VAT and the Capital Goods Scheme

This document should be read in conjunction with sections 63, 64 and 94(1) of the VAT Consolidation Act 2010

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Introduction

This guidance outlines the meaning and application of the Capital Goods Scheme (CGS) which was introduced with effect from the 1st July 2008.

For information on the VAT treatment of transitional freehold properties , please see 'Transitional properties - freehold or freehold equivalent interests held prior to 1 July 2008'.

Similarly, for information on the VAT treatment of legacy leases, please see 'Transitional measures applying to Legacy leases'.

1. The Capital Goods Scheme (CGS)

The Capital Goods Scheme (CGS) is a mechanism for regulating the amount of Value-Added Tax (VAT) reclaimed over the VAT-life (adjustment period) of a capital good. For VAT purposes a capital good is a developed property.

The scheme operates by ensuring that the VAT reclaimed reflects the use to which the property is put over its VAT-life.

1.1 How does the CGS operate?

The normal rules for reclaiming VAT apply. The CGS is a mechanism for adjusting the amount of VAT you have reclaimed over the VAT-life of a capital good. It requires an annual review of the use to which the capital good is put. Where there is a change in the proportion of use for taxable purposes for any year in comparison with the use during the initial 12 months (initial interval), an adjustment of a proportion of the VAT reclaimed will be required.

At the end of the initial interval following completion or acquisition (where the property is acquired following completion), you must review the amount of VAT reclaimed on the acquisition or development of the property. If the proportion of taxable use of a property during that 12-month period differs from the proportion of the VAT reclaimed on the acquisition or development of that property, then an adjustment is required.

If too much VAT has been reclaimed, you must pay back the excess. If too little VAT has been reclaimed initially, you are entitled to claim the deficiency as an input credit.

This adjusted amount reclaimed for the first 12 months is the benchmark figure for comparison purposes under the scheme, for the remainder of the VAT-life of the property.

The annual adjustments will reflect the difference between the use in the initial interval and the use in the year being reviewed. Ultimately, the proportion of VAT reclaimed following all annual adjustments will reflect the actual use of the property over the adjustment period or VAT-life of the property.

It is important to note that for the majority of businesses these CGS reviews will have no effect. For example, if a company reclaims all of the VAT charged on acquisition or development, and uses the property for wholly taxable activities during the adjustment period then no adjustments will arise.

1.2 When does the CGS apply?

The Capital Goods Scheme (CGS) applies, when you:

- have been charged Value-Added Tax (VAT) on the acquisition or development of a property

  and

- are engaged in business.

If you acquire or develop a property in these circumstances you are known as a capital goods owner and will be referred to, for the purpose of this section, as the owner.

CGS also applies to transitional properties and the owner of such property is also known as the capital goods owner.

However, in the application of CGS to immovable goods and interests in immovable goods that are transitional properties, certain elements of the CGS are disregarded in respect of the person who owns those immovable goods or holds an interest in those immovable goods on 1 July 2008. These elements are the interval-based adjustments, the big swing rule (but see below**), and the opportunity for a landlord to claim a credit for residual VAT when he exercises an option to tax a letting of a property that had previously been exempt.

If a development is completed on or after 1 July 2008, and it is a refurbishment for VAT purposes then these elements of the CGS mentioned above are not disregarded in respect of that refurbishment.

**Where on or after 23 February 2010, a transitional property is used for the first time or there is a change of use in the property, the big-swing test will apply to such properties. The owner of such a property will be obliged to make a big-swing adjustment if the first use or the changed use of that property results in a swing of more than 50 percentage points.

Where there is a transfer of ownership of a transitional property within its VAT-life, the CGS adjustments relating to supplies, apply to that transaction. If such a property is sold and the sale is exempt from VAT, the claw-back provisions of the CGS in relation to exempt supplies apply. If such a property is sold and the sale is taxable, the additional input credit provisions of the CGS in relation to taxable supplies apply.

1.3 When does the CGS not apply?

The scheme does not apply if:

- You are not engaged in an economic (business) activity.
- You are a taxable person who acquires or develops a property in a non-business capacity.
- No VAT was charged on the supply of the property to you.

2. CGS and development by the tenant

Where a tenant has a leasehold interest in a completed property and carries out development work on that property then the tenant creates a capital good. The tenant is regarded as the owner of this capital good. This development is a refurbishment and the adjustment period is ten years.

All of the obligations in relation to the initial, second and subsequent intervals arise for the tenant in relation to the development work carried out. Any change in use must be adjusted for over the adjustment period, which is ten intervals.

There are obligations on the tenant if the lease is assigned or surrendered during the adjustment period for the refurbishment.

The normal annual adjustment (based on 1/20) provisions in the CGS, and the CGS provisions relating to the landlord’s option to tax, do not apply to refurbishments which were completed prior to 1 July 2008.

3. VAT-life of a capital good and CGS intervals

For properties acquired or developed after 1 July 2008, the Capital Goods Scheme (CGS) provides that in most cases each capital good will have a Value-Added Tax (VAT) life or adjustment period of 20 intervals. It is during this period that adjustments are required to be made. Once the period has elapsed, there are no further obligations under the scheme.

Certain properties have an adjustment period of ten intervals. Where development work is carried out on a previously completed building, a new capital good to the value of the cost of the development is created by this development work. This is known as a refurbishment.

The adjustment period for a refurbishment is ten intervals. This means that there can, in some cases, be two or more capital goods schemes in relation to a single property at one time.

A person who owns a freehold or a freehold equivalent interest in a building or a tenant who has a lease in a building, can create a refurbishment (capital good) by carrying out development work on a previously completed building.

The adjustment period for transitional freehold properties and legacy leases is set out in Freehold interests held prior to 2008 and Transitional measures applying to Legacy leases.

3.1 What is a Capital Goods Scheme (CGS) interval?

The adjustment period is divided up into intervals. There are 20 intervals in the case of a new capital good and ten in the case of a refurbishment.

An interval, other than the initial interval and second interval, will be the owner's accounting year.

3.2 What is the CGS initial interval?

In the case of an owner who constructs a property, the initial interval begins on the date on which a property is completed.

In the case of an owner who purchases a property the initial interval begins on the date the property is purchased. In both cases the initial interval ends 12 months from those dates.

Example 1

On 13 September 2013, ABC Ltd purchased a property on which VAT is charged. The initial interval begins on that date and ends 12 months later on 12 September 2014.

3.3 What is the CGS second interval?

The second interval begins on the day after the initial interval ends, and ends at the end of the owner's accounting year in which the initial interval ends. The purpose of this shorter interval is to align the adjustments that may be required under the scheme with the owner's accounting year.

Example 2

Using example 1. ABC's accounting year ends, on 31 December. The initial interval ends on 12 September 2014 (in the accounting year that ends 31 December 2014). The second interval begins on 13 Sept 2014 (day following end of initial interval) and ends on 31 December 2014, that is, at the end of the accounting year during which the initial interval ends.

3.4 What are the CGS subsequent intervals?

A subsequent interval means each interval after the second interval until the end of the adjustment period. The interval immediately following the second interval begins on the day after the end of the second interval and ends at the end of the owner's accounting year.

Example 3

Continuing with example 2 above, where the second interval ends on 31 December 2014, the third interval will begin on 1 January 2015 and end on 31 December 2015. Each subsequent interval will run from 1 January - 31 December until the end of the twentieth interval on 31 December 2032.

Tables 3.1 and 3.2 below illustrates when each interval will begin and end for a new capital good and for a refurbishment. The capital good is acquired on 13/9/2013 and a refurbishment is carried out on the property during 2023, that is completed on 31/7/2023.

