

What you should know about deduction of VAT

The right to deduct VAT is an essential element of VAT. VAT payers charge VAT to their clients. This VAT is transferred to the Treasury. However they can deduct the VAT which they have paid themselves. A VAT payer should not carry the charge of VAT. A simple rule, which in practice is not always that simple.

Only VAT payers can deduct VAT

Not everyone who pays VAT can deduct this VAT. It is the purpose that the VAT is actually carried by the end consumer of a product (the consumer). Therefore only VAT payers have the right to deduct VAT. These are persons which sell goods and services within the scope of their economic activity. In the complete production chain from the producer over the distributor up to the retailer, all persons are VAT payers with right to deduct VAT. Until the product comes with the consumer, who finally pays the total VAT. You notice that the persons actually carrying the cost of the VAT is not a VAT payer in this system.

A VAT payer has right to deduct VAT when he exercises or will exercise an economic activity. If an entrepreneur before he actually starts his activity already makes costs in order to prepare for his economic activity, he can already deduct the paid VAT. The intention to start an economic activity is sufficient, but should be proven based upon objective circumstances. The right to deduct VAT remains even when the activity never actually started, e.g. when based on a market study the project was not viable.

Special cases (1): exempt VAT payer

Not all VAT payers can deduct VAT. Some VAT payers perform activities which are themselves VAT exempt. So they have an economic activity, but cannot charge VAT to their clients. On the other hand they cannot deduct VAT either. Amongst others, doctors are considered here. They are referred to as exempt VAT payers.

Small businesses with an annual turnover of less than 15.000€ are in a similar situation. Small businesses should not charge VAT to their companies, but cannot deduct VAT neither. As a consequence they have less administrative burdens. This special scheme is optional, meaning that such small businesses can still opt to be subject to the normal rules.

Special cases (2): mixed VAT payers

A mixed VAT payer has different activities: some activities are VAT exempt, others are taxable. He does not have full right to deduct VAT. The right to deduct VAT exists to the extent that the mixed VAT payer performs taxable transactions. E.g. Mr. Smith is 65% real estate broker (taxable activity) and 35% insurance broker (exempt activity). He can deduct 65% of the paid VAT.

Special cases (3): occasional VAT payer

In some cases a private individual can become an occasional VAT payer. Everyone selling a new building (also a private individual) can opt to do this with VAT instead of with stamp duties. In such case the supplier (= the occasional VAT payer) can deduct the VAT which he has paid in order to build the building, e.g. VAT on labour and materials.

A building is new until the 31 December of the second year following the year of occupation.

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Limited deduction for certain expenditure

The VAT on gifts for business relations is only deductible if the value of the gift (exclusive VAT) is less than 50€. If the gift is more expensive, VAT is not deductible. VAT on costs for producing and distributing free samples is however fully deductible.

For cars expenditure VAT is limited to 50%. For a car which is used partly professional, partly private, deduction is limited to the professional part (without exceeding 50%). In order to calculate the professional/private fraction, the VAT authorities have developed three formulas in their administrative circular.

No deduction for certain expenditure

Privately acquired goods and services never give right to deduct VAT. Even when they are bought by a VAT payer. If a dealer buys a smart phone for its sales team, the VAT is deductible, since this purchase is done within the scope of his professional activity. When he buys this smartphone for the birthday of his wife, he act as a private consumer and the VAT is not deductible.

VAT on reception costs is not deductible. These are all costs (food, drinks, ..) to accommodate visitors not being part of the business (suppliers and customers, but also shareholders or partners). On the other hand VAT on publicity expenditure is deductible. As a result discussions may occur. Imagine that a company organizes a party for its tenth anniversary: these costs could be both reception costs and publicity costs ...

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