Letting of Property

This document should be read in conjunction with sections 97 and paragraph 11(1) of schedule 1 of the VAT Consolidation Act 2010 (VATCA 2010)

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Introduction

This guidance covers the Value-Added Tax (VAT) treatment of letting property from 1 July 2008, with the exception of lettings covered by transitional measures for a waiver of exemption.

Letting property is a service and includes leasing and letting. It does not include supplies of freehold equivalent interests. Lettings are exempt from VAT. However, you may opt to tax a letting subject to certain conditions.

For information in relation to the letting of accommodation for use as 'emergency' accommodation please "Supplies of emergency accommodation and ancillary services" guidance.

1 How does a landlord opt to tax a letting?

You are treated as exercising the landlord's option to tax when you claim the repayment of VAT incurred on the acquisition or development of the property.

When you let your property you must do one of the following to confirm your option to tax, either:

- include a written provision for the taxation of the rent in the letting agreement
  or
- issue a document to the tenant stating that VAT is chargeable on the letting.

Otherwise, the option to tax will be regarded as terminated.

On termination of the option, you will be subject to a Capital Goods Scheme (CGS) adjustment. It is not possible to backdate a landlord's option to tax.

Example 1

Exercising the landlord's option to tax at development stage and at commencement of the letting.

Mr A develops a building in 2012 which is to be let to commercial tenants. He intends to opt to tax the lettings and registers for VAT on the basis that he will make taxable lettings of the property. He claims a repayment in respect of the VAT charged by the builder, architects, and so on. Mr A is treated as having exercised the landlord's option to tax the letting.

When he comes to let the building, Mr A can do one of two things. He can either include a provision in the letting agreement to the effect that the rents will be taxable, or issue a document to the tenant stating that the VAT is chargeable on the rents.

Mr A then charges his tenants VAT on the rents and accounts to Revenue for that tax.

Example 2

Terminating a development-stage landlord's option to tax

As in Example 1, Mr A intends to exercise the landlord's option to tax the rents from the property. However, when he lets the property, he neither includes a provision in the letting agreement to tax the rents, nor issues a document to his tenant to that effect.

Mr A must make a CGS adjustment in the VAT period in which the letting is made, and repay the tax deducted in relation to the property (see Capital Goods Scheme (CGS) - other adjustments for further details).

2 Can a landlord opt to tax the letting of a property where previous lettings were exempt?

Yes. You can opt to tax such rents by either:

- agreeing in writing with the tenant (either an existing or new tenant) that the rents will be taxable
  or
- by issuing a notice in writing to the tenant to this effect.

With effect from the date of the agreement or notice, rents from that property will be taxable. You may be entitled to make a CGS adjustment in respect of VAT incurred on the acquisition or development of the property (see Capital Goods Scheme (CGS) - other adjustments for further details).

A positive CGS adjustment does not apply where you exercise the landlord’s option to tax after 1 July 2008, in respect of a transitional property. This is because the provisions in the CGS that would give rise to such an adjustment are not applied for transitional properties. It is not possible to backdate a landlord's option to tax.

Example 3

Opting to tax a particular letting

Ms B incurred €250,000 VAT on the acquisition of a property in 2010 and has been letting the property for a number of years. She did not claim input credit for this VAT.

In November 2014, the existing tenant leaves and in May 2015, Ms B succeeds in getting a new tenant. The new letting agreement includes a provision that the rents will be subject to VAT.

Ms B will be required to account for VAT on the rents from the new tenant. She will be entitled to a VAT credit in respect of a CGS adjustment. This will be by reference to a proportion of the VAT incurred on the acquisition or development of the property. The input credit in this case will be €250,000 x 16/20 = €200,000 (see Capital Goods Scheme (CGS) - other adjustments for further details).