Table 3.1 - Illustration of dates for adjustment period

20 intervals - new capital good		
Interval	**Begins**	**Ends**
1	13/09/2013	12/09/2014
2	13/09/2014	31/12/2014
3	01/01/2015	31/12/2015
4	01/01/2016	31/12/2016
5	01/01/2017	31/12/2017
17	01/01/2029	31/12/2029
18	01/01/2030	31/12/2030
19	01/01/2031	31/12/2031
20	01/01/2032	31/12/2032

Table 3.2 - illustration of dates for adjustment period

10 intervals - refurbishment

Interval	Begins	Ends
1	31/07/2023	30/07/2024
2	31/07/2024	31/12/2024
3	01/01/2025	31/12/2025
4	01/01/2026	31/12/2026
5	01/01/2027	31/12/2027
6	01/01/2028	31/12/2028
7	01/01/2029	31/12/2029
8	01/01/2030	31/12/2030
9	01/01/2031	31/12/2031
10	01/01/2032	31/12/2032

Note:

Interval 1 = initial interval

Interval 2 = second interval

Intervals 3-20 = subsequent intervals

3.5 Obligation at the end of a CGS interval

As illustrated in section 3 above, (see example 3 & table 3.1), the initial interval for a capital good runs for a full 12-month period. At the end of this period the owner must examine the use to which the property was put during that 12 months. ‘Use’ in this context means the taxable or exempt use of the property.

This percentage of taxable use will usually be readily identifiable by the owner as it is based directly on the use of the property. However, in some cases a property may be used as a headquarters of a business that is engaged in various taxable and exempt activities. In these cases, the percentage of taxable use will depend on the overall mix of taxable and exempt activities carried on by the business.

Where the percentage of taxable use during the first year differs from the percentage of the Value-Added Tax (VAT) reclaimed by the owner on the acquisition or development of the property then one of the following adjustments is required:

- If the percentage of taxable use for the initial interval is less than the percentage of the VAT reclaimed on the acquisition or development of the property, VAT is payable by the owner. See example 4.
- If the percentage of taxable use for the initial interval is greater than the percentage of the VAT reclaimed on the acquisition or development of the property then the owner is entitled to an additional VAT credit. See example 5.

Clearly, if the owner reclaims all of the VAT and uses the property for fully taxable purposes, then no adjustment is required.

The above does not apply to transitional freehold properties and legacy leases.

Note: There is an exception to the normal rules at the end of the initial interval. If a property developer rents out residential properties (exempt activity - option to tax rents not allowed), then there is no obligation to carry out the adjustment at the end of the initial interval.

Example 4

Adjustment at the end of the initial interval (tax payable)

ABC Ltd purchases a property on 13 September 2014. The cost of the property is €10,000,000 + VAT €1,350,000. This is the total tax incurred. ABC Ltd reclaims all of this VAT on the basis that the company intends to put the property to a fully taxable use.

At the end of the initial interval, 12 Sept 2015, ABC Ltd calculate that the use to which the property is put during the initial interval was 80% taxable. As ABC Ltd reclaimed 100% of the VAT charged, it is obliged to make an adjustment (because there is a difference between these two figures) and repay the excess amount reclaimed.

For the purposes of the adjustment, ABC Ltd must calculate the total reviewed reclaimed amount which is calculated by multiplying the total tax incurred by the initial interval proportion of reclaimed use (80%):

Total reviewed deductible amount = €1,350,000 x 80% = €1,080,000

This figure represents the tax reclaimed in relation to the property on the basis of the taxable use during the initial interval and is the benchmark VAT reclaimed figure for the remaining 19 intervals.

The adjustment required at the end of the initial interval is calculated as the difference between the amount of the VAT reclaimed and the total reviewed deductible amount using the formula:

A - B

(A = amount of total tax reclaimed, B = total reviewed deductible amount)

A - B = €1,350,000 - €1,080,000 = €270,000

As A is greater than B, this amount is payable as VAT due for the taxable period immediately after the end of the initial interval which will be Nov/Dec 2015. The effect of the calculation is that there is a claw-back of €270,000 from ABC Ltd (20% of the VAT initially reclaimed).

Example 5

Adjustment at the end of the initial interval (tax deductible)

XYZ Ltd purchases a property on 7 April 2014. The cost of the property is €1,000,000 + VAT €135,000. This is the total tax incurred. XYZ Ltd deducts 10% (€13,500) of the VAT on the basis that it intends to use the property for 10% taxable activities (90% exempt activities).

At the end of the initial interval, 6 April 2015, XYZ Ltd calculate that the use to which the property is put during the year was 20% taxable. As XYZ Ltd reclaimed 10% of the VAT charged, it is obliged to make an adjustment because there is a difference between these two figures. For the purposes of the adjustment XYZ Ltd must calculate the total reviewed deductible amount which is simply the total tax incurred multiplied by the percentage of taxable use for the initial interval (20%) - €135,000 x 20% = €27,000.

The adjustment is calculated as the difference between the amount of the VAT reclaimed and the total reviewed deductible amount:

A - B

A = (amount of total tax incurred reclaimed, B = total reviewed deductible amount)

€13,500 - €27,000 = - €13,500

As B is greater than A, this amount is given as a VAT credit to XYZ Ltd for the taxable period immediately after the end of the initial interval which will be May/June 2015.

The effect of the calculation is that XYZ Ltd is entitled to an additional input credit of €13,500 (10% of the VAT charged to them).

3.6 CGS second and subsequent intervals

At the end of the second and each subsequent interval the owner should examine the use to which the property was put during that interval and compare that use with the use to which the property was put during the initial interval.

Where the percentage of taxable use during the interval in question differs from the percentage of taxable use for the initial interval then an adjustment is required.

If the percentage of taxable use for the interval is less than the percentage of taxable use for the initial interval then an additional amount of Value-Added Tax (VAT) is payable by the owner.

If the percentage of taxable use for the interval is greater than the percentage of taxable use for the initial interval, then the owner is entitled to reclaim additional VAT. However, if the percentage of taxable use for the interval is the same as the percentage of taxable use for the initial interval, no adjustment is required.

The adjustments at the end of the second and each subsequent interval are calculated using certain defined terms:

- The base tax amount is calculated by dividing the total tax incurred by the number of intervals in the adjustment period.
- The reference deduction amount is calculated by dividing the total reviewed deductible amount by the number of intervals in the adjustment period. This amount is treated as if it were the amount that was reclaimed by the owner at the beginning of the second and each subsequent interval.
- The interval deductible amount is the amount of the base tax amount that is reclaimed on the basis of the use in the interval in question (the second or subsequent interval). For example, if the proportion of deductible use for the second interval is 70% then the interval deductible amount is calculated by multiplying the base tax amount by 70%.

Example 6

Using the same figures as example 4 with company ABC Ltd, and property acquired 13 September 2014. Accounting year ends 31/12.

Total tax incurred = €1,350,000

Base tax amount = €67,500 (€1,350,000 / 20)

This is the total tax incurred divided by the number of intervals in the adjustment period.

As illustrated in the example the initial interval proportion of deductible use was 80%.

Total reviewed deductible amount = €1,080,000

Reference deduction amount = €54,000 (€1,080,000 / 20)

This is calculated by dividing the total reviewed deductible amount by the number of intervals in the adjustment period and is used for any calculations required at the end of the second or subsequent intervals.

