# CHAPTER 7

# DEEMED SUPPLIES AND SELF-SUPPLIES

## 7.1 Introduction

Deemed supplies and self-supplies are in existence as an anti-avoidance measure.

This anti-avoidance legislation requires a trader to **account for output tax** even though there is no supply for consideration to a third party.

The anti-avoidance legislation effectively covers two types of avoidance.

The **deemed supply legislation** applies where a taxable business buys something, recovers the input tax, and then puts those items to a non-business use.

The **self-supply legislation** applies to partially exempt and fully exempt businesses, so businesses that make exempt supplies and cannot recover input tax in full.

## 7.2 Deemed supplies

A common example of a deemed supply is **goods bought for business purposes but then supplied free for private consumption**. The input tax originally claimed on the purchase is clawed back using an output tax charge. VATA 1994, Sch 4 Para 5

Also where petrol or diesel for motor cars is purchased by a business but then supplied to the employee of that business, there is a deemed supply and output tax is charged on the supply using a fixed standard scale. We will look at this in more detail later. VATA 1994, s.56

Finally where a business is registered for VAT but is now going to deregister. Any goods held by the business on deregistration are treated as deemed supplies if those goods had input tax recovered on their purchase. VATA 1994, Sch 4 Para 8

## 7.3 Self-supplies

Self-supplies operate in a similar way to deemed supplies. The self-supply legislation ensures that there is no VAT saving in a situation where input tax should have been irrecoverable.

For example, assume some cars are purchased by a car dealer who plans to sell those cars to the public. The full input tax is recoverable as he is buying stock for 100% use in his business. SI 1992/3122 Art 5

The dealer later puts one of those cars to private use by taking a car out of stock and making it available to be used by an employee. This would be a **self-supply** and there is an **output tax charge on the cost of the car**.

## 7.4 How to account for deemed/self-supplies

A business that makes a deemed or a self-supply will have to account for output tax on the supply, so there will be output tax to put on the VAT return. This output tax will be paid to HMRC when the VAT return is submitted.

This **self-supply or deemed supply counts towards the registration limit** when looking at whether a business should register for VAT or not.

**Deemed supplies** will only be in point if the trader has recovered input tax on the goods or services in question.

When accounting for output tax on a **self-supply**, input tax is available for credit. This input tax can only be recovered to the extent that the item is to be used for making taxable supplies.

The deemed and self-supply rules apply to all businesses, whether taxable or exempt.

## 7.5 Gift of goods (deemed supply)

Input tax is clawed back on goods that are given away by making an output tax charge on the replacement cost of such goods. VATA 1994, Sch 4 Para 5

These rules will not apply unless the donor is entitled to input tax recovery on the goods.

However even where input tax is recovered, the gift may still be **exempt** from this legislation. There are two exemptions.

VATA 1994, Sch 4 Para 5(2)a

The first exemption is where there is a gift of goods made in the course or furtherance of the business where the **cost to the donor is not more than £50.**

No output tax will be due on a series of gifts provided the total cost of gifts made to the same person does not exceed £50 in any 12 month period. If the £50 is exceeded VAT will be due on all the gifts made in the previous 12 months.

The other situation where the rules do not apply is where there is a **gift to any person of a sample of any goods.** This applies only to the first gift where a succession of identical samples is given to the same person. VATA 1994, Sch 4 Para 5(2)B

## 7.6 Private use of business assets (deemed supply)

Consider the scenario of an asset owned by a VAT registered business which is made available for private use by an employee. The rules on gifts of goods do not apply in this instance as no gift has been made.

Ordinarily where goods are acquired with the expectation of some non-business use, the trader will apportion the initial input tax recovery. VATA 1994, s.24(5)

However following the *Lennartz* ruling, a full input reclaim can be made initially followed by an output tax charge in every VAT quarter in which private use takes place. The output tax charge reflects the cost of providing that asset for private use. VATA 1994, Sch 4 Para 5(4)

Thus the *Lennartz* rule allows purchasers of goods which are to be used both for business and non-business purposes to recover the VAT in full on the purchase of the item, and then charge output tax on the market value of the non-business use as it arises.

