

The tax treatment of rent-to-buy schemes

Part 22-01-03

This document should be read in conjunction with sections 97, 118, 120, 540, 639 and 641 of the Taxes Consolidation Act 1997

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1. Executive summary

This manual provides guidance on the treatment for income tax, corporation tax, capital gains tax and stamp duty of 'rent-to-buy' and similar schemes. These are schemes devised by builders or developers to provide an incentive for individuals to purchase a property by giving them the opportunity to live in the property for a trial period before deciding whether to purchase that property and by discounting the purchase price of the property in certain situations.

1.1 Each case depends on its own facts

Because there are a variety of arrangements, each case is decided on its own facts and circumstances. This guidance is of a general nature only. The structure of each scheme and the legal form of its transactions will usually determine the tax treatment of the parties to the transactions. Arrangements which appear similar may have different tax consequences.

The legal form of a transaction is not necessarily the determining factor. Revenue may need to look to the substance of the transaction in deciding on the appropriate tax treatment. For example, in certain cases where a licence was said to exist, case law has established that the label put by parties on their relationship is not conclusive. It may be necessary to look behind that label to establish the intention of the parties and the true nature of their relationship.

1.2 Examples of types of arrangement

This manual outlines some of the tax consequences for both the seller and buyer that are likely to result from three different types of arrangements. The manual is for general guidance and should not to be taken as definitive or exhaustive. The arrangements considered are:

- Occupation under a letting agreement;
- A caretaker's agreement, where the occupier pays a deposit rather than rent;
- A payment for an option to purchase a property.

1.3 VAT Treatment

The VAT treatment of 'rent-to-buy' schemes is outlined in the [Rent to Buy Scheme](#) area of the Revenue website. The VAT treatment is not relevant in determining the treatment under other tax heads.

2. Rent-to-buy: potential buyer occupies the property under a letting agreement

Where the person occupying the property decides at some stage within a pre-agreed period to purchase the property, the purchase price is reduced by some, or all, of the rent that has already been paid. The purchase price may be further discounted to reward early purchase. Usually, any rent that has already been paid is not refunded where the person renting decides not to purchase the property. As walking away from the arrangement means the rent paid is lost, there is an incentive for the person to go ahead with the purchase.

(a) Seller

Where the person renting out the property is a builder or developer, section 641(2)(b) Taxes Consolidation Act 1997 (TCA) states that land (or an interest in land) that is held as trading stock can only cease to be trading stock if the particular trade is discontinued. This means that the option to treat trading stock as fixed assets is not available to builders or developers, whose trading stock is residential property. Section 641(2)(a) TCA prevents rent received in those circumstances from being treated as a trading receipt. Where such property is rented out, the rental payments are Case V rental receipts. However, the eventual proceeds of a sale of the property will be a Case I trading receipt and not a capital receipt from the disposal of a fixed asset.

During the period when the property is occupied by the tenant, interest payments on a loan used to finance the development of the property become a Case V expense deduction under section 97(2)(e) TCA instead of a Case I trading deduction.

On sale of the property, the trading receipt will be the net amount received by the seller from the buyer for the purchase of the property, i.e. after any discount given to the buyer, for example, for rent previously paid or for early purchase.

For companies and the charge to corporation tax, Case V (rental) profits are taxed at the 25% non-trading rate while Case I (trade) profits are taxed at the 12½% trading rate. In the case of close companies, any Case V income is considered in determining whether a surcharge on undistributed estate income applies.

(b) Buyer

Any rent paid by the buyer or any discount received by the buyer for rent paid (or for early purchase) is not regarded as part of the cost of the property and will not be taken into account in determining the cost of the property for **Capital Gains Tax** purposes.

A lease of a residential property for a term not exceeding 35 years, or for any indefinite term, is exempt from Stamp Duty, where the rent does not exceed €40,000 per annum (€30,000 in respect of leases entered into before 25th December 2017).

3. Rent-to-buy: occupation of the property other than under a letting agreement and where a deposit is paid by a potential buyer instead of rent (e.g., a caretaker's agreement)

The deposit may be paid up-front or by instalments over a pre-agreed period.

(a) Seller

Where the prospective buyer pays a non-refundable deposit towards the purchase price of the property, that deposit will be a Case I trading receipt when it is received. This applies whether the deposit is paid as a lump sum or by instalments, or whether or not the person goes ahead with the purchase of the property. The balance of the purchase price will also be a trading receipt if, and when it is received.

(b) Buyer

Where the person occupies the property under a caretaker's agreement instead of a letting agreement, that person is potentially assessable to 'benefit in kind' (BiK) on the benefit of rent-free occupation of the property as the creation of a caretaker agreement establishes a 'master/servant' or 'employer/employee' relationship between the seller and the prospective buyer. The BiK charge arises where a body corporate (section 118(1) TCA 1997) or any other employer (section 120 TCA 1997) provides living accommodation for a person employed by it in an employment. The BiK assessable on the caretaker/employee is the open market rent of the property together with any expenses connected with the property borne by the employer, less any rent payable by the employee.

The deposit is treated as part of the cost of the property for Capital Gains Tax purposes.

4. Rent to buy: potential buyer pays for an option to purchase the property in the future

The option payments may be paid up front or by instalments over the pre-agreed period.

(a) Seller

Where the prospective buyer pays for an option to purchase the property, for example, at a pre-agreed price and/or within a pre-agreed timeframe, that payment is treated as a Case I trading receipt when it is received. Section 641(2)(a) TCA 1997 treats any consideration (other than rent or an amount treated as rent) for the disposal of an interest in land as a consideration for the disposal of trading stock and, thus, a trading receipt. Section 639(2) TCA 1997 states that an option, or other right, to acquire or dispose of any interest in any land is deemed to be an interest in the land. Thus, the grant of such an option is treated as the disposal of an interest in land and as a trading transaction. This applies whether the payment is paid as a lump sum or by instalments or whether or not the person goes purchases the property. Where the payment for the option reduces the purchase price, that discounted purchase price will be a Case I trading receipt if and when it is received.

(b) Buyer

Where the person occupies the property under a caretaker's agreement instead of a letting agreement, that person is potentially assessable to 'benefit in kind' as outlined in paragraph 3.

For Capital Gains Tax purposes, the exercise of an option to purchase a property and the associated purchase of the property are treated as a single transaction (section 540(4) TCA 1997). Therefore, the payment for the (exercised) option forms part of the cost of the property.

A liability to Stamp Duty can arise on the grant of an option to purchase property. The duty is chargeable on the amount paid for the option at the rates of duty applicable to non-residential property.