

Talk Tax – Sale of Going Concern Business

FS: What are the VAT implications on the sale of a business?

CEO: For VAT purposes, a business or a commercial activity that is operated continuously or regularly is known as a taxable activity. When a taxable activity (business) is sold by a VAT registered person, the supply will be subject to Value Added Tax (VAT) at nine percent (9%). However, a supply may be taxed at zero percent (0%) if it involves the sale of a taxable activity as a going concern to another registered person.

FS: Can you elaborate on the difference?

The sale of a taxable activity or assets is treated as an ordinary taxable supply. It is treated in the same way as the supply of trading stock. Therefore the seller must include 9% VAT in the sale price unless it can be zero-rated.

When a supply is zero-rated, two things must exist and these are (1) the buyer and seller must be registered persons and (2) the business must be operating at the point of transfer and the buyer must be capable of running it.

The following is a guide that can be used to determine whether a supply is taxable at 9% or 0%:

- A business is operating but the buyer is not registered, 9% VAT applies ;
- If a business is sold to another registered person but has ceased operations at the time of sale, 9% VAT applies
- Assets of a business sold, 9% VAT applies;
- A business is sold as a going concern where both the buyer and seller is registered for VAT, 0% VAT applies;

FS: What is a 'going concern' for tax purpose?

CEO: The term 'going concern' is not defined in any tax law. Therefore the Authority relies on the ordinary concept under which a business that is being sold operates right up to the date of settlement. It could be sold on an as-is basis or walk out - walk in basis but the main thing is that the buyer is able to continue operations without interruption. This means that the sale should include all or most of the things that are necessary to enable the taxable activity to continue operating before and after the day of sale. Only the legal ownership of the business changes.

FS: How does FRCA determine that a business was sold as a going concern?

CE: A business can only operate normally when it has certain assets. For tax purposes, the transfer of assets which are central to the taxable activity are indicators that a business is sold as a going concern. Some of the issues that the Authority considers are listed below-

- (1) transfer of legal ownership of the premises or right to use the premises – this is usually stated in the sale and purchase agreement;
- (2) agreement between the buyer and seller that the business is a going concern - this must be stated in the sale and purchase agreement or confirmed in writing by both parties;

- (3) the taxable activity must be operating at the settlement date;
- (4) transfer of all assets needed to run the business – these would include customer lists, special equipment/tools etc. - a description of the assets being transferred will normally be included in the sale and purchase agreement;
- (5) transfer of employees – employees are needed to run a business therefore information on arrangements made for continuing employment of existing employees must be included.
- (6) transfer of goodwill - even if goodwill is not specifically mentioned, it may be included in the transfer of assets. e.g. there may be an exclusive right to use a vendor's name or a transfer of clientele.
- (7) transfer of business license to enable the smooth continuity of such taxable activity without interruptions e.g. the sale of a hotel may involve the transfer of a liquor license.

FS: What if only part of a business is sold?

CE: Such supplies are taxable and charged with VAT at 9%. However if that part is capable of separate operation, meets the tax requirements of a going concern and is sold to another VAT registered person, the supply is taxed at 0%.

FS: What is the process for applying for VAT to be zero-rated on sale of a Going Concern business?

CEO: There is no legal requirements for registered persons to apply for approval to zero-rate a supply of goods or services. However, in relation to the sale of a going concern, registered persons are encouraged to seek advice from us or their tax agent or representative. This is important because although general rules are provided, whether a going concern exists or not and whether a sale is a going concern or not are decided on a case by case basis. A person may apply in writing for tax advice and must attach all the relevant details.

FS: What if a person does not apply for advice and zero-rates a supply?

CE: VAT is a self- assessment system and it is important for registered persons to know how the law applies to them. Self-assessment means that they calculate the tax to pay and account for it in returns. However, they face the risk of audit and will be required to pay the VAT component, if the information reported is found to be false. Where it is established at a later date that any of the information was false or the arrangement was entered into for the purpose of avoiding tax, the supplier will be required to pay the VAT that should have been paid, even though no VAT was charged. The total value of the supply will be treated as VAT inclusive.

FS: Is a site inspection conducted for every request?

CE: If a request for tax advice is received, wherever possible, our auditors will conduct a site visit, after which FRCA will provide a formal written notice, advising on the tax rate that may apply (9% or 0%) based on the available information.

FS: What else is the seller required to do when a business is sold as a going concern?

CEO: When a business is sold as a going concern, VAT on the supply must be accounted for in the taxable period in which the sale took place. If the person will cease to be a registered person, the person must file a final VAT return and account for VAT on the sale of the taxable activity in that return.