3 Can the landlord's option to tax a letting apply in all cases?

No. There are restrictions on the option to tax rents. The option to tax cannot apply in the following circumstances:

- Where the property is occupied for residential purposes.
- Where the letting is between connected persons. However, if the tenant is entitled to deduct at least 90% of the tax chargeable on the rent, this restriction does not apply.
- Where the property is occupied by the landlord, or a person who is connected with the landlord. This rule applies whether or not the agreement between an unconnected tenant (who holds the original lease from the landlord) and the person who occupies the property is a letting agreement or any other agreement (for example, a licence) which allows the person to occupy the property (see example below). However, if the occupant is entitled to deduct at least 90% of the tax chargeable on the rent, this restriction does not apply.

Example 4

A's tenant is an unconnected person, but that person sublets the property to C who is in partnership with A in another venture and has a 50% VAT recovery rate.

Since the property is now occupied by a person connected with A who is not entitled to reclaim at least 90% of the tax chargeable on the rent, the option to tax cannot apply.

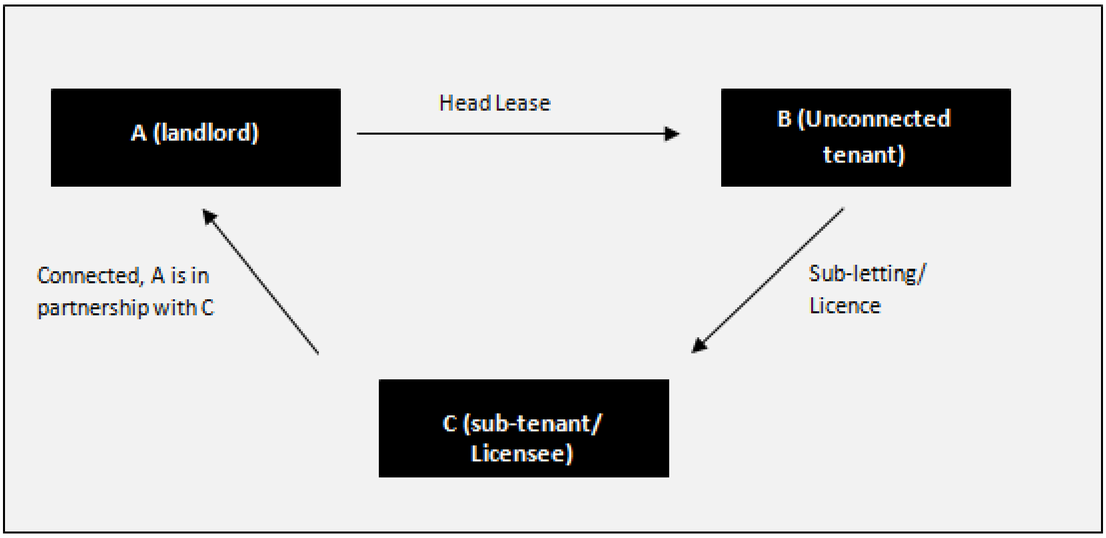

Figure 1: Option to tax cannot apply

4 When is a landlord regarded as connected with a tenant or occupant?

Generally, connected persons can be established, as outlined below. The following list is indicative only. Reference should be made to definition of a connected person for the full definition.

Individuals are connected with:

- their spouses or civil partners
- their relatives (brothers, sisters, ancestors or lineal descendants), or relatives of their spouses or civil partners
- individuals, or spouses or civil partners of individuals with whom they, or their spouses or civil partners, are in partnership
- the settlor or beneficiary of a trust where the individual is a trustee of that trust and vice versa.

Companies, or other bodies of persons, are connected with:

- persons who control that company
- other companies that act in pursuit of a common purpose with the company
- a person or persons with a reasonable commonality of interests who have the power to determine the activities of two companies.

5 VAT chargeable when an option to tax a letting is exercised

All of the consideration attributable to the letting while the option is in effect becomes subject to VAT.

Payments or other consideration received by you prior to effecting the option to tax or after terminating it, for example, a premium or balloon rent payment, are taxable. These payments will be taxable to the extent that they relate to the letting supplied while the option is in effect.

A rent holiday, in other words a rent-free period that is allowed for bona fide commercial reasons, will not require special VAT treatment.

6 What is the VAT treatment of premiums?

A premium is a sum payable in connection with the granting, surrendering, or the assignment of a lease.

