

SUBSALES-SOME SDLT AND VAT POINTS TO WATCH OUT FOR

The basic SDLT relief for subsales is straightforward and is found in FA 2003 Sch 2A (and see also HMRC Guidance on the SDLT pre-completion transactions rules, July 2013) but there are some points to watch out for as well as some VAT points.

Basic Relief

If A contracts to sell to B and B to C with completion taking place by A vesting the legal estate in C direct, C pays SDLT on the consideration C pays to A and B, and B can make a claim to HMRC (under Sch 2A para16) and pay no SDLT.

The same result follows if at completion A vests the legal title in B by way of transfer and B executes a second legal transfer in favour of C.

If B and C are connected then C pays SDLT on the higher of what C pays and what B pays (see Sch 2A para12).

Charities

The subsale relief provisions apply even though C may be a charity.

B contracts to buy land for £1m from A and subsells it on to a charity for the same price. No SDLT is payable. SDLT charities relief in FA 2003 Sch 8 applies.

Agreements to assign leases

A wholly separate (and less pernicious) code applies to agreements to assign leases and FA 2003 Sch 17A para 12B must be referred to.

No sale and leaseback relief

A sale and leaseback is a land exchange within Sch 4 para 5 (see also SDLTM16040) but generally the leaseback element is SDLT free under FA 2003 s57A.

This relief however does not apply to subsales within Sch 2A.

Example

B contracts to buy from A for £10m and subsells on to C, with a rack rent leaseback, for £10m. If B makes a claim, only C pays SDLT on the £10m. However SDLT is also payable on the capitalized rent at 1%.

VAT on acquisition

VAT on subsales raise many issues.

In an appropriate case the relief may be available if B contracts to buy from A and sells to C and takes a leaseback.

Note however if B is buying to let but A is seeking to cease its letting business prior to the sale the TOGC relief is not available.

Notice 700/9/12 reads thus:

6.2 Examples of when a property business can be transferred as a TOGC

— Own a property and have found a tenant but not actually entered into a lease agreement when you transfer the freehold to a third party (with the benefit of a contractual agreement for a lease but before the lease has been signed), there is sufficient evidence of intended economic activity for there to be a property rental business capable of being transferred.

6.3 Examples where there is not a TOGC

— Sell a property where the lease you granted is surrendered immediately before the sale, your property rental business ceases and so cannot be transferred as a going concern — even if tenants under a sublease remain in occupation. When the lease is brought to an end the property rental business carried on by the former freeholder has ceased and cannot be transferred.

Alternative property finance (APF)- SDLT and VAT

If B contracts to buy property from A and transfers it to C as security for a borrowing the transfer to C is a security transaction and exempt from SDLT (see FA 2003 s48(2)(a)).

An Islamic Mortgage (APF) is essentially the same thing.

B contracts to buy an office from A for £3m and needs a “loan” of £1m. Under APF, a financial institution (C) – e.g. a Bank – will buy the freehold under the subsale contract for £1m and let the same back to B with rental rights to reflect the £1m outlay plus interest and the terms (e.g. B may have a buy back option as well as the rental obligations) will ensure that when B has repaid the “borrowing” and interest the financial institution will transfer the freehold back to B.

The APF provisions are in FA 2003 s71A -73CA and these exclude from SDLT the purchase by C of the freehold and the leaseback.

The subsale relief provisions in Sch 2A do not apply if C qualifies for the APF relief and B will simply pay SDLT on the £3m. See Sch 2A para 16(5)(b).

Note no special APF code applies for VAT.

The HMRC view is found in the VAT Finance Manual VATFIN8100.

It reads thus:

VATFIN8100 - Islamic products: purpose of VATFIN8000

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VAT treatment

The central supplies are (i) the gradual sale of equitable interest, and (ii) lease of property. As such consideration for supplies made under this form of arrangement will follow the normal rules for

property. See VAT Notice 708 Buildings and construction, VAT Notice 742 Land and Property and VAT Notice 742A Opting to tax land and buildings.

VATFIN8740 - Islamic products: transfers of a going concern

VAT Notice 700/9 Transfers of a going concern sets out the conditions that must be met if the transfer of a business is to be treated as a going concern. If the conditions are not met then the transfer cannot be treated as a going concern and the normal VAT rules will apply to supplies of assets (note particularly paragraph 2.3.3 of the Notice on consecutive transfers of businesses).

This being the case the VAT position assuming all the parties are VAT elected is B bears input tax on the purchase and will charge C VAT on the £1m. C will charge VAT on the rents. The Tax Editor cannot see there being a VAT charge on the exchange of (approx.) £2m worth of freehold for £2m worth of leasehold interest (*Abbey National BS v Cann* [1991] 1 AC 56 and *Sargaison v Roberts* [1969] 3 ALL ER 1076 and *Arrowtown* [2003] HKCF 46 at [35] and other cases). For good measure B could (in England but not Scotland) carve out a lease and then sell the freehold on to C subject to the lease so there is no offending leaseback as such (see *Ingram v IRC* [1985] STC 835).

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