The reference deduction amount is the same for the second and each subsequent interval. Where the deductible amount for the second or any subsequent interval (known as the interval deductible amount) differs from this amount an adjustment will be required.

2nd interval - no adjustment

For the second interval (which ends on 31/12/2015), ABC Ltd's taxable use was 80%. (This is known as the proportion of deductible use for the interval.) As this is the same as the use for the initial interval, no adjustment is required.

3rd, 4th and 5th intervals - no adjustment

For the 3rd (ending 31/12/2016), 4th (ending 31/12/2017) and 5th (ending 31/12/2018) intervals, the proportion of deductible use is still 80%, so adjustments are not required for those intervals.

6th and 7th intervals - change in taxable use - VAT payable on adjustment

For the 6th interval (ending 31/12/2019), the proportion of deductible use is 70%. As this differs from 80% (use during initial interval) an adjustment is required.

In order to carry out the calculation ABC Ltd is obliged to calculate the interval deductible amount which is the proportion of deductible use for that interval multiplied by the base tax amount €67,500 x 70% = €47,250.

The adjustment is the difference between the reference deduction amount and the interval deductible amount:

C - D where (C = reference deduction amount, D = interval deductible amount)

€54,000 - €47,250 = €6,750

As C is greater than D, €6,750 is payable as tax due for the taxable period following the end of the interval, which is Jan/Feb 2016.

For the 7th interval (ending 31/12/2020) the proportion of deductible use was 70%.

Again, an adjustment is required:

C - D

€54,000 - €47,250 = €6,750

As C is greater than D, €6,750 is payable as tax due for the taxable period following the end of the interval, which is Jan/Feb 2021.

8th and 9th intervals - no adjustment required

For the 8th (ending 31/12/2021) and 9th (ending 31/12/2022) intervals, the proportion of deductible use for the interval is 80%, so no adjustment required.

10th interval - change in taxable use - VAT deductible on adjustment

For the 10th interval (ending 31/12/2023), the proportion of deductible use is 95%. As this differs from 80% (use during initial interval) an adjustment is required. Similar to above, the interval deductible amount is €67,500 x 95% = €64,125.

Adjustment for the interval:

C - D

54,000 - €64,125 = - €10,125

As D is greater than C, €10,125 is given as a VAT credit for the taxable period following the end of the interval, which is Jan/Feb 2024.

For the remainder of the intervals the proportion of deductible use is 80% which means there are no adjustments made at the end of all the intervals. The twentieth interval ends on 31/12/2033. After this date there are no further obligations under the scheme.

As can be seen from this example, the scheme ensures that the total VAT reclaimed in respect of the property reflects the use to which the property is put over the adjustment period.

Tables 3.3 and 3.4 illustrate how the figures from this example lead to adjustments at the end of the initial interval (based on the full amount of VAT incurred) as well as the 6th, 7th and 10th interval based on 1/20th of the VAT incurred.

Table 3.3 - Adjustments for intervals				
Interval	**Amt Reclaimed €**	**Total Rev Ded amt €**	**Adjustment €**	**VAT**
1	1,350,000	1,080,000	270,000	Payable

Base tax Amount = €67,500 for all intervals.

Table 3.4 - Adjustments for intervals				
Interval	**Ref Deduction Amt €**	**Interval Deduction Amt €**	**Adjustment €**	**VAT**
2	54,000	54,000	-	-
3	54,000	54,000	-	-
4	54,000	54,000	-	-
5	54,000	54,000	-	-
6	54,000	47,250	6,750	Payable
7	54,000	47,250	6,750	Payable
8	54,000	54,000	-	-
9	54,000	54,000	-	-
10	54,000	64,125	10,125	Deductible
11	54,000	54,000	-	-
12	54,000	54,000	-	-
13	54,000	54,000	-	-
14	54,000	54,000	-	-
15	54,000	54,000	-	-
16	54,000	54,000	-	-
17	54,000	54,000	-	-
18	54,000	54,000	-	-
19	54,000	54,000	-	-
20	54,000	54,000	-	-

3.7 CGS adjustment where property use is linked to overheads

In the majority of cases the taxable use of a property will be determined by direct attribution, that is, the actual use to which the property is put.

In such cases, the adjustment must be made at the end of the appropriate interval, and any tax payable or reclaimed must be accounted for in the Value-Added tax (VAT) return for the taxable period following the end of that interval.

However, where the taxable use of the property is determined using the same methodology as used for reclaiming VAT on the general overheads (such as, a headquarters) of the business, Revenue will allow the adjustment to be made in any of the three taxable periods following the end of the relevant interval.

This concurs with the timescale we allow for adjustments arising from reviews of apportionment of input credits.

If a taxpayer attempts to abuse these rules for the purpose of avoidance or deferral of tax, we may withdraw this treatment for the taxpayer at our discretion.

3.8 Big swing in taxable use

There are special rules that apply where the taxable use for an interval differs by more than 50 percentage points from the taxable use for the initial interval. These rules recognise the fact that there has been a significant change in the taxable activities of the business and require a full adjustment.

This adjustment is based on the full Value-Added Tax (VAT) incurred at the initial interval stage, reduced by the number of intervals that have already expired in the adjustment period.

The big-swing rule operates by providing for an adjustment at the end of an interval where there has been a change of more than 50 percentage points when compared to the initial interval.

Where such an adjustment is required there is a re-balancing of the benchmark figures and the re-balanced benchmark figures are then used for all remaining intervals after the interval in which the big-swing occurs.

Example 7

Changes of more than 50 percentage points in taxable use

C LTD is an IT company. It provides both software services and training services. The breakdown of the business over the last number of years is 30% software (taxable), 70% training (exempt). Its accounting year ends on 31/03 each year. C Ltd purchases a property on 21/08/2011 for €3m + VAT (€405,000 total tax incurred).

Base tax amount = €20,250 (€405,000 / 20)

The initial interval begins on the date of purchase (21/08/2011). C Ltd deducts 30% of the VAT charged.

At the end of the initial interval (20/08/2012), the initial interval proportion of deductible use = 30%, so no adjustment is required.

Total reviewed deductible amount = €121,500 (€405,000 x 30%)

Reference deduction amount = €6,075 (€121,500 / 20)

C Ltd's 2nd interval ends on the date of the next accounting year, which is the 31/03/2013 (accounting year for C Ltd ends on 31/03 each year). The 3rd interval ends on the 31/03/2014, and the 4th interval on the 31/03/2015. The proportion of deductible use is 30%, so no adjustment is required.

During 2015, C Ltd wins a high value contract to develop software for a large multinational.

As a result of this increase in taxable use, the proportion of deductible use for the 5th interval (ending 31/03/2016) is 90%. As this differs from the initial interval proportion of deductible use by more than 50 percentage points (90% less 30%), a big-swing adjustment is triggered. When such an adjustment occurs, there is no normal adjustment based on 1/20 of the deductibility.

The interval deductible amount = €18,225 (base tax amount x 90%)

Adjustment is calculated as follows:

(C - D) x N

C = (reference deduction amount, D = interval deductible amount, N = number of full intervals remaining +1)

(€6,075 - €18,225) x 16 = - €194,400

As D is greater than C, €194,400 is given as an additional VAT credit to C Ltd in the taxable period following the end of the interval May/June 2016.

As part of the big-swing adjustment the benchmark figures for the capital good are also changed.

The initial interval proportion of deductible use is changed to 90%, from 30%. This is necessary, as essentially C Ltd has been given a VAT credit of 90% for 16 intervals.