Where a freehold equivalent interest is being granted or assigned, the premium is treated as part of the consideration for the supply of the property. The VAT treatment of such a premium will follow the general rules for VAT on supplies of property.

Where the interest in the property is not a freehold equivalent or a legacy lease, the VAT treatment of the premium is outlined as follows:

1. Premium payable by tenant to landlord as consideration for landlord agreeing to grant the lease

The VAT treatment of the payment will depend on whether the landlord has opted to tax the letting in question. Where the landlord has opted to tax the letting, the premium is taxable. Where the landlord has not opted to tax the letting, the premium is exempt.

2. Premium payable by tenant to landlord as consideration for the landlord agreeing to the surrender of the tenant's lease.

The VAT treatment of the payment depends on whether the landlord has opted to tax the letting in question. Where the landlord has opted to tax the letting, the premium is taxable. Where the landlord has not opted to tax the letting, the premium is exempt.[1]

3. Premium payable by a landlord to induce a tenant to enter into a lease; this may be in the form of a payment to assist tenant with cost of fit out.

In merely agreeing to take a lease, a tenant is not providing a service to the landlord. If no other service is involved the payment is therefore not made in respect of the provision of a service by the tenant and no VAT arises.

However, if by taking the lease the tenant is providing a service, that service is taxable. An example of such a service would be a well-known brand proprietor, which provides an advertising service by agreeing to be a tenant in a new shopping complex. In this case the premium is subject to VAT.

4. Premium payable by a tenant (the assignor) to another person (other than the landlord) as consideration for that person agreeing to accept an assignment of the lease. The person to whom the payment is made is usually referred to as the assignee.

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[1] A Capital Goods Scheme (CGS) adjustment may arise where the assignment or surrender occurs during the adjustment period for refurbishments carried out by the assignor. This is separate to the tax status of the premium. In certain circumstances, the CGS adjustment may be avoided by the assignee agreeing to be responsible for the CGS in relation to the refurbishments (See Capital Goods Scheme - other adjustments).

In agreeing to take over the tenant's rights and obligations, the assignee is providing a taxable service to the assignor. The service is subject to VAT at the standard rate.

5. Premium payable to a tenant (the assignor) as consideration for assigning the lease to another person (the assignee).

In assigning his interest in the lease the assignor supplies a service for consideration that is subject to VAT at the standard rate.

7 When is an option to tax a letting terminated?

An option to tax a letting is terminated if:

- you enter into an agreement in writing with the tenant that the rents will no longer be taxable
  or
- you issue a notice in writing to the tenant that the rents will no longer be taxable.

The termination date will be no earlier than the agreement date or the date of receipt of the notification by the tenant.

An option to tax rents will be terminated automatically if:

- you become connected with the tenant[2]
- the property becomes occupied by a person connected with you[3]
- the property is used, or to be used, for residential purposes
- you fail, having claimed the VAT on the acquisition or development of the property, to:

include a written provision for the taxation of the rent in the letting agreement, or issue a document to the tenant stating that VAT is chargeable on the letting.

[2] The option to tax will not be terminated if the occupant is connected, but entitled to claim at least 90% of the tax chargeable on the rent.

[3] The option to tax will not be terminated if the occupant is connected, but entitled to claim at least 90% of the tax chargeable on the rent.

8 What happens if an option to tax is terminated?

If the option is terminated during the adjustment period relating to the property, a CGS adjustment will be due (see Capital Goods Scheme (CGS) – other adjustments). The landlord must account to Revenue for the tax due as a result.

9 What is the difference between a letting and a licence?

In contrast to the supply of a letting service which is exempt from VAT, the supply of a licence is subject to VAT at the standard rate.

While these concepts exist in land law, the difference between a lease and licence for VAT purposes are determined by European Union (EU) guidelines. Specifically, it is determined in accordance with the EU VAT Directive 2006, and the European Court of Justice case law. Each agreement will be determined on its own merits as to whether or not it is a lease or a licence.

However, a lease would generally have the following characteristics:

- The tenant has the right to occupy the property and to exclude all others.
- The tenant will pay a consideration in exchange for this right and the right will usually be for a fixed period of time.