

New VAT on Property Regime

Summary

The main provisions of the new regime will include:

- ◆ The supply of buildings – whether by the sale of the freehold or via a very long lease (a “freehold equivalent”) - will be subject to VAT only while the building is considered “new”. For this purpose, a building will be regarded as “new” for a period of up to five years following completion. The first supply of a building within five years after completion will always be subject to VAT. Subsequent supplies within five years after completion will also be subject to VAT except where the building has been occupied for two years or more at the time of supply. An existing building that is substantially refurbished or is adapted for materially altered purposes will be considered “new” following such work and sales of those buildings will be subject to the rules for sales of new buildings.
- ◆ The supply of “old” buildings will be exempt from VAT, but there will be an option to tax such supplies. Where the option to tax is exercised, VAT will be charged on the actual consideration. The option will be exercised jointly by the vendor and purchaser. VAT will be accounted for by the purchaser, under the reverse charge mechanism.
- ◆ The supply of “building land” will be taxed in the same way as it is taxed currently. The VAT treatment of undeveloped land (e.g. farm land) will not be affected. Land that is sold in connection with a contract to develop it will continue to be subject to VAT.
- ◆ Most leases will be exempt from VAT but leases that represent effective ownership will be treated in the same way as supplies of the freehold.
- ◆ There will be an option to tax rents on commercial buildings where the landlord and tenant are not connected persons. The option may be exercised by the landlord and provision will be made for cancellation. Where the option is cancelled while the building is still subject to the Capital Goods Scheme (please see below), a Capital Goods Scheme adjustment will apply. Anti-avoidance measures will ensure that no unjustified advantage arises on the cancellation of an option. ‘Connected persons’ will be given a broad definition so as to prevent abuse of the option to tax facility.
- ◆ A Capital Goods Scheme will be introduced. Deductibility for input VAT relating to a property will be initially allowed by reference to the use of the property for the first twelve months of full use. The Capital Goods Scheme will require an annual review by the taxpayer of the use to which a property is put over the following twenty years (in terms of taxable or exempt use). Where there is a change in use, an adjustment of deductibility will be required. The adjustment will reflect the difference between the use in the initial twelve months of use and the use in the year in question. Ultimately, the proportion of VAT allowed to be deducted will reflect the actual use of the property over the twenty-year period.

The purpose of this summary is to provide an overview of the new VAT on Property regime which will take effect on 1 July 2008.

No action should be taken on the basis of this summary without obtaining professional taxation advice.

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