Total reviewed deductible amount = €364,500 (€405,000 x 90%)

Reference deduction amount = €18,225 (€364,500 / 20)

The total tax incurred and the base tax amount stay the same as they are based on the VAT charged at acquisition.

For the 6th interval (ending 31/3/2017), the proportion of deductible use = 90%, so no adjustment is required as this is the same as the new initial interval proportion of deductible use.

For the 7th interval (31/3/2018), the proportion of deductible use = 75%, so an adjustment is required.

The interval deductible amount = €15,188 (base tax amount x 75%)

C - D

€18,225 - €15,188 = €3,037

As C is greater than D, €3,037 is payable as tax due by C Ltd for the taxable period following the end of the interval May/Jun 2018.

For all the remaining intervals, that is, 8th to 20th, the proportion of taxable use is 90%, so no further adjustments are required.

The example above illustrates how adjustments are calculated when there is a change of more than 50 percentage points in the proportion of taxable use of the property when compared with the use during the initial interval.

In this example, the use increased by more than 50 percentage points, so there was a VAT credit given. The rule also applies where there is a decrease in the taxable use by more than 50 percentage points. The decrease results in a claw-back of VAT. The benchmark figures are re-balanced.

4. Capital Goods Scheme (CGS) - other adjustments

There are a number of rules within the Capital Goods Scheme (CGS) for dealing with sales of capital goods (properties) during the adjustment period.

This section sets out the CGS adjustments for vendors, landlords, tenants and assignees in respect of:

- a taxable sale of a property
- an exempt sale of a property
- a tenant’s CGS
- the assignment or surrender of a lease
- passing on CGS liabilities
- the landlord's option to tax a letting
- residential property.

The CGS adjustments for a big-swing or annual adjustment are covered in section 1 to section 3.

4.1 Taxable sale during the CGS adjustment period

If the sale is taxable there are two possible scenarios for the vendor:

- If you were not entitled to reclaim some or all of the Value-Added Tax (VAT) on the acquisition or development of the property, then a VAT credit is given to you at the time of the sale. The VAT credit is based on the non-deductible VAT and the number of intervals remaining in the adjustment period.
- If you were entitled to reclaim all of the VAT on the acquisition or development of the property then there is no adjustment required.*

***You must also have used the property for 100% taxable activities for the initial interval. This condition does not have to be met if the property is sold before the end of the initial interval.**

Example 8

In this example the sale is exempt but a joint option to tax is exercised.

BL owns a green field site. It engages a builder to construct a new office. The builder charges €5m + VAT €675,000 (total tax incurred).

BL deducts 15% of this VAT on the basis that it intends to use the property for 15% taxable activities.

The building is completed on 3/2/2010. The initial interval begins on this date. At the end of the initial interval (2/2/2011), the initial interval proportion of deductible use = 15%, so no adjustment required.

Total reviewed deductible amount = €101,250

Non-deductible amount = €573,750 (€675,000 - €101,250)

For the 2nd, 3rd, 4th, 5th and 6th intervals, the proportion of deductible use = 15%, so no adjustment required at the end of those intervals.

On the 6 May 2016 (during the 7th interval), BL sells the property to JB Ltd. The sale is exempt as it is over five years since the completion of the building. However, BL and JB Ltd exercise the joint option to tax the sale. The sale price is €7million. An adjustment is required by BL which gives it a credit for part of the non-deductible VAT.

The adjustment is calculated as follows:

(E x N) / T

E = non-deductible amount

N = number of full intervals remaining + 1

T = total number intervals in the adjustment period

(€573,750 x 14) / 20 = €401,625

BL claims €401,625 VAT credit for the taxable period in which the sale occurs (May/June 2016). BL has no further obligations under the scheme.

As the sale is subject to the joint option to tax, JB Ltd must account for VAT on the reverse charge, on the sale €7m x 13.5% = €945,000.

Obligations for JB Ltd the purchaser

JB Ltd has acquired a developed property on which VAT is chargeable.

JB is an owner for the purpose of the scheme. The initial interval for JB Ltd begins on 6/5/2016. There will be 20 intervals and the total tax incurred = €945,000.

Points to note:

The VAT credit given to BL also applies to situations where the sale takes place while the property is new (for example, if the property was sold by BL within five years of its completion).

The VAT credit given to BL ensures that when VAT is charged on the sale that any non-deductible VAT for the remainder of the VAT life is given as a VAT credit.

If the seller (BL) had been entitled to reclaim the full VAT charged (the total reviewed deductible amount was the full VAT charged) no further input credit arises.

In cases where the sale is taxable while new, BL will charge VAT to JB Ltd in the normal way. BL will remit the VAT to Revenue and JB Ltd will reclaim whatever proportion of the VAT to which it is entitled.

4.2 Exempt sale during the CGS adjustment period

If the sale is exempt there are two possible scenarios for the vendor:

- If you were entitled to reclaim some or all of the Value-Added Tax (VAT) then there is a claw-back based on the amount of VAT reclaimed by you and the number of intervals remaining in the adjustment period.
- If you were not entitled to reclaim any of the VAT then there is no adjustment required. [1]

[1] You must also have used the property for 100% exempt activities for the initial interval. This condition does not have to be met if the property is sold before the end of the initial interval.

Example 9

M Ltd purchases a new property from B Ltd on 6/10/2012 for €3m + VAT €405,000 (B Ltd completed the property on 01/09/2012 but never occupied the property). The initial interval for the property begins on the 06/10/2012. M Ltd deducts all of the VAT on the basis it intends to use the property for a fully taxable activity. M Ltd occupies the property on 25/10/2012.

At end of the initial interval (5/10/2013):

Initial interval proportion of deductible use = 100%

Total reviewed deductible amount = €405,000

The property is used for 100% taxable purposes until sold on 4/5/2015 to RS Ltd. As it is the second or subsequent sale following completion and the property has been occupied for a period of more than two years the sale is exempt.

The exempt sale triggers an adjustment as follows:

(B x N)/ T

B = total reviewed deductible amount

N = number of full intervals remaining + 1

T = total number of intervals in the adjustment period

(€405,000 x 17) / 20 = €344,250

M Ltd the seller

€344,250 is payable as tax due by M Ltd in the taxable period in which the sale occurs (May/June 2015). There are no further obligations under the scheme for M Ltd.

Obligations for RS Ltd the purchaser

RS Ltd acquires a developed property but no VAT is chargeable on the acquisition. Therefore, the property is not subject to the CGS in the hands of RS Ltd.

4.3 When does a tenant create a capital good?

Where you have a leasehold interest on a property and you carry out development work on that property then you have created a capital good that is separate to the underlying property.

The development is considered a refurbishment (development work on a previously completed building) and you are a capital good owner in respect of the refurbishment. Where such a development occurs, the adjustment period is ten years.

Aside from the change of use provisions, the Capital Goods Scheme (CGS) contains particular provisions where a tenant assigns or surrenders the lease.

4.4 Assignment or surrender of a lease by a tenant

If, during the ten-interval adjustment period a tenant assigns or surrenders a lease of a property in which they created a capital good, a Capital Goods Scheme (CGS) adjustment arises.

A claw-back of the Value-Added Tax (VAT) reclaimed (reduced by the number of years that have elapsed in the adjustment period) arises in the hands of the tenant.

Example 10

PH Ltd takes a lease in a property from 1 June 2010. PH Ltd carries out development work on the property to prepare the unit for trading. The total cost of this work is €500,000 + VAT €67,500. PH Ltd reclaims 90% of this VAT on the basis that the property is to be used for 90% taxable activities.