From 22nd January 2010 the position regarding *Lennartz* recovery has changed following the *Vereniging Noordelijke Land-en Tuinbouw Organisatie (VNLTO)* case. It will allow input tax to be reclaimed only on goods where there will be part business and part private use. Where there will be non-business use, input tax must be disallowed on the part of the cost that relates to the non-business use at the time the goods are purchased.

**Illustration 1**

Up & Away Ltd is a small company running hot air balloon tours in Kent. They own one hot-air balloon which is used for business purposes 60 days per quarter and for private purposes by the company employees 20 days per quarter.

Costs associated with maintaining the balloon are £6,000 per quarter.

We have to work out the private cost of maintaining the balloon. That will be our deemed supply for one quarter.

| | |
|---|---|
| Deemed supply for one quarter: | £ |
| Balloon costs<br>£6,000 x 20/80 | 1,500.00 |
| VAT = 17.5% x £1,500.00 | £262.50 |

## 7.7 Motor fuel provided for private use (deemed supply)

If a business buys petrol or diesel and allows private use of it by an employee or the owner of the business, then the business has three choices as to what it will do from a VAT point of view. VATA 1994, s.56

1) **reclaim all input tax** incurred on all fuel purchased and then, using the **scale charges** set by HMRC, calculate the appropriate output tax. The fuel scale rates are dependent on $CO_2$ emissions. The scale rates can be found at s.57 VATA 1994. VATA 1994, s.57

2) **claim absolutely no input tax** on all fuel purchased. As there are no input tax issues, there is no need for any output tax calculations. Notice 748 ESC 3.1

3) **keep very detailed mileage records** so that the business can prove that the fuel purchased is used for business purposes only (ie, to convince HMRC that the business does not pay anything towards the cost of fuel used for private purposes). In such a case, input tax can be recovered and there is no output tax charge.

### Example 1

In the quarter ended 30 September, Jonas Ltd spent £235.00 on petrol. The petrol was for Mr Jonas's car in which he travels 1,000 business miles and 1000 private miles each quarter. The car has $CO_2$ emissions of 215 g/km.

**What is the net VAT payable or (recoverable) for the business for this quarter if it wishes to recover the input tax on the fuel?**

*Tutor note – at the end of this chapter you will find a table of VAT scale charges. In the actual exam you will need to look up s.57 VATA 1994.*

## 7.8 Goods held on deregistration (deemed supply)

When a business deregisters for VAT, this will mean that the assets contained in the business, when eventually sold, will not have VAT charged on their sale. As input tax would have been reclaimed when these assets were bought, a possible VAT loss to HMRC will arise. VATA 1994, Sch 4 Para 8

In this situation, a special rule says that when a business deregisters for VAT there is a deemed supply at the date of deregistration on all the assets that were held on the date the business deregistered. VATA 1994, Sch 6 Para 6

Output tax is charged on the "replacement cost" of the assets. Replacement cost is the cost of an asset in exactly the same condition.

This rule only applies to assets on which input tax was claimed originally. For example if there is a car in the business when it deregisters, and there was no initial input tax recovery on that car, output tax is not charged.

There is also **no charge** if the **output tax** that is due comes to **£1,000 or less.**

The following are **excluded** from the charge to VAT:

- Goods bought from an unregistered businesses
- Motor cars (except qualifying cars on which input tax has been claimed)
- Goods used wholly for business entertainment
- Goods that have been directly attributed to an exempt business activity (unless the input tax was reclaimable through the partial exemption rules)
- Goods not bought for business purposes
- Land or buildings which were purchased under a supply on which VAT was recovered (e.g. where a fully taxable business buys a new commercial property) if at the time of deregistration the sale would be exempt (because the business has not opted to tax the property which is then over three years old). In such circumstances, VAT due on the supply of the property would be nil and so not exceed the £1,000 limit.

## 7.9 Motor cars (self-supply)

The self-supply charge on motor cars applies where a car dealer purchases a car from a manufacturer to put into stock. Because the car is part of his stock, he is allowed to recover input tax in full on that car (new and for resale).

