

TOGC ahead!

Edd Thompson explains when transfer of a going concern treatment applies to business transactions.

A topic tested quite frequently in the Association of Taxation Technicians paper 6 (VAT) examination is that of a business being transferred as a going concern, commonly referred to as a TOGC. The subject of such transfers comes up in a variety of guises – both as part of the ‘short form’ and ‘long form’ questions which make up the paper.

This article aims to present an overview of some of the key points that students – and perhaps rusty tax advisers – need to be familiar with when it comes to a TOGC.

What is a TOGC?

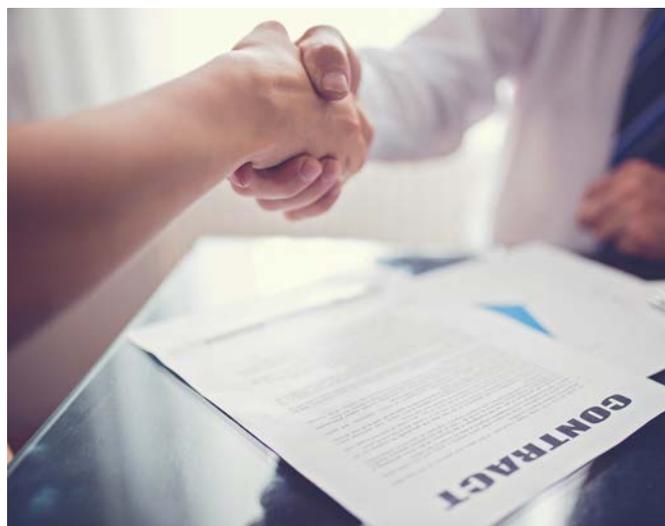
Let’s imagine your client Mario is a plumber. He is approaching retirement age and would like to sell his business. The business itself will comprise assets such as a van, tools and maybe some stock including pipes. Mario has a good reputation and many repeat customers, so he will have valuable goodwill and he also employs one member of staff. If Mario were to transfer the entire business, including the assets, customer list and employee, to another person, how is this treated for VAT?

As mentioned, under VAT law, if a business is sold as a going concern and specific conditions are met, rather than dealing with the sale transaction as a supply for VAT purposes it is disregarded and treated as outside the scope of VAT. So no VAT is charged on the transfer.

Note that the TOGC treatment is not optional. So, to the extent that the conditions are met, the business sale must be treated as outside the scope of VAT. This means anyone purchasing a business should be vigilant; if VAT is charged on a TOGC and it should not have been, HMRC is within its rights to disallow an attempt to reclaim the VAT as input tax.

Key points

- A business sale, if treated as a transfer of a going concern, is outside the scope of VAT.
- Examples of when the transfer of a going concern provisions might apply in a business context.
- HMRC’s *VAT Notice 700/9* has a useful list of the conditions for a TOGC.
- Problems may arise when standard-rated land forms part of the transfer.
- Generally, the seller’s costs are treated as general business overheads.
- VAT will be recoverable by the purchaser on costs if the assets are used to make taxable supplies.



It is also worth noting that, when thinking about a TOGC, we are largely talking about a sale of trade and assets; a transfer of shares in a company will generally be an exempt supply for VAT purposes.

What are the conditions?

Transfer of a going concern treatment applies when the transfer of a business meets particular conditions, but what are they? I point students towards *VAT Notice 700/9* (tinyurl.com/ybnfn52c) because it contains a succinct, bulleted list of the conditions HMRC believes make a transfer a TOGC:

- the assets, such as stock-in-trade, machinery, goodwill, premises, and fixtures and fittings, must be sold as part of the TOGC;
- the buyer must intend to use the assets in carrying on the same kind of business as the seller;
- where the seller is a taxable person, the buyer must be a taxable person already or become one as the result of the transfer;
- in respect of land or buildings which would be standard rated if they were supplied, the buyer must notify HMRC that they have opted to tax the land/buildings by the relevant date, and must notify the seller that their option has not been disapplied by the same date (I will return to this below);
- where only part of the business is sold it must be capable of operating separately; and
- there must not be a series of immediately consecutive transfers of the business.