Total tax incurred = €67,500

Base tax amount = €6,750 (€67,500 / 10)

The development work is completed on 23 July 2010. The initial interval for the capital good begins on that day. At the end of the initial interval (22/7/2011), PH Ltd's exempt activity is greater than forecast as the initial proportion of deductible use is 65%. As this differs from 90%, an adjustment is required.

Total reviewed deductible amount = €43,875 (€67,500 x 65%)

Reference deduction amount = €4,388 (€43,875 / 10)

Adjustment calculated as follows:

A – B

A = the amount of the total tax incurred to that capital good which was deductible by the owner

B = the total reviewed deductible amount in relation to that capital good

A = 60,750 (67,500 * 90%)

B = 43,875 (67,500 * 65%)

€60,750 - €43,875 = €16,875

As A is greater than B, €16,875 is payable as tax due in the taxable period following the end of initial interval (Sept/Oct 2011). For the second (31/12/2011), third (31/12/2012) and fourth (31/12/2013) intervals, proportion of deductible use = 65%, so no adjustments are required.

During 2014 (5th interval), PH Ltd decide to upscale and move to a new property. It surrenders the lease to the landlord on 1 April 2014.

This triggers an adjustment under the scheme calculated as follows:

(B x N) /T

B = total reviewed deductible amount

N = number of full intervals remaining + 1

T = total number of intervals in the adjustment period

(€43,875 x 6)/ 10 = €26,325 payable as tax due in taxable period when surrender occurs (Mar/Apr 2014)

Points to note:

The normal annual adjustment (based on 1/20) provisions in the CGS and the CGS provisions relating to the landlord's option to tax, do not apply to refurbishments which were completed prior to 1 July 2008.

The adjustment required on the assignment or surrender of a lease where the tenant has carried out a refurbishment also applies to the assignment and surrender of a legacy lease (where the tenant has carried out a refurbishment). In such cases, there is a supply of goods (the assignment or surrender of the legacy lease) and a deductibility adjustment in relation to the refurbishment under the CGS.

Generally, if a tenant carries out a refurbishment in say year 15 of a 20 year lease and the lease expires after 20 years without being renewed, there are no adjustments required by the tenant after the lease has expired.[1]

[1] However, Revenue will look at cases where a tenant carries out a significant refurbishment approaching the end of a lease to examine if the refurbishment is to the benefit of the landlord. In such situations, the issue of entitlement to input credit of the landlord would need to be considered.

4.5 Passing on CGS liabilities in certain circumstances

There are two exceptions to the rule, whereby there is a claw-back of Value-Added Tax (VAT) reclaimed, where the tenant assigns or surrenders a lease on a property in which the tenant has carried out a development.

First exception

The first exception is where the tenant used the property for 100% taxable use during the initial interval.

Where the lease is assigned or surrendered and where the tenants enters into a written agreement with the person to whom the lease is being assigned or surrendered then the tenants obligations under the Capital Goods Scheme (CGS) can be passed on to that person.

The tenant is obliged to issue a copy of the capital good record to the other party. That person uses the information in the capital good record for the purposes of operating the scheme.

In order for the claw-back to be avoided it is necessary that the following occur:

- The property is used for 100% taxable purposes during the initial interval.
- There must be a written agreement between the tenant and the person to whom the lease is assigned or surrendered to the effect that that person is taking over all obligations of the tenant under the CGS.
- The tenant must issue a copy of the capital good record to the person to whom the lease is assigned or surrendered.

Example 11

GR Ltd takes a lease in a property from 1 April 2010. The property is a shell and GR Ltd intends to open a restaurant. GR Ltd carries out development work on the property installing a bar, kitchen and air-conditioning units.

The total cost of this work is €1,500,000 + VAT €202,500. GR Ltd reclaims all this VAT on the basis it intends to make fully taxable supplies. The development work is completed on 6 August 2010.

Total tax incurred = €202,500

At the end of initial interval the initial interval proportion of deductible use = 100% (so no adjustment required).

Total reviewed deductible amount = €202,500 (€202,500 x 100%)

During the third interval, GR Ltd ceases trading. GR Ltd's landlord is willing to accept the surrender of the lease on 1 September 2012.

The landlord is willing to leave the tenant's fixtures in place as another tenant might wish to run a restaurant from the premises.

The landlord agrees in writing with GR Ltd to take over the responsibilities under the CGS scheme from the date of the assignment.

GR Ltd issues a copy of the capital good record to the landlord.

The landlord will have to make adjustments at the end of each of the remaining intervals for any changes of use, until the end of the adjustment period (31/12/2019).

Second exception

The second exception to the claw-back from the tenant is where there is an assignment or surrender of a lease where the development work is essentially ripped out.

Example 12

If a kitchen and bar has been installed and the kitchen and bar are taken out of the property prior to the assignment or surrender of the lease then there is no claw-back from the tenant under the scheme.

4.6 Exercising and terminating a landlord's option to tax a letting

The basic rule is that the letting of a property is exempt from Value-Added Tax (VAT). However, you may opt to tax the letting (but an option to tax residential property is not allowable).

The effect of exercising the option to tax, is that the property is put to a fully taxable use. You are entitled to reclaim the acquisition and development VAT costs.

As the option to tax can be exercised or cancelled at any time, there are implications for the Capital Goods Scheme (CGS) as a property can move from taxable to exempt use (or the other way around).

If you terminate an option to tax a letting or exercise an option to tax a previously exempt letting, then you are deemed for the purposes of the CGS to have supplied the property and immediately reacquired it.

Where you terminate the option to tax, the supply is deemed to be exempt, which gives rise to a withdrawal of the VAT already reclaimed.

Where you exercise an option to tax a letting that was previously exempt, the supply is deemed to be taxable, thus giving input credit for the VAT you could not previously reclaim.

The adjustment period for the capital good begins at the deemed acquisition date and comprises the number of full CGS intervals remaining in the original adjustment period plus one.

4.6.1 What if your property is a transitional property?

In the application of CGS to immovable goods and interests in immovable goods that are transitional properties, certain elements of the CGS are disregarded. This is in respect of the person who owns those immovable goods or holds an interest in those immovable goods on 1 July 2008.

The landlord cannot claim an input credit for VAT that he or she could not previously reclaim when he or she opts to tax a letting of a transitional property.

Example 13

Terminating the landlord’s option to tax

L acquired a commercial property on 12/7/2010. His accounting year ends on 31/12 each year. The property cost €15m + VAT €2,025,000 (total tax incurred).

L reclaimed all of the VAT on the basis that he intended to rent the property and exercised the landlord's option to tax and charged VAT on the rents. L entered into a 21-year lease with an un-connected tenant beginning on 1/9/2010, and charged VAT on the rents.

Total reviewed deductible amount = €2,025,000

The initial interval began on 12/7/2010. After ten years the tenant exercises the break clause in the lease. L secures a new tenant. The new tenant K, has no entitlement to reclaim VAT and therefore does not want to be charged VAT on the rents.

L creates a new 15-year lease to K beginning on 1/10/2020. He does not charge VAT on the rents and so terminates the landlord's option to tax. This is deemed to be an exempt sale of the property by L. This triggers an adjustment on 1/10/2020.

The formula is the same as in exempt sale:

(B x N)/T

B = total reviewed deductible amount

N = number of full intervals remaining + 1

T = total number of intervals in the adjustment period.

(€2,025,000 x 10)/ 20 = €1,012,500

€1,012,500 is payable by L for the taxable period during which the option to tax is terminated Sept/Oct 2020.

