

**EXPLANATORY MEMORANDUM TO
THE VALUE ADDED TAX (BUILDINGS AND LAND) ORDER 2011**

2011 No. 86

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs and is laid before the House of Commons by Command of Her Majesty.

This memorandum contains information for the Select Committee on Statutory Instruments.

2. **Purpose of the instrument**

- 2.1 This Treasury Order amends, with effect from 1st March 2011, Schedule 10 ("Schedule 10") to the Value Added Tax Act 1994 (c.23) ("the Act"). The amendments made by this Order have two purposes.

- 2.2 The first provides further facilitation in the use by businesses of the option to tax supplies of land and buildings. In the absence of the option to tax such supplies would fall to be exempt from Value Added Tax ("VAT") and this would impact on the ability of businesses to claim credit for VAT incurred on supplies made to them that are used for making the supplies of land and buildings concerned.

- 2.3 The second simplifies the 'change in use' provisions for new buildings that were zero-rated as intended to be used for a relevant residential or relevant charitable use and for whom, within a period of 10 years, the building ceases to be used for a relevant purpose. The current provisions are unfair in that they produce different tax results depending upon how the change in use of the building came about even though the same amount of the building, in percentage terms, is still being used for a relevant use.

- 2.4 The new provisions will produce the same tax charge based upon the amount of relevant use still taking place in the building irrespective of circumstances in which the change in use comes about.

3. **Matters of special interest to the Select Committee on Statutory Instruments**

- 3.1 None

4. **Legislative Context**

- 4.1 Section 4(1) of the Act provides that VAT is chargeable on supplies of goods or services made in the United Kingdom where it is a taxable supply made by a taxable person in the course or furtherance of a business carried on by that person.

4.2 Group 5 of Schedule 8 to the Act relieves new buildings that are intended to be used solely for a relevant residential or relevant charitable purpose of VAT on their construction or acquisition. A building that does qualify for that relief is expected to be used solely for that qualifying purpose for a period of, at least, 10 years following completion of the building.

4.3 Subject to the exclusions mentioned therein, Group 1 of Schedule 9 to the Act (“Group 1”) exempts from VAT the grant of any interest in or right over land or of any licence to occupy land or, in relation to land in Scotland, any personal right to call for or be granted such interest or right.

4.4. Part 1 of Schedule 10 to the Act relates to the option to tax land. Where a business opts to tax land or a building, supplies of it made by the business (which would otherwise be exempt from VAT by virtue of Group 1) are chargeable to VAT at the standard rate of 20%. Part 1 Schedule 10 contains the main rules for the operation of an option to tax. This includes an anti-avoidance provision at paragraphs 12 to 17, under which an option to tax has no effect where certain conditions apply.

4.5. Part 2 of Schedule 10 provides for self supply that has the effect of a ‘claw back’ of some or all of the relief mentioned at 4.2 if the building in question ceases to be used solely for a relevant residential or relevant charitable use within that 10 year period or if that use decreases.

4.6 This Order makes three amendments to Schedule 10. Two of the amendments are to Part 1 and are designed to facilitate the use of the option to tax by businesses. The third amendment is to Part 2 of the Schedule (the Change of Use) provisions. In particular, the amendments made by the Order-

- exclude certain transactions from the effect of the “anti-avoidance provision” and allow developers of land to tax supplies of buildings where they intend to be in occupation of minor parts for making exempt supplies (see paragraph 15 of the Schedule which defines “exempt land” for the purposes of the provision);
- exclude occupation by reference solely to automatic teller machines (ATMs) from being treated as occupation for the purposes of the provision. This includes a consequential amendment to paragraph 16 of the Schedule); and
- replace the two methods of calculating a tax charge with a single method that applies in all circumstances that a change in use occurs.

4.7 The first amendment to the Schedule amends paragraph 15 by substituting a new sub-paragraph 3A. Sub-paragraphs 15A(1)(b)(ii), (2) and (4) are also amended. The meaning of “exempt land” for the purposes of the anti avoidance rules is amended as follows:

- occupation by grantors or persons connected to grantors is not to be treated as occupation where the occupation amounts to no more than 2% by area of any building included in the grant; and

- occupation of land which is solely in the form of an ATM is excluded from being treated as occupation .

