

Amended legislation could see landlords liable for VAT on leasehold improvements affected by tenants

The 2017 Draft Taxation Laws Amendment Bill and Draft Tax Administration Amendment Bill, clarifying the Value Added Tax (VAT) Act treatment of leasehold improvement, were recently released for comment.



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“A recent proposed amendment to the VAT Act may result in landlords being liable for VAT on leasehold improvements affected by their tenants,” says Christo Theron, chairman of the SAICA VAT Sub-Committee. “This may result in a nasty surprise for a landlord that is not aware of the potential new dispensation.”

In practice lessees are often required to affect improvements to the leased property, commonly known as leasehold improvements.

“Such improvements are normally for the account of the lessee with no right of recovery from the lessor. Until recently the VAT implications of arrangements of this nature were unclear. New proposed amendments to the VAT Act have clarified the issue in some respect, effectively shifting the VAT liability to the lessor,” added Theron.

Lessee will not be liable

In terms of the proposed new rules the lessee will not be liable for any VAT on leasehold improvements affected, although in law such improvements are effectively supplied to the lessor (the improvements becoming part of the property owned by the lessor).

“The lessor is not so lucky, he says. “The new proposed rules determine that the lessor will be liable for VAT on the value of the improvements. The good news is that the VAT will only be payable to the extent that the property is not used for taxable purposes such as, for example, for VAT exempt residential accommodation. For instance, where a lessee erects a building on land owned by a lessor and erects a building consisting of office space and residential accommodation (e.g. a penthouse), VAT will only be payable by the lessor on the value attributable to the penthouse with which VAT exempt residential accommodation will be supplied.”

“The current proposed wording of the draft legislation is slightly obscure and will need to be tidied up, but the intention is clear. The new rules will only apply with effect from 1 April 2018. In the interim landlords should be aware of the future consequences of entering into such arrangements. You have been warned.”

Comments on the draft legislation are due by 18 August 2017. Submit any comments on the matter to SAICA via email at taxcomments@saica.co.za.

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