L is deemed to immediately re-acquire the property and the property is deemed to be a capital good for the purposes of the scheme.

Total tax incurred is deemed to be €1,012,500

Non-deductible amount = €1,012,500

Total reviewed deductible amount = Nil (since the property will be subject to an exempt letting)

The adjustment period will have 10 intervals beginning with the initial interval that commences on 1/10/2020 and ends on 30/9/2021. The second interval begins on 01/10/2021 and ends on 31/12/2021.

There is no variation in the lease and the adjustment period ends (with no further adjustments during the remaining ten intervals) on 31/12/2029.

Example 14

Exercising the landlord’s option to tax with previously exempt letting

OCS purchased a property on 17/2/2010 for €6m + VAT €810,000 (total tax incurred). It did not reclaim any of the VAT on the basis that it intended to make an exempt letting of the property.

OCS's accounting year ends on 31/12. OCS secured a tenant and created a 25-year lease which began on 1/4/2010.

Non-deductible amount = €810,000

Total reviewed deductible amount = nil

The letting continues for eight years until the tenant exercises a break clause and exits from the lease. OCS secures a new tenant who is fully taxable.

On 1/5/2018, OCS creates a new lease for 20 years to T Ltd and exercises the landlord's option to tax. This is deemed to be a taxable sale of the property by OCS. This triggers an adjustment under the scheme.

The formula is the same as in taxable sale:

(E x N) / T

E = non-deductible amount

N = number of full intervals remaining + 1

T = total number intervals in the adjustment period

(€810,000 x 12)/20 = €486,000 which is given as VAT credit for the taxable period when the option is exercised May/June 2018.

OCS is deemed to immediately re-acquire the property on 1/5/2018. It is a capital good as it was acquired for a business purpose and VAT was deemed to have been charged.

For the purposes of the scheme:

the total tax incurred is deemed to be €486,000

OCS is deemed to have fully reclaimed this amount

the total reviewed deductible amount = €486,000

The adjustment period will have 12 intervals beginning with the initial interval that commences on 1/5/2018 and ends on 30/4/2019. The second interval begins on 01/05/2019 and ends on 31/12/2019.

There is no variation in the lease and the adjustment period ends (with no further adjustments during the remaining 12 intervals) on 31/12/2029.

4.7 Letting of a residential property by a builder (developer)

The supply of a residential property, held as stock in trade by the person who developed the property, is always taxable regardless of when it takes place.

Where you let the property, this letting is exempt, as an option to tax residential property is not allowed.

Under the normal Capital Goods Scheme (CGS) rules the exempt letting of a property leads to a full adjustment of the tax reclaimed. However, where you have developed residential properties and subsequently let them, special rules apply.

If you were entitled to reclaim the Value-Added Tax (VAT) incurred on the acquisition or development of residential property where that property is completed on or after 1 July 2008, and that property is rented on or after 1 July 2008, no immediate claw-back occurs.

Instead, you will be required to adjust the VAT reclaimed at the end of the second CGS interval, and each subsequent interval up until the property is sold. There is no adjustment required in the year of sale.

Example 15

Developer E constructed a house for sale. The cost of constructing this house is €1,000,000 + VAT €135,000. E reclaimed all of this VAT.

The development of the house was completed on 15 Jul 2008. E was unable to sell the house and instead rented it out. The letting was for two years and was created on 4 August 2008. There was no immediate claw-back of the VAT reclaimed. E's accounting year ends on 31 December each year.

The CGS initial interval for E in respect of the property begins on 15 Jul 2008. It ended on 14 Jul 2009. The second interval ended on 31 December 2009 (end of accounting year).

An adjustment arises as follows:

C - D

C = reference deduction amount

D = interval deductible amount

C = €6,750 (€135,000 / 20 intervals)

D = 0

€6,750 - 0 = €6,750

€6,750 is payable as tax due by E for the taxable period following end of second interval (31/12/2009). The tax was due for the Jan/Feb 2010 VAT period.

This payment essentially amounts to E paying back 1/20th of the VAT reclaimed in respect of the development of the property.

At the end of each subsequent interval (in the taxable period following the end of each 31/12 financial year) €6,750 is payable by E for as long at the property is not used for a taxable purpose.

What is the position when this residential property is sold after being rented?

At the end of the lease 3 Aug 2010, E sold the property for €1,200,000. The sale was subject to VAT @ 13.5% = €162,000.

A VAT credit was not given for the claw-back of €6,750 that occurred in the Jan/Feb 2010 taxable period as the property was put to an exempt use during the second interval.

No further claw-back of VAT reclaimed arises as the taxable supply of the property in August 2010, constitutes a taxable use for the third and all subsequent intervals.

VAT of €162,000 was payable by E for the Jul/Aug 2010 taxable period in respect of the sale of the property.

5. Capital Goods Scheme (CGS) - Transfer of Business Relief

This section outlines how the Capital Goods Scheme (CGS) operates when property is transferred as a business or part of a business to an accountable person.

5.1 Transfer of a business

Value-Added Tax (VAT) is not chargeable on the transfer of a property if Transfer of Business Relief (TOB) applies. There are special rules within the Capital Goods Scheme (CGS) that apply to this type of transaction.

There are two main rules that apply to the transferee on the transfer of the property.

The first rule applies when the transfer of the property would have been taxable but for the TOB Relief. This typically would arise when the property is considered new for VAT purposes.

The second rule applies when the transfer of the property would have been exempt. This typically would arise when the property is not considered new for VAT purposes or on the transfer of a legacy lease as part of a transfer of a business.

There are also rules dealing with the transferor.

5.2 Transfer of a property during the period it is considered new

Where a transfer of a property occurs in the course of a transfer of a business, no Value-Added Tax (VAT) is charged on the sale of the property to the transferee. If this occurs during the period when a property is considered new then for Capital Goods Scheme (CGS) purposes:

- The transferor is treated as if he or she has made a taxable supply of the property,

and

- The transferee is treated as if he or she has been charged the VAT that would have been charged, but for the fact that relief for the transfer of business applied. [1]

[1] The amount of tax that would have been charged is treated as the total tax incurred. The transferee must pay to Revenue the difference between this amount and the amount that would have been deductible if this amount of VAT had been charged on the supply of the property.

Example 16

Transfer of business while property is new — taxable (transferor, transferee)

B Ltd constructs a property that is completed on 6 Oct 2013, for a cost of €1,000,000 + VAT €135,000 (total tax incurred). It deducts all of the VAT on the basis it intends to run a fully taxable bookshop business.

B Ltd operates a fully taxable business for three years so there are no adjustments required under the CGS scheme. During their third year of occupation of the property, C Ltd makes B Ltd an offer to buy their business for €2,000,000.

Of this, the property is valued at €1,500,000, the stock at €100,000 and the goodwill at €400,000. As this is a transfer of a business, no VAT applies. The business is sold to C Ltd on 14/11/2016.

CGS implications for B Ltd (transferor)

B Ltd is treated as having made a taxable supply of the property.

There are no CGS implications on the transfer, as B Ltd has already deducted all of the VAT and used the property for fully taxable purposes. The CGS rules for properties acquired through the transfer of business rules mirror those for taxable supplies from the perspective of the transferor.

CGS implications for C Ltd (transferee)

C Ltd is treated as having incurred VAT on the acquisition of the property. As C Ltd is using the property for fully taxable purposes there is no difference between the amount of VAT deemed to have been charged and the amount of that VAT that would have been deductible.

