# VAT ON A FORCED SALE – RECEIVERS & MORTGAGEES IN POSSESSION

TAX SPECIALIST **FINOLA O'HANLON** ASSESSES THE VAT IMPLICATIONS THAT MAY ARISE ON PROPERTY SALES WHERE A CREDITOR OR BANK STEP IN TO EFFECT A SALE

The VAT treatment of mortgagees in possession and receivers can be complex, particularly if the property in question is a legacy lease granted under the "old" VAT on property regime, but being transferred under the current regime (which came in on 1 July 2008).

**Supplies of Property - Forced Transfers**

A client with cashflow issues may allocate a property to satisfy a debt, and the case can proceed in a number of different ways. The client may transfer the property to the creditor in satisfaction of the debt which is effectively a sale of the property by an owner/vendor and is treated as such for VAT purposes (see VAT on sale by owner below).

The client may default on the loan and the mortgagee may step in and take possession by way of a Well Charging Order or an Order of Possession, with a view to selling it to repay the loan. This is a VAT supply by a mortgagee in possession, rather than a supply by the mortgagor/owner. Alternatively a creditor may have the right to put in a receiver who may look at recovering cash by disposing of property held by the debtor, or letting it in the short or medium term to generate cash to service the debt (see VAT on sale by a mortgagee in possession or receiver below).

**VAT on Sale by Owner**

If the property is transferred to satisfy a debt it is effectively a sale and the usual VAT rules apply. The fact that the consideration is being paid by way of forgiving a debt rather than a cash payment should not impact on the VAT treatment.

If a freehold or freehold equivalent is sold and the property is new, the supply is subject to VAT. If the property is no longer new there will be no supply for VAT purposes unless the parties opt to charge VAT. Generally a property will be "new" if it was completed within the last five years and (in the case of a second supply post completion) if it has been occupied for less than two years.

It will be in the vendor's interests to charge VAT if he has an exposure to adjustment under a capital goods scheme (CGS). If an input credit was claimed when the vendor bought the property, and the property is within its 20-year "CGS life" then an adjustment under the CGS scheme will arise if a sale is exempt from VAT. Any VAT cost may be a serious issue for a vendor transferring in satisfaction of a debt (as there will be no sales proceeds to pay the VAT).

The purchaser will acquire the property and begin a new 20-year CGS period in relation to the property, and his entitlement to a VAT input credit will depend on the use to which he puts the property.

### VAT on Sale by Mortgagee in Possession or Receiver

The Revenue Commissioners have published some guidance on the correct tax treatment of transfers by mortgagees in possession, such as the article in Guidance Note Tax Briefing Issue 10 July 2010 on the VAT treatment of forced sales.

If the mortgagee in possession of a property sells or leases the property he makes the taxable supply as a taxpayer in his own right and his VAT position is determined accordingly. A receiver is different from that of a mortgagee in possession in that a receiver is acting as agent of the borrower, and therefore stands in that borrower's shoes, but the two roles are treated in a similar way for VAT purposes.

### Legacy Leases from the pre-2008 Era

The client may hold a leasehold rather than a freehold interest in a property which is securing a debt. If a lease was created before 1 July 2008 (the date the new VAT on property rules came into effect) and the leased property is in use in a business, it will be a "legacy lease" and special rules apply (S. 95(1)(b) Value Added Tax Consolidation Act 2010). If the lease was a long lease under the pre-2008 regime (i.e. an interest for more than 20 years) then the grant of the lease would have been subject to VAT at the rate that applied to goods (13.5%) on the capitalised value of the lease. The surrender or assignment of a legacy lease is regarded as a supply of immovable goods if it occurs within a period of 20 years from the later of two dates; (i) the original grant of the lease or (ii) the most recent assignment or surrender before 1 July 2008.

If the tenant was entitled to an input credit for any VAT charged on the acquisition of the legacy lease (or on a later development of the property) he will have a VAT adjustment (similar to a CGS clawback) on any surrender or assignment within the 20-year period. If the tenant had no entitlement to deduct any VAT paid on the grant of the lease, the assignment or surrender of the lease is exempt from VAT, but the parties can jointly opt to tax. If they opt to tax, no VAT adjustment will arise (so the vendor will not face a VAT cost).

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Where a legacy lease is supplied by a mortgagee in possession or a receiver and he does not opt to charge VAT on the assignment of the lease then there may be a clawback of VAT under the capital good scheme and the mortgagee in possession or receiver will have to pay the VAT clawback to the Revenue Commissioners (S. 76(2) Value Added Tax Consolidation Act 2010). If the mortgagee in possession or receiver does opt to charge VAT on the transfer then no clawback will arise.

In order for a mortgagee in possession or a receiver to make an informed decision as to whether to pay any clawback that may arise on the sale or assignment of an asset, or charge VAT on the sale or assignment, he will need to review the VAT history of the assets being supplied. In many cases the borrower will be uncooperative in terms of supplying information and without a VAT history the mortgagee in possession/receiver may not be able to determine the VAT position. As this problem is becoming more common Revenue indicated in e-Brief 16/12 that they will assist if they can. The Revenue Operational Manual 04-02 indicates that:

"Revenue is satisfied that, where... information is available in Revenue records, it may be disclosed to an MIP/receiver to enable him... to meet his... obligations under the VAT Acts....."

### Conclusion

As there continues to be a significant level of unstable debt in the economy we can expect to see more and more transfers of property arising from loan/debt default and an increase in the number of clients divesting themselves of property (or being divested) to cover debts. The taxation implications of such transactions should be considered in detail to ensure that any VAT arising is correctly accounted for, and returns filed when due.

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