I will not explore these conditions in more depth here, but suffice to say, much of the time, it is a case of considering these bullets carefully and applying them to the specific scenario(s) presented to state or explain if TOGC treatment applies. Bear in mind, though, that HMRC guidance is its interpretation of the law and not the law itself.

Rental Ltd

Rental Ltd owns a three-storey commercial building and rents out one of these floors to Tenant Co. It decides to sell the building to Property Ltd. The benefit of the existing lease to Tenant Co is also transferred to Property Ltd.

In this example, Rental Ltd has transferred a property rental business and the sale of the commercial building can be treated as a TOGC. It does not matter that only one of the three floors has been rented out, the sale still qualifies for the TOGC treatment.

Property complications

Some of the trickier issues that arise with a TOGC concern land and buildings. A common scenario is property rental businesses. Broadly speaking, it is possible for a building which is transferred with tenants to be a TOGC for VAT purposes. If there are tenants before and after the transfer of a property and the benefit of the lease or leases to the tenants passes to the purchaser, normally we would expect this to be a TOGC. This can even apply when the property is not let out in its entirety.

This is illustrated in the example of *Rental Ltd*.

Another tricky situation can occur when, as part of the transfer, there is 'standard-rated land'. This includes new commercial property, in other words three years old or less, and land and buildings more than three years old over which the seller has applied an 'option to tax'. For such land to form part of a TOGC, the purchaser must opt to tax the property and notify HMRC before the transfer takes place. Otherwise, the standard-rated property is stripped out of the TOGC and VAT must be charged on it (see *Vendor Ltd*).

VAT recovery

A further point worth highlighting is the VAT recovery position on costs associated with a TOGC, such as legal fees and due diligence costs. Students are normally comfortable with the idea that VAT is recoverable on costs used to make taxable supplies, but it is not generally recoverable on those used for exempt supplies. But what about costs used for a TOGC that is not a supply at all?

Case law has helped to develop some principles here. Broadly speaking, the position depends on whether we are

Seller Ltd

Seller Ltd is selling the trade and assets of a discrete business to Buyer Ltd. It has received professional advice and is satisfied that the sale satisfies the TOGC conditions.

Seller Ltd has incurred a significant amount of VAT (£10,000) on professional fees associated with the sale. It should treat the VAT on these costs as general overheads. Because Seller Ltd is a partly exempt business with a partial exemption residual recovery rate of 50% it can recover half of the VAT on these costs – in other words, £5,000.

Planning point

For standard-rated land to form part of a TOGC, the purchaser must opt to tax the property and notify HMRC before the transfer takes place. Otherwise, VAT must be charged on it.

Vendor Ltd

Vendor Ltd is selling a business to Purchaser Ltd. The business qualifies for treatment as a TOGC but the assets of the business include a factory which was built two years ago. Purchaser Ltd does not opt to tax the factory before the transfer takes place.

The factory is standard rated because it is land and buildings that is not more than three years old. Purchaser Ltd has not opted to tax the factory, so it cannot form part of the TOGC. This means that while the remainder of the business transferred will be outside the scope of VAT, VAT must be charged by Vendor Ltd at the standard rate on the factory.

talking about the costs of the seller or the purchaser. Normally, the costs of the person selling the business are treated as general business overheads. Hence, if the seller is partly exempt, VAT is recovered in line with the seller's partial exemption method. On the other hand, for the purchaser, the VAT recovery position usually depends on how it intends to use the assets it is buying. So, if the purchaser will use the assets to make taxable supplies, VAT will be recoverable. If it is using them to make exempt supplies, it will be irrecoverable. Finally, if it is using them to make both, the VAT will be residual.

This is illustrated in the example of *Seller Ltd*.

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Final thoughts

The subject of TOGCs is often tested in ATT paper 6 but that should not cause panic. It is important to become familiar with the main conditions – *VAT Notice 700/9* is a useful reminder of these. In many questions it is then a case of carefully applying the conditions to scenarios presented and ensuring you understand the common trickier issues that can arise – such as transfers including land and buildings.

Finally, as with all exam topics, there is no substitute for a healthy dose of question practice. ●

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