Using the formula to calculate the amount payable:

F - G

F = amount of VAT that would have been chargeable if the transfer of business relief had not applied

G = amount of that VAT that would have been deductible but for the application of the transfer of business relief

€202,500 - €202,500 = 0 (amount payable by C Ltd is nil)

A new CGS adjustment period begins for C Ltd

Total tax incurred = €202,500 (Amount that would have been chargeable €1,500,000 x 13.5%)

C Ltd is deemed to have fully deducted this amount.

Base tax amount = €10,125 (€202,500 / 20)

The initial interval begins on 14/11/2012 and ends on 13/11/2013.

At the end of the initial interval the 'initial interval proportion of deductible use' = 100%, so no adjustment required.

Total reviewed deductible amount = €202,500

Reference deduction amount = €10,125

C Ltd must then operate the CGS scheme for the property for the remaining 19 intervals in the normal way and account for any change of use or any possible adjustments required when the property is sold.

Example 17

Transfer while property new - exempt (transferor, transferee)

Training Ltd (TL) purchases a new property on 7 Nov 2010 for €4m + VAT €540,000 (total tax incurred). Training Ltd are engaged in the fully exempt activity of vocational training and do not deduct any of the VAT. At the end of the initial interval (6/11/2011), there is no adjustment, as the initial interval proportion of deductible use is 0%.

Total reviewed deductible amount = 0

Non-deductible amount = €540,000 (€540,000 - 0)

During 2011, an international consortium (IC) makes an offer to buy the business for €6m. The valuation of the property as part of the offer is €4.5m. Training Ltd agrees to sell the business to IC on 1/12/2011. As there is a transfer of a business as a going concern, no VAT applies.

CGS implications for TL (transferor)

However, the transfer triggers a CGS adjustment for Training Ltd. The adjustment mirrors the credit that would be given if the property were subject to a taxable supply:

(E x N) / T

E = non-deductible amount

N = number of full intervals remaining +1

T = total number of intervals in adjustment period

(€540,000 x 19)/20 = €513,000

This is given as a VAT credit to Training Ltd for the taxable period when the transfer occurs (Nov/Dec 2011).

CGS obligations for IC (transferee)

IC is treated as having been charged VAT that would have been charged on the supply of the property if the transfer of business relief had not applied.

Total tax incurred = €607,500 (amount that would have been chargeable if the transfer of business relief had not applied €4,500,000 x 13.5%)

As IC would not have been entitled to deduct all of the VAT that would have been chargeable, there is an adjustment triggered in the taxable period when the transfer occurs (Nov/Dec 2011):

F - G

F = amount of VAT that would have been chargeable if the transfer of business relief had not applied

G = amount of that VAT that would have been deductible but for the application of the transfer of business relief

€607,500 - 0 = €607,500 (payable as tax due by IC)

IC is deemed to have deducted none of the total tax incurred.

The initial interval begins on 1/12/2011 and ends on 30/11/2012.

Initial interval proportion of deductible use = 0%

Total reviewed deductible amount = 0

Non-deductible amount = €607,500

IC must operate the scheme for the remaining 19 intervals in the normal way and will be entitled to a VAT input credit at the end of any interval during which the property is used for taxable or partly taxable purposes. It will also be entitled to a credit if the property is sold during the adjustment period and the sale is taxable.

It should be noted that the obligations on the exempt transferor and exempt transferee, as illustrated in this example, applies only to transfers that occur during the period while the property is new.

5.3 Transfer of a property no longer classified as new

If a transfer occurs outside the period where a property is considered new (that is, if the property was sold at the time the transfer takes place, it would be exempt from Value-Added Tax (VAT)) then the transferee essentially steps into the shoes of the transferor.

The transferee takes over from the transferor and inherits the adjustment period of the property. That is, if six Capital Goods Scheme (CGS) intervals have elapsed then there will be 14 CGS intervals remaining in the adjustment period for the transferee.

Example 18

Transfer outside period where property is new

Mr S is a sole trader who runs a fully taxable business. He purchased his current office space for his business on 13/4/2010, for €3m + VAT €405,000. He has no adjustment at the end of the CGS initial interval as his initial proportion of deductible use = 100%.

Total reviewed deductible amount = €405,000

Mr S continues to trade for six years engaging in fully taxable activities (No adjustment at end of any intervals to that point).

During 2016 (seventh interval), Mr S begins to plan his retirement.

A big firm (BF) becomes aware of this and makes Mr S an offer for the business of €5m. The property is valued at €4m. Mr S accepts the offer and sells the business on 1/7/2016.

As there is a transfer of a business as a going concern, no VAT applies. If the Transfer of Business Relief had not applied, the supply of the property would have been exempt from VAT. Because of this the treatment of the transfer for the purposes of the CGS is different to that as outlined in the previous examples.

Essentially BF becomes the successor to Mr S and steps into the shoes of Mr S for the purposes of the CGS scheme. Mr S is obliged to provide a copy of the capital good record to BF, and BF continues to operate the CGS as if it had owned the property from the date it was acquired by Mr S (13/4/2010).

BF must comply with the scheme for the remaining 14 intervals in the normal way and account for any change of use or any possible adjustments required when the property is sold.

5.4 Legacy lease as part of a transfer of a business

A legacy lease is a lease of ten years or longer, granted prior to 1 July 2008.

Where a legacy lease is transferred as part of a transfer of a business, the person acquiring the business steps into the shoes of the transferor for the purposes of the Capital Goods Scheme (CGS).

The transferee uses the capital good record for the legacy lease for the purposes of operating the CGS until the end of the adjustment period for the legacy lease.

There is no obligation on the transferor to issue a document, as would be the case if the legacy lease was assigned and the Transfer of Business Relief had not applied.

6. CGS – The Big Swing for Transitional Properties

6.1 When does the big-swing "test" apply to transitional properties?

Where on or after 23 February 2010 a transitional property is used for the first time, or there is a change of use in the property, the big-swing test (Section 64(4)) will apply to such properties. This means that the owner of such a property will be obliged to make a big-swing adjustment if the first use or the changed use of that property results in a "swing" of more than fifty percentage points.

6.2 What does “first use” mean?

First use means any use of a transitional property by a taxable person on any date on or after 23 February 2010 where the property has not been used prior to 23 February 2010. First use does not however include a letting of the property by the taxable person.

6.3 What does “changed use” mean?

Changed use means any situation where on any date on or after 23 February 2010 the property is used by a taxable person for a purpose that is different to its use by the taxable person prior to that date. Changed use does not however include a letting of the property by the taxable person.

In order to qualify as a "changed use", it is not necessary that the changed use be an exempt use. For example, if a person uses a property from January 2006 for the purposes of making widgets (taxable) and changes this use to selling stationery (also taxable) in January 2011, this would constitute a changed use and the big-swing test would apply to that property. If part of a property is used for a "changed use" the big-swing rule will apply.

6.4 What happens if the big-swing test applies but there is a change of less than fifty percentage points in the taxable use of the property?

In such cases even though the big-swing test applies, no adjustment of deductibility will be required. This is because there has not been a "swing" of more than fifty percentage points in the taxable use of the property. (See Example 21 below). In addition, as the annual CGS adjustments under Section 64(3)[1] VATCA 2010 continue to be disapplied on or after 23 February 2010 in relation to transitional properties, there will be no obligation on the owner of the property to make a "normal" CGS adjustment in such cases.

6.5 What happens if the property is for the purposes of a letting on or after 23 February 2010 having previously not been used or used for a different purpose?

