VAT on Property Rules

The Finance Act 2008 introduced rules relating to the VAT treatment of property transactions which commenced on 1 July 2008.

These rules completely replaced the pre 1 July 2008 VAT on property system and aimed to exempt most property transactions from VAT but with an option to tax the transaction in certain circumstances.

The legislation after 1 July 2008 affects the following:

- Sales of commercial property.
- Sales of residential property.
- Leases of property.
- Long leases of property (i.e. leases for 10 years or more) which are currently in place but where the term of the lease does not expire until on or after 1 July 2008.

Sales of commercial property

New buildings

VAT must be charged on the sale of a property at the 13.5% rate where the property is considered “new”. The property is considered “new” in the following circumstances:

- The first supply of a completed property within five years of its completion.
- The second and subsequent supply of a property, if the supply is made within five years of completion, and the building has been occupied for less than two years.

Second hand buildings

The supply of second hand buildings which were developed before 1 July 1988 will be outside the VAT net provided the property was not redeveloped in the meantime.

The supply of all other second hand buildings is exempt from VAT however the seller and the buyer may jointly opt to tax the sale of the building. If the joint option to tax is not exercised, the vendor will suffer a claw back (time apportioned to reflect the remaining VAT life of the property) of the VAT previously recovered on the acquisition or development of the property.

Sales of residential property

Where the property is residential the first supply of the newly completed property will always be liable to VAT regardless of when it is supplied and of what use the supplier has put the property to prior to the supply.

Leases of property

It is important to note that the point or time of supply for VAT purposes is usually the earlier of the date the tenant takes occupancy or the date the lease is signed.

The pre 1 July 2008 distinction between long term and short term lettings has been discontinued. Under the new system all lettings are exempt from VAT. However the landlord still has the option to tax the letting and charge 21% VAT on rents. If the landlord's option to tax is not exercised, the landlord will suffer a clawback (time apportioned to reflect the remaining VAT life of the property) of the VAT previously recovered on the acquisition or development of the property.

The option to tax will never be available on lettings of residential property and will no longer be available on lettings between connected parties unless the tenant can recover at least 90% of the VAT charged on the rents.

Also, the option to tax will cease, or no longer be available, if the landlord occupies the property themselves or a person connected with the landlord occupies the property.

Long leases of property

Long leases, currently in place, but where the term of the lease does not expire until on or after 1 July 2008, may be assigned or surrendered on or after 1 July 2008. The assignment or the surrender will be chargeable to VAT if the tenant who is making the assignment or surrender was entitled to some VAT recovery on the acquisition of the lease or the development of the property (time apportioned to reflect the remaining VAT life of the property). The VAT is then accounted for under the reverse charge mechanism.

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