – 20% VAT.

Certain supplies for alterations, to facilitate disabled use or disabled access, are zero rated eg provision of ramps, widening of doorways and adaptations to bathrooms and washrooms

The reduced rate of 5% applies to certain residential conversions or renovations

Extensions and enlargements will not generally benefit from VAT relief in their own right. This contrasts with the construction of a ‘Self-contained annexe’, intended for use solely for a ‘Relevant Charitable Purpose’, which may be eligible.

Intended use of building

When commissioning building work, keep in mind the intended use and function of the completed project. Both the design and intended use of the building can have an impact on the VAT position. The application of VAT will usually be determined in the first instance by the intended use. However, this may have to be revisited if the intention changes or the actual use differs from that initially planned.

That’s why it is helpful to have a clear view of the likely use over the longer term and at least for the first ten years of the life of the building.
What evidence will be required?

In all cases, the planning permission is key and must be retained. Work must be carried out in accordance with the planning permission if any VAT relief is to apply.

It is not easy to evidence intention if this has not been documented. Keep a written record of any trustees’ decisions that concern the intended use and function of a new development.

For completeness, we recommend that you retain full plans, sections and elevations (both the existing and intended, or before and after). Also, capture photographic evidence of the extent of the work, including shots of before, during and after completion.

Make sure you retain evidence of discussions of the VAT position, including any professional advice received and correspondence with HMRC.

Will I need to issue a certificate?

If the work is to construct dwellings, there is no requirement for the charity customer to issue a certificate.

An ‘Eligibility Certificate’ is required when the work relates to a building intended either for a ‘Relevant Charitable Purpose’ or a ‘Relevant Residential Purpose’. The main contractor must receive this from the customer before the work can benefit from VAT relief. Sub-contractors working to a main contractor must charge 20% VAT and should not be issued with an ‘Eligibility Certificate’.

It is normal practice for a main contractor to seek to check the validity of certificates. So it is important that the issuing of the certificate is done in good time, in case the main contractor wishes to clarify any points.

An ‘Eligibility Certificate’ confirms:
- details of the building in question
- details of the charity customer
- estimated value of the work
- estimated date of completion
- details of the building contractor

The charity customer must confirm that the relevant HMRC public notice has been read and indicate the intended use of the building. The certificate must be signed by a responsible person at the charity, confirming that the information given is correct and complete. This should also acknowledge that a VAT charge will arise if there is a change of use or disposal of the property within ten years from the date of completion.

VAT treatment of professional services

Architectural, surveying, consultancy or supervisory services are always subject to 20% standard rated VAT.

It may be possible to achieve a VAT saving by using a ‘Design & Build’ procurement route, but do take advice from your legal advisor and VAT expert on this point.
## VAT reliefs at a glance

### ZERO RATE 0%
- New build ‘Dwelling’ or number of dwellings (eg block of flats)
- ‘New build’ for ‘Relevant Charitable Purpose’
- ‘New build’ for ‘Relevant Residential Purpose’
- ‘Self-contained annexe’ for ‘Relevant Charitable Purpose’
- Disabled toilet and bathroom facilities
- Ramps
- Widening of doorways and passageways
- Stair lifts, vertical lifts and hoists
- Hearing induction loop

### REDUCED RATE 5%
- Residential renovations after being empty for two years
- Residential conversions – from non-residential to residential, or change in number of dwellings

## Glossary of terms

**Dwelling** – the dwelling consists of self-contained living accommodation; there is no provision for direct internal access to any other dwelling or part of a dwelling; the separate use or disposal of the dwelling is not prohibited by the term of any covenant, statutory planning consent or similar provision; statutory planning consent has been granted in respect of that dwelling and its construction or conversion has been carried out in accordance with that consent.

**Eligibility Certificate** – a contractor must receive a specific eligibility certificate from the customer and check its validity in order to be able to charge only 5% or 0% VAT. HMRC provide sample certificates within section 18 of their notice 708, but issuers can create their own certificate, provided that it contains the same information and declaration.

**New build** – built from scratch (no pre-existing building); the new building makes use of only a single façade, or double façade on a corner site, of a pre-existing building, where the façade/s are retained as a condition or requirement of statutory planning consent or similar; a new building constructed against an existing building so that they share a wall but there is no internal access between them.

**Relevant Charitable Purpose (RCP)** – use by a charity in either or both of the following ways - otherwise than in the course or furtherance of a business; as a village hall or similarly in providing social or recreational facilities for a local community.

**Relevant Residential Purpose (RRP)** – use as a home or other institution providing residential accommodation for children; a home or other institution providing residential accommodation with personal care for people due to old age, disablement, past or present dependence on alcohol or drugs, or past or present mental disorder; a hospice that provides residential accommodation; residential accommodation for students/school pupils; residential accommodation for members of the armed forces; a monastery, nunnery or similar establishment; an institution that is the sole or main residence of at least 90% of its residents but not used as a hospital, prison, hotel or similar establishments.

**Self-contained annexe** – the annexe is intended for use solely for an RCP; the annexe is capable of functioning independently from the existing building; the annexe and the existing building each have their own independent main access.
Conclusion

The VAT implications for building projects and large developments are complex. An unexpected 20% VAT cost could push your project over budget, potentially impacting its financial viability or intended impact. Added to that is the risk of miscalculating your project’s VAT liability, incurring an HMRC penalty and reputational damage. So it is prudent to take professional advice from a legal advisor and/or VAT expert, before entering into contractual commitments.

Get in touch with the VAT team at Knill James for an initial consideration of the facts and CAF Bank if your charity needs assistance financing a new build or refurbishment project.

About Knill James LLP

Knill James LLP is an innovative firm of Chartered Accountants based in Lewes, providing one-stop specialist advisory and compliance service to clients in the Charities and Education sector. We have many years’ experience working with not-for-profit organisations and understand the issues and challenges they face. As a 60 strong team of financial experts, our starting point is always the same: to understand our clients’ needs first.

Alison Sampson is the dedicated VAT Consultant at Knill James, with over 30 years’ experience of helping charities make the right choices in respect to VAT issues. Please contact the team to discuss any issues raised in this guide on 01273 485083 or email Alison at alisonsampson@knilljames.co.uk

About CAF Bank

CAF Bank offers flexible loans for UK charities and not-for-profit organisations looking to grow their impact.

Owned by a major UK charity, Charities Aid Foundation (CAF), we’re driven by a social purpose and trusted by our 14,000 customers with over £1 billion of deposits. Our experienced relationship managers travel to meet every borrower. This helps us understand your business model, financial position and vision for the future. We will make sure you’re aware of the potential risks associated with borrowing, so you can consider if loan finance could be a suitable funding option for your organisation.

Get in touch on 03000 123 444 or find out more about our secured loans at www.cafonline.org/loans

Useful sources of information

HMRC notice 708, Buildings and construction

HMRC notice 701/7, Reliefs from VAT for disabled and older people

HMRC notice 701/1, How VAT affects charities
https://www.gov.uk/guidance/how-vat-affects-charities-notice-7011

HMRC internal manual, VAT Construction
https://www.gov.uk/hmrc-internal-manuals/vat-construction
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Loan applications subject to credit assessment. Security will be required.

Charity assets may be at risk if you do not keep up with the repayments for a mortgage, loan or any other debt secured on them.

If you’re thinking of consolidating existing borrowing, you should be aware that you may be extending the term of the debt and increasing the total amount you pay.

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