As stated above, the big-swing test does not apply in such cases. In addition, the special rules in the CGS which deal with the exercising and termination of the landlord's option to tax continue to be disapplied. The claw-back rules in Section 95(4)(a) VAT CA 2010 in relation to exempt lettings of transitional properties continue to apply.

Example 19

Mr H purchases a property on 1 January 2008 for €5 million + VAT €675,000. He deducts all this VAT on the basis that he is going to use the property for the purposes of his fully taxable business. Mr H does not secure the funding he needs to get the business off the ground and the property remains vacant.

On 1 January 2011 Mr H commences operating a crèche from the facility. As this is the "first use" of the property and this "first use" occurs on or after 23 February 2010 the big swing test applies to Mr H in relation to the property. At the end of the CGS interval [2] in which the first use occurs (31/12/2011), Mr H will be obliged to calculate whether or not a big-swing adjustment is required.

As he took a full deduction in respect of the acquisition of the property, the benchmark figure is 100% taxable. The use during the interval in which the first use occurs is 0% taxable. As this is a change of more than 50 percentage points, an adjustment is required. The formula to be used is-

(C - D) x N

C = reference deduction amount, D = interval deduction amount, N = number of full intervals remaining in the adjustment period for the property + 1.

(33,750 [3] – 0) x 17= €573,750

This amount represents VAT payable by Mr H in the taxable period following the end of the interval in which the use took place. (The VAT is payable in Jan/Feb 2012). This amount corresponds to a claw-back of 17/20 of the VAT initially deducted.

The benchmark figure for the CGS for Mr H in respect of this property after this adjustment is made is 0% taxable. The big-swing test will continue to apply until the end of the adjustment period and if there is any further change of more than fifty percentage points (by reference to the new benchmark figure of 0% taxable), a further adjustment will be required.

Note: if the initial deduction was zero and the first use was taxable, a VAT credit would have been given to Mr H.

[1] This is the "normal" CGS annual adjustment which is based on 1/20.

[2] Interval in this case means the 12 month period beginning on 1/1/2011 that ends

31/12/2011.

[3] 33,750 represents the VAT deducted (€675,000) divided by 20 (number of intervals in the CGS adjustment period).

Example 20

Mr D develops a property that is completed on 1 January 2005. He does not deduct any of the VAT (€500,000) charged to him on the basis that he is going to use the property for the purposes of a fully exempt business – vocational training of hairdressers.

In 2010 Mr D spots an opening in the market and decides to use a significant amount of the space in the building for the purposes of running a hairdressing salon. The salon opens on 3 January 2012. As this is a "changed use" on or after 23 February 2010, the big-swing test applies to this property. During the year a fair apportionment of the use to which the property is put is 70% for the salon, 30% for continuing the training business.

At the end of the interval in which the salon opens (31/12/2012) Mr D is obliged to calculate if a big-swing adjustment is a required. As there is a change of more than fifty percentage points in the taxable use an adjustment is required. The formula to be used is:

(C - D) x N

C = reference deduction amount, D = interval deduction amount, N = number of full intervals remaining in the adjustment period for the property + 1

(0 - 17,500) x 13 = - €227,500.

This amount is given as a VAT credit to Mr D in the taxable period following the end of the interval in which the changed use took place. (The VAT credit is due in Jan/Feb 2013 taxable period). This amount corresponds to a credit of 13/20 of 70% of the non-deductible VAT (€500,000).

The benchmark taxable figure for the CGS for Mr D in respect of this property following this adjustment is 70%. The big-swing test will continue to apply until the end of the adjustment period and if there is a subsequent change of more than fifty percentage points (by reference to the new benchmark figure of 70% taxable), a further adjustment will be required.

Note: if the initial deduction was fully taxable and the changed use was exempt, a VAT claw-back would have arisen.

6.6 Interaction of Section 95(11) with section 95(4)(a)

Where a person has carried out a big-swing adjustment and paid over VAT to Revenue by virtue of a diversion of a transitional property from fully taxable to fully exempt use (other than letting) and that person subsequently creates an exempt letting of the property, there will be no deductibility adjustment in accordance with Section 95(4)(a). If an adjustment is based on a diversion of less than a 100% change then the figure to be used for "T" in the formula referred to in Section 95(4)(a) shall be reduced by the amount of the tax paid over under the big-swing adjustment for the purposes of calculating the VAT due when the exempt letting is created.

Example 21 – changed use, less than fifty percentage points “swing”.

Ms C develops a property, which is completed on 1 January 2005. She deducts all the VAT incurred in relation to the development on the basis that she will use the property for a fully taxable business, manufacturing furniture for sale.

In January 2013 Ms C begins providing insurance brokerage services as well as the existing furniture business. This represents a "changed use" and Ms C is therefore subject to the big-swing test in relation to that property.

At the end of the interval in which the brokerage business begins (31/12/2013) Ms C is obliged to calculate if a big-swing adjustment is required. The property is used for 30% exempt use (insurance business) during 2013. As there is not a change of more than fifty percentage points in the taxable use, no adjustment is required.[5]

The big-swing test will continue to apply until the end of the adjustment period and if there is any change of more than fifty percentage points (by reference to the benchmark figure of 100% taxable), an adjustment will be required.

[5] There is no obligation to make the "normal" CGS annual adjustment based on 1/20 because section 64(3) continues to be disapplied in respect of transitional properties.

Example 22 – Changed use where there was exempt use before 23 Feb 2010.

DevCo constructed a crèche and incurred €2m VAT on the development. The development was completed on 1 January 2008. It deducted all the VAT on the basis it was going to sell the crèche. DevCo was unable to sell the crèche and instead opened the crèche for operation on 1 April 2009. There was no CGS adjustment required as per Section 95(11) as it applied on that date.

On 1 January 2013 DevCo closed the crèche and began operating a nursing home. As this represents a "changed use", the “big-swing” test applies to the property. At the end of the interval in which the nursing home is opened (31/12/2013), DevCo is obliged to calculate if a big-swing adjustment is required. The benchmark figure is 100% taxable (as DevCo deducted 100% of the VAT on the development of the property). The use during 2013 is 0% taxable. As there is a change of more than fifty percentage points in the taxable use an adjustment is required. The formula to be used is:

(C – D) x N

C = reference deduction amount, D = interval deduction amount, N = number of full intervals remaining in the adjustment period for the property + 1

(100,000 – 0) x 15 = €1,500,000

VAT payable by DevCo in the taxable period following the end of the interval (year) in which the changed use took place. (The VAT is payable in Jan/Feb 2014). This amount corresponds to a claw-back of 15/20 of the VAT initially deducted.

The benchmark taxable figure for the CGS for DevCo in respect of this property after this adjustment is made is 0% taxable. The big-swing test will continue to apply until the end of the adjustment period and if there is any further change of more than fifty percentage points (by reference to the new benchmark figure of 0% taxable), a further adjustment will be required.

7. Capital Goods Scheme (CGS) — exporters

Certain exporters may receive supplies of goods and services at the zero rate of Value-Added Tax (VAT).

These supplies would include the sale of property to the exporter and construction services and other services and goods used by an exporter for the purpose of developing property.

Where an exporter has property-related costs zero-rated under this provision, special rules apply for the purposes of the Capital Goods Scheme (CGS).

The property related input costs are treated as if Section 56 had not applied to them.

Notional Value-Added Tax (VAT) is deemed to have been charged at the rates appropriate to the goods or services concerned. The notional VAT is treated as having been fully deducted by the exporter.

This means the exporter has the same responsibility within the CGS in respect of capital goods, as a company or individual who does not have a Section 56 authorisation.