

Changes to UK VAT on Aircraft from 1st September 2010

David Anderson and Graeme Perry both solicitors at Sykes Anderson LLP Solicitors and Chartered Tax Advisers.

Please note that tax law is a complex subject and you should not rely on this article without professional advice on the facts of your case.

2010 Budget

Amongst the raft of tax announcements in the 2010 Budget, one element which has not been highly publicised is the amendment to the VAT regime for aircraft. The changes will have a big impact on purchasers of jets in the UK who may, from 1 September 2010, have to pay VAT (at 17.5% of the purchase price) on an acquisition which might currently be exempt. In many circumstances this VAT will not be recoverable. The amendment comes in light of an order from the European Commission that the UK changes its VAT regime to comply with the European VAT directive.

Current Position

Up to now in the UK the distinction used to determine whether a transfer of an aircraft comes within VAT at 17.5% or can be zero rated (equivalent of exempt) has been based on the maximum take-off weight of the aircraft. This has meant that transfers of aircraft with a maximum take-off weight of over 8,000kg have been free of VAT. The buyer's proposed use for the jet is not taken into account.

This has been helpful for many entrepreneurs who have purchased private jets in the UK as a good number of these weigh in excess of 8,000kg and will not be used for business purposes. If VAT had been charged on the purchase, it would not have been possible to recover this due to the predominantly private use of the jet.

Change of regime

This regime will be changed completely so that there will no longer be a weight distinction. When the law is amended, from 1 September 2010, the purchase of any aircraft in the UK, regardless of its weight, will be potentially within a VAT charge. There will still be a distinction between those transfers which are standard rated (17.5%) and those which are zero-rated (exempt). This will be based on the proposed use by the purchaser.

The suggested approach from HMRC is that supplies will be zero-rated only where the aircraft will be used by an 'airline operating for reward chiefly on international routes'. This will obviously require some guidance, not least as to what requirements will dictate who is an 'airline' and what proportion of international flights is required to qualify.

Whatever the outcome of the finalised legislation and guidance, the proposed position will require significant due diligence on the part of aircraft sellers who will need some form of undertaking from the purchaser as to their proposed use of the aircrafts. Only when they have this will they be able to decide whether VAT should be payable or not on the transfer. If there is doubt the sellers may require the VAT to be paid into an escrow account until the buyer's commercial status is accepted by HMRC.

Compliance of UK with EU rules

This brings the UK into line with the general application of the VAT Directive throughout the EU. One of the countries which has operated this practice for some time is France where there is an annual list published of 'airlines' which fall within the exemption. Parties other than these airlines who acquire any type of aircraft must be charged VAT on their purchases. It is likely the UK will have to take a similar approach as other EU countries have been concerned residents in their countries have been buying private jets in the UK thereby avoiding the local VAT which would otherwise have been payable on a purchase in the buyer's country of residence. Although they may technically have a liability for local VAT if they start using the private jet in their country in most cases local VAT has not been claimed.

Impact

This will increase significantly the purchasing costs for those individuals seeking to acquire a private jet. An initial assessment of the proposed legislation indicates that it will be difficult to fall within the VAT exemption, particularly when the approach in other EU countries is considered. It may be possible to recover the VAT by carrying on a chartering business which amounts to a business. This will however complicate matters as the jet for instance will have to be compliant as a public carrier.

There will also be an impact on cash flow for businesses which intend to operate aircrafts as part of their business but perhaps do not fall within the required definitions for the exemption. Although they will be able to reclaim the VAT paid out on the purchase this will take some time and could prove problematic. It will also raise questions as to the level of directors' personal use of the jets, for which VAT recovery will be disallowed, which in turn will lead into issues about benefits in kind.

There may therefore be an increase in the jet acquisition market in the UK before 1 September 2010. We at Sykes Anderson LLP have advised on numerous jet transactions and have set up structures for tax efficient ownership and operation of private aircraft.

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David Anderson
Solicitor and Chartered Tax Adviser
Graeme Perry
Solicitor
Sykes **Anderson** LLP
9 Devonshire Square, London EC2M 4YF Tel 020 3178 3770
www.sykesanderson.com
david.anderson@sykesanderson.com