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PRIVATE USE OF BUSINESS ASSETS TRIGGERS VAT

Operating a business in this ever-changing environment has grown to become a complex trade that require the utmost flexibility in making business decisions. In some instances, a business may be forced to diversify operations resulting in it changing the use of business assets. Change of use may also come through allocating a director a business asset or awarding it to employees. It is therefore key to comprehend Value Added Tax (VAT) implications involved in such situations. In this article, words importing the masculine shall be deemed to include the feminine

The basics

To fully comprehend this seemingly complex matter it is vital to take a step back and understand a few basic elements around the VAT cycle. Firstly, let us have a look at the principles of claiming of input tax i.e., VAT incurred when one makes a purchase. The input tax is only claimable when the respective purchase is used to make sales subject to VAT at 14% or 0%, alternatively known as taxable supplies. This is however subject to certain restrictions provided by the law. Let us now look at what happens when an asset which was purchased for taxable supplies is applied to a different use.

Enter change of use

When a business acquires an asset such as a lorry to use it for transportation services subject to VAT, it claims the VAT from BURS. However, when the same asset is taken for the personal use of the MD or CEO, then the business is deemed to have sold the same asset at the lesser of the original cost at which it was acquired or the market value at the time of the switch in usage. That deemed sale simply means that the business must then account for output VAT as if it indeed sold the said asset. It is also key to note that such adjustments are not only restricted to goods or assets but they are also applicable to services. However, only goods or services that previously qualified for input tax credit should trigger this deemed VAT adjustment. Consequently, entertainment goods or services and motor vehicles which do not qualify for input tax claim are excluded from the change of use aspect.

It should also be noted that the use of a service might also change. For instance, if fees were paid for the design of a software program that is used for use in property management and the program is subsequently used to manage a private venture of the MD, a change of use occurs. Output tax will need to be determined and declared to BURS.

The illustration

To bring clarity to this aspect, let us assume than one Tiro Pty Ltd acquired trucks worth P11.4m (including VAT) in 2021 which were used to make taxable supplies. The company will be allowed a VAT claim of P1.4m, which it obtains from BURS. If the MD of the company decides to take the trucks as his bonus, that transaction is deemed as a sale to the MD. In other words, the company must declare the said P1.4m in VAT to BURS, technically paying back the same VAT which it claimed initially. That is what a change of use is!

Conclusion

Practically, many such changes of use occur which we can't enumerate in full. However, to avoid any pitfalls which might result in tax penalties and interest, taxpayers need to analyse and account for VAT on all substantial changes in the business assets and or services.

Well folks, we hope that was insightful. As us the two Yours Truly say goodbye, remember to pay to Caesar what belongs to him. If you want to join our free Tax WhatsApp group, send us a text on the cell number below.