

VAT Property Rental Business Purchase

Background

A purchaser may buy a commercial building with a sitting tenant where the seller has exercised a VAT option to tax that building. The purchaser must consider the VAT implications, outlined below.

Option to tax: general implications

Where an owner has exercised a VAT option to tax a building, the owner must charge VAT both on lease rentals and on the selling price on a sale. Therefore, when the building is sold the seller will add VAT to the price; almost invariably the price will be negotiated on an exclusive of VAT basis.

There are two main consequences of the addition of VAT to the purchase price, as follows-

- As noted above, the purchaser will be required to pay the agreed price plus VAT, and the purchaser must consider whether this VAT can be recovered from HMRC.
- The purchaser will be liable to Stamp Duty Land Tax (SDLT) in England, Wales and Northern Ireland, or Land and Buildings Transaction Tax (LBTT) in Scotland. The liability to these property taxes is based on the whole price including VAT, irrespective of whether or not the purchaser can later recover the VAT. The progressive rates of SDLT and LBTT can mean that the liabilities rise by more than 20% because of the addition of VAT.

Transfer of a going concern: general principles

Where the purchase of a business meets the conditions for a transfer of a going concern (TOGC), the transaction is outside the scope of VAT, i.e. no VAT is charged.

Suppose a shop were purchased together with its stock, and along with the transfer of employees' contracts of employment. This would be a TOGC. Subject to conditions, the seller would not charge VAT, and the purchaser would not pay any VAT.

Further, it has been established that a property rental business may be transferred as a TOGC. The simplest example is the purchase of a single building with a sitting tenant. Further details are given below.

In other words, the purchase of a commercial building where the seller has exercised an option tax may be either-

- the purchase of a mere asset, where VAT is chargeable. The VAT may be later recoverable if the purchaser is going to occupy it for the purposes of a

trade which he carries on, or, conversely, if it is to be later let and the purchaser opts to tax the property, or

- the transfer of a going concern which, if it meets other conditions, is a VAT free TOGC.

Property rental business TOGC

VAT Notice 700/9 at section 6 details examples of what HMRC both does and does not accept as being the transfer of a going concern of a property rental business.

HMRC does accept a transfer in the following circumstances, in principle, as meeting the conditions for a TOGC-

- a property that is only partly let;
- a lease to the tenant that is in a rent free period;
- a lease that has been signed by tenants who have yet to take occupation;
- a seller who has found a tenant but the lease has not yet been signed;
- the sale of a package of buildings, some let and some unlet, some completed and some unfinished. (This is distinct from the sale of only some of a larger number of properties, partly let, partly unlet, where the TOGC implications are considered on a case by case basis.)

By contrast, HMRC's view is that a TOGC would not occur where the seller is only at the stage of actively marketing the property; where there is an occupant who has no right to remain after the purchase; or where there is a purchase of a property by the tenant.

A key test is whether the transferor can evidence an intended or actual economic activity.

TOGC conditions

The transfer of a property rental business as a TOGC outside the scope of VAT is also subject to some conditions to be fulfilled by the purchaser. In practical terms the purchaser conditions are-

- The purchaser must register for VAT, if not already registered. (Form VAT1)
- The purchaser must opt to tax the property from the date of the purchase, and notify HMRC of this by that date. (Form VAT1614A)
- The purchaser must notify the seller of his option to tax.
- The purchaser may need to complete an HMRC property questionnaire. (Form VAT5L)

Legislation

- VAT (Special Provisions Order) 1995 art s4,5.

Commentary

- HMRC VAT Notice 700/09: transfer of a business as a going concern.
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