4.8 The second amendment is a consequential amendment. Sub-paragraph 16(7), under which occupation by reference to an ATM is treated as occupation for eligible purposes, is repealed.

4.9 The third amendment to the Schedule amends paragraphs 35 to 37 by substituting new paragraphs 35 to 37.

5. Territorial Extent and Application

5.1 This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

David Gauke MP has made the following statement regarding Human Rights:

In my view the provisions of the Value Added Tax (Buildings and Land) Order 2011 are compatible with the Convention rights.

7. Policy background

• What is being done and why

7.1 The option to tax land afforded by Schedule 10 of the Act is politically and legally important because of its relevance to the commercial property sector. It is also by its nature one of the most complex and difficult parts of the VAT legislation, arising in part from the complexities of English and Scottish land law and because it contains extensive anti avoidance legislation.

7.2 Following the introduction of the Value Added Tax (Buildings and Land) Order 2008, 2008 No.1146, which came in force on 1 June 2008, there has been dialogue with business to ensure the re-written Schedule 10 is achieving its objectives and not creating unnecessary burdens for business.

7.3 The amendments now being made are part of an on-going programme to simplify Schedule 10 and ensure the anti avoidance provision is better focused on tax avoiders. Two of the changes being made are to the “exempt land” test (part of the anti avoidance provision). The relief provided is similar to that provided to “financiers”, under The Value Added Tax (Buildings and Land) Order 2010, 2010 No, 485) from 1 April 2010. The following changes are made:

- The anti avoidance test will no longer be “tripped” where the person making a grant of the land (the grantor) also intends to be in occupation of a minor or insignificant part of the land. A “minor” part of the land means no more than 2% of the area of any building included in the grant. This will prevent an option to tax from being disapplied in cases where there is

no intention to gain a tax advantage and mean that additional VAT costs, incurred by the grantor as a result of the disapplication, will be avoided.

- Occupation of the land which is solely by way of an automatic teller machine is no longer to be treated as occupation for the purposes of the provision and result in an option to tax being disapplied. A similar effect is currently achieved by treating such occupation as being for “eligible purposes” under sub-paragraph 16(7) of the Schedule. This sub-paragraph is to be repealed..

7.4 The ‘change in use’ provisions afforded by Schedule 10 are important because the zero-rate can only be applied to the construction and first supply of a building used for a relevant residential or relevant charitable purpose. When that use ceases, in full or in part, that building ceases, to that extent, to be eligible for relief and VAT must be applied. This provision applies a fair and reasonable ‘claw back’ of the VAT relief by way of a self-supply.

7.5 Following scrutiny of the existing legislation, the Government considers it to be unfair as it produces different results according to how the change in use came about, and has ambiguities that are at least confusing and at worse, have the potential to be exploited for tax avoidance purposes.

7.6 The amendments to the legislation will provide fairness, certainty and consistency. It will remove any ambiguity and so will minimise any opportunity for tax avoidance.

- **Consolidation**

7.7 Not applicable

8. Consultation outcome

8.1 The amendments to Part 1 of the Schedule are the result of continuing consultation with business and trade bodies on the simplification of Schedule 10 and, in particular, the anti-avoidance provision. Consultations on the draft legislation over a four week period were also undertaken in relation to both the amendments to Part 1 and Part 2 of the Schedule. Those consulted included members of trade organisations representing the property industry and representatives of UK charities including the Charities Tax Group. The measures were welcomed by those responding.

9. Guidance

9.1 An Information Sheet will be issued at the time the SI is laid. A revised version of Notice 742A Opting to tax land and buildings and Notice 708 Buildings and construction will also be issued as soon as possible.

10. Impact

10.1 An Impact Assessment has not been prepared for this instrument as it has negligible impact on business, charities, voluntary bodies or the public sector.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 To minimise the impact of the requirements on firms employing up to 20 people, the approach taken is to simplify the mechanics of the option to tax as far as possible.

12. Monitoring & review

12.1 The working of the legislation will be monitored jointly with business and the legislation may be amended accordingly to ensure that it is fit for purpose.

13. Contact

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