Then the car dealer takes the car out of stock for private use (eg for use by an employee). Normally the purchase of a car for private use is subject to a blocking order on the input VAT, which basically means input VAT on a motor car cannot be recovered. The self-supply legislation **aims to stop a car dealer being able to get a car into private use and yet still recover input tax.** SI 1992/3122 Art 5

The self-supply charge claws back the VAT that was recovered when the motor car was purchased as stock. It is calculated on the cost of the car and not on the selling price of the car. The trader will have to account for output tax on the self-supply.

## Example 2

**Draw a line between the supply and the correct title box.**

| | | |
|---|---|---|
| Goods and services bought for business use and supplied free for private use | Cars bought for business use and transferred to private use | Motor fuel purchased by business for private use |
| | Goods held on deregistration | |

| | |
|---|---|
| DEEMED SUPPLY | SELF-SUPPLY |

**Answer 1**

The business bears the cost of private fuel, and so the choice it has made is to recover input tax in full but then to charge output tax using the scale charge.

The business mileage actually travelled by the car is irrelevant, except that we need to know that there is actually some private mileage.

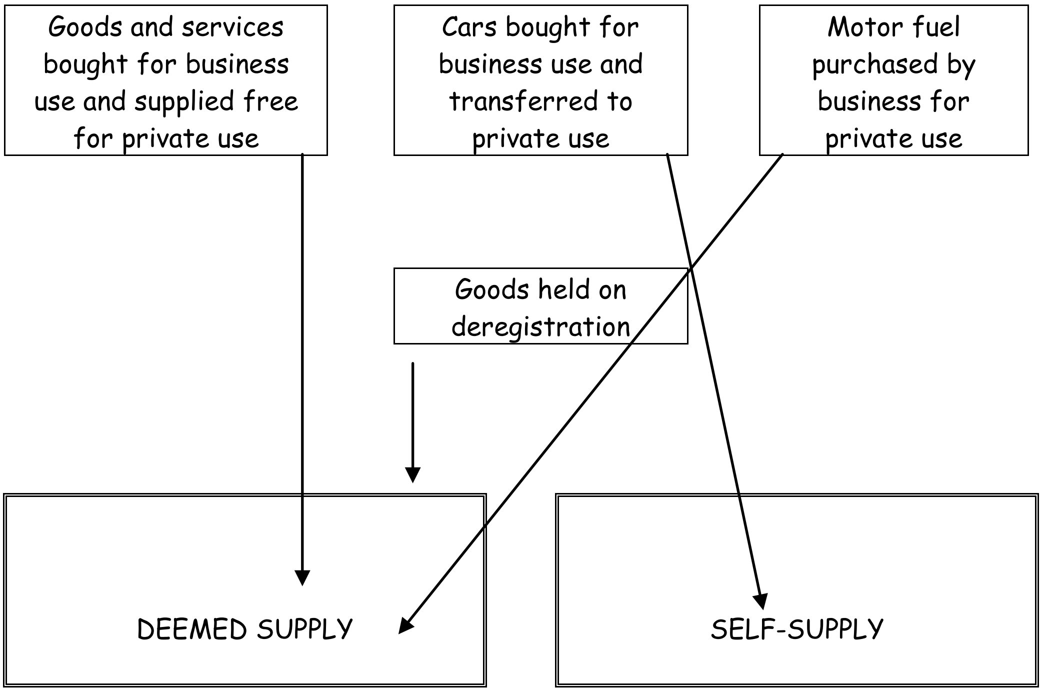
The output tax for a car with $CO_2$ emissions of 215 g/km in a 3-month period is £67.62 (s.57 VATA 1994)

We then take the cost of the petrol £235.00 (VAT inclusive), and multiply it by 7/47 to get the recoverable input tax.

| | £ |
|---|---|
| Output tax | 67.62 |
| Input tax | |
| £235.00 x 7/47 | (35.00) |
| Net VAT payable | 32.62 |

In this example, Jonas Ltd should be advised to claim no input tax on fuel. If this were the case, the fuel scale charge need not be accounted for and the business would save £32.62 this quarter.

**Answer 2**


Goods and services bought for business use and supplied free for private use
Cars bought for business use and transferred to private use
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Goods held on deregistration
DEEMED SUPPLY
SELF-SUPPLY