VAT and barter transactions

Tax voice



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Barter transactions are more common than many assume – Marc Selby sets out the key VAT issues for practitioners to take into account

Property transactions often involve the giving or receipt of consideration other than, or in addition to, money. These are barter transactions and it is important for those advising the parties to identify any non cash consideration, to analyse the VAT implications and to ensure that there are no unexpected VAT costs by appropriately documenting the transactions.

The following are examples of barter in the context of property transactions (but the list is by no means exhaustive):

1. An exchange of property interests, such as a surrender of an old lease in exchange for the grant of a new lease or a sale and leaseback transaction.
2. The purchase of a property where the consideration comprises or includes the buyer, or an associate of the buyer, agreeing to carry out works on land retained by the seller.
3. The supply by a tenant entering into a new lease of services in consideration for the tenant being granted a rent free period.

In the first instance it is necessary to establish whether a party who is acquiring land or an interest in land, and who is doing something in addition to making a cash

payment, is making a supply for consideration. For example:

- Works which a buyer carries out on land retained by the seller solely for the buyer's benefit, eg the installation of service media on land retained by the seller for the benefit of the buyer's land, would not be consideration for a supply by the buyer;
- Generally, the grant of a rent-free period does not count as consideration for a supply by the tenant, eg a rent free period during which the tenant will be fitting out the premises to its specifications. However, a rent free period can constitute consideration where the tenant is providing a benefit to the landlord (in addition to accepting the grant of the lease), such as carrying out improvements to the building, see HMRC's VAT, Supply and Consideration Manual, para VATSC4800.

Having established that the buyer or tenant is providing non cash consideration, it will be necessary to ascertain the VAT status of each party's supply. For example:

- Each party could be making a VAT exempt supply, eg the surrender of an existing lease of a building containing only dwellings in exchange for a new (longer) lease of the building (whether or not there is also cash consideration).
- Each party might make a taxable supply, eg the sale of the freehold of a newly constructed commercial building and the leaseback of part of the building from a buyer who opts to tax the building before granting the lease back.
- Each party might make a supply of a different status, eg the seller could sell a commercial investment property subject to leases with that transaction being a transfer of a going concern (and thus outside the scope of VAT), with the buyer opting to tax the property and granting a lease of a commercial part of the building back to the seller (and thus making a taxable supply).

When advising a party to a barter transaction, the following should be noted:

- Non-cash consideration which is received for a taxable supply must be valued. For VAT purposes the value of the supply is such amount as, with the addition of the VAT chargeable, is equal to the consideration, VATA 1994, Section 19. So, the VAT liability of the person who provides non cash consideration will be determined by reference to the value which, together with the VAT chargeable, that person receives as consideration for the supply.

- The value of the consideration received for the supply is determined subjectively by reference to the value assigned to the supply by the recipient of the supply see *Naturally Yours Cosmetics Limited v C&E* (No2) [1988] STC 879. Generally, this will be the value of the payment which the recipient of the supply would have expected to make if the consideration for the goods or services which he or she receives had been in money.
- A party who receives cash consideration in a barter transaction should ensure that the value on which that person accounts for VAT includes the non cash, as well as the cash, consideration.
- In principle, where unconnected parties are dealing on an arm's length commercial basis, it is likely that the total value of the supplies by each party will be of equal value.
- Ideally, the value of each party's supply should be expressly agreed and confirmed in the contract, although such an agreement will not bind HMRC. HMRC may be more likely to scrutinise the value of the supply in cases where each party is making a supply of a different status to the other, eg where one party is receiving an exempt supply in exchange for a standard rated supply by the other party.
- Where a party is making a supply which is taxable at the standard (or reduced) rate, it is important to ensure the value attributed to the supply in the contract is exclusive of VAT and that the contract requires payment of such VAT by the recipient of the supply, otherwise the value of the supply will be VAT inclusive (and the person making the supply will effectively bear the VAT charge).
- The contract should also provide for the issue of VAT invoices by each party who is making a taxable supply and for payment by the recipient of the supply of the VAT which arises from the supply.
- If and to the extent that each party is making a taxable supply for non cash consideration and the value of such supplies by each party is equal, the VAT accounting can be dealt with by the issue of VAT only invoices, with the VAT payable by each party being set off, thereby avoiding the need for each party to make a cash payment of the VAT due in respect of the non cash consideration received.
- Each party making a taxable supply will need to establish the tax point for the supply, since this will determine when VAT must be accounted for to HMRC. Generally, a tax point will arise on receipt of payment, including non cash consideration, for example in a sale and leaseback transaction (assuming each party is making a standard rated supply) the tax point for each party's supply

will normally occur on completion of the transaction. However, a tax point can arise at an earlier stage, eg on the issue of a VAT invoice prior to the completion date.

A suggested precedent for a VAT clause in a sale and leaseback transaction where each party is making standard rated supplies is set out in an Appendix to this article. This precedent will, of course, need to be adapted according to the circumstances of each transaction, in particular where one party is making a supply which is of a different VAT status to the other.

Barter can arise even in apparently straightforward property transactions, such as a sale and leaseback. It is important that the VAT implications of such transactions are properly addressed and documented. It is hoped that the commentary set out in this article, and the precedent which follows, will assist the reader.

Appendix

Suggested precedent for a VAT clause for a sale and leaseback transaction where both the Seller and the Buyer are making standard rated supplies, with the Buyer agreeing to carry out works to premises leased back.

X.1 The Seller and the Buyer warrant and confirm to each other that:

X.1.1 they have opted to tax the Property for VAT with effect from a date on or before the Completion Date and that their respective options to tax have been duly notified to HMRC; and

X.1.2 they are duly registered for VAT.

X.2 The Seller and the Buyer consider that:

X.2.1 the sale or transfer of the Property by the Seller to the Buyer pursuant to this Agreement will be a supply by the Seller to the Buyer;

X.2.2 the carrying out by the Buyer of the Works and the grant of the Lease to the Seller pursuant to this Agreement will be supplies by the Buyer to the Seller;

X.2.3 the supply by the Seller to the Buyer will, to the extent of the Purchase Price (which is exclusive of VAT chargeable), be for consideration in cash and will, to the extent that its value exceeds the Purchase Price, be for non monetary consideration; and

X.2.4 for VAT purposes the value of the supply by the Seller, to the extent that it exceeds the Purchase Price, and the value of the supplies by the Buyer will be [£] (exclusive of VAT payable).

X.3 Upon completion:

X.3.1 the Seller shall issue to the Buyer a VAT invoice in respect of the Purchase Price payable and the Buyer shall pay the VAT chargeable (together with the Purchase Price) upon completion; and

X.3.2 each of the Seller and the Buyer will issue to the other a VAT only invoice with the amount of the VAT payable calculated by reference to the value of the supply made by the Seller (to the extent that it exceeds the Purchase Price) and the value of the supply made by the Buyer (as the case may be) referred to in clause X.2.4 above; and

X.3.3 the amount of VAT payable by the Buyer in the VAT invoice issued by the Seller under clause X.3.2 above being equal to the amount of VAT payable by the Seller in the VAT invoice issued by the Buyer under clause X.3.2 above, each party agrees to the set off of such VAT due from the other such that no cash payment will be required to be made between the parties in respect of such VAT.