

# Transfer of going concern

## 1. Introduction

In tax, the concept of 'transfer of a going concern' is important in many different areas. The most obvious ones are Entrepreneurs' Relief, disincorporation relief and VAT.

This podcast is going to concentrate on the VAT implications of a transfer of a going concern (TOGC) because this is a commercial risk that needs to be dealt with correctly when the transaction occurs. It is a complex area and the many decisions before the tribunal illustrate that HMRC frequently get it wrong, seeking VAT when it is not due.

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## 2. Entrepreneur's relief

The differential between income tax and CGT for individuals is substantial. Currently, we have a top rate of income tax of 45% but the top rate of CGT is 28% but if the disposal qualifies for entrepreneur's relief the rate is 10%.

Entrepreneur's relief is largely based on the old retirement relief which was last available in 2002–03 and its effect is to preserve the effective 10 % rate for businesses which applied under taper relief.

The relief is to be given if a claim is made in respect of 'qualifying business disposals', of which there are three:

- (1) a material disposal by an individual;
- (2) a disposal by an individual which is associated with a material disposal; and
- (3) a disposal by trustees.

Entrepreneur's relief is available on gains up to £10m for qualifying business disposals occurring on or after 6 April 2011. It is not available on the sale of assets. To qualify what is disposed of must be a business or part of a business carried on by the individual or by a partnership of which he was a member; the assets used for the purposes of that business.

A business is something more than a mere collection of assets. For the purposes of entrepreneurs' relief, it is defined as a trade, profession or vocation which is conducted on a commercial basis with a view to profit (TCGA 1992, s. 169S(1)). Thus relief is not due where an individual or partnership sells one or more of its business assets whilst continuing with its business as before.

Whether the subject matter of a disposal represented a part of a business or merely assets used in that business is a question of fact. The leading case on this point is **McGregor v Adcock 51 TC 692**, in which the taxpayer owned 35 acres of land and sold 4.8 acres for development. He continued farming the remaining land and claimed that as the sale of the 4.8 acres was a sale of part of his farming business. He lost his claim as what he sold were assets of the business but the business continued and no part of the business was sold.

Two further cases confirmed the courts thinking on the above point. The principle that emerged from the cases of **Atkinson (HMIT) v Dancer and Mannion (HMIT) v Johnston** [1988] BTC 364 is that the only relevant matters in a comparison of the position after the sale with that before are those caused by the sale; changes in activities and/or assets caused by matters other than the sale are irrelevant. In Mr Dancer's case the significant change in his business occurred when egg production ceased but there was no link between the cessation of egg production and the sale of the land. In Mr Johnston's case each of the two dispositions

had to be considered separately and the changes caused by each one were merely insignificant changes of scale. Accordingly neither taxpayer was entitled to the relief claimed.

It may seem a fine point of law but in a related case, **Jarmin (HMIT) v Rawlings** [1995] BTC 3, the taxpayer had for many years run a dairy business on 64 acres of land before selling 1.2 acres, including the milking parlour, at auction in October 1988. Between this date and completion of the sale in January 1989 some of the dairy herd was sold, the remainder being transferred to the taxpayer's wife's farm pending sale, the taxpayer having no further interest in or financial benefit from the milk production of these animals. All of the herd had been sold by May 1989. From January 1989, the taxpayer carried on the business of rearing and finishing store cattle on the land previously grazed by the dairy cattle. In this case the claim for relief succeeded because the part of the business related to milk production and a dairy herd had ceased. There was a disposal of a part of a business.

The concept of a business and part of a business can also be important for IHT and the new disincorporation relief.

### **3. VAT: The importance of TOGC**

VAT is a transaction based tax. With standard rate at 20%, it is essential that the nature of the supply is identified correctly. If the sale amounts to a transfer of a going concern (TOGC) for VAT purposes, e.g. because goodwill and stock are also sold, the transaction is outside the scope of VAT being a non-supply. The sale or transfer of a business as a going concern to a person who will carry on the business as the transferor has done is treated as not involving any supply for VAT purposes, and is therefore outside the scope of VAT, provided certain conditions are met (**Value Added Tax (Special Provisions) Order 1995 (SI 1995/1268), art. 5**). The same applies to the sale or transfer of part of a business which is capable of separate operation. Few areas of VAT law have caused as much trouble for traders and their advisers as the provisions for transfers of going concerns (TOGCs). This is partly because they depend on questions of fact which can be difficult to determine, partly because of some quite complex special conditions and partly because of the circumstances in which HMRC check the application of the law.

In practice this can be a difficult area and it is recommended that expert legal and tax advice should be obtained if the sums involved are material and significant. A vendor selling the assets of a business but not a part of the business should charge VAT whereas if it is a TOGC and the appropriate option to tax elections have been made for any elected property, no VAT should be charged. If property is involved, there may be implications for SDLT as well.

If there is doubt, any VAT potentially chargeable should be held in suspense until a ruling can be obtained and this is where expert legal advice should be obtained to protect the client's interest.

It is an area where HMRC frequently make mistakes and such an error could have commercial repercussions. For example, the difference to a micro business between being registered for VAT or not could be substantial. If an adviser is helping the client, it is important to get it right because any mistake could prove expensive.

### **Gargo and McWilliams t/a The Pende Café v HMRC, 2009 UK FTT 381**

**Point at Issue:** Whether a new trade had been acquired as a TOGC from a quite different business and therefore required to register from the outset.

**Facts:** HMRC considered the business begun by the appellants had the characteristics of a transfer of a going concern and should have been registered to VAT from the date of commencement. The previous business was a fine dining restaurant called The Courtyard with a licence to sell alcoholic liquor and the provision of high quality foodstuffs. The previous owner was made bankrupt but on deregistration had ticked the box, indicating a TOGC had occurred but the appellant had no knowledge of this.

Most of the assets of the previous business were not transferred but Ms Cargo and Ms McWilliams had previously worked as waitresses in that business as well as taking on two kitchen hands from the previous business but this was not under a transfer of a going concern.

The first quarter's activity indicated a turnover of £19,896 so HMRC multiplied this by four suggesting annual turnover would exceed the registration threshold and encouraging Ms Gargo to register for VAT voluntarily.

**Decision:** The judgement is fairly critical of the HMRC officer who failed to take into account that the café business was quite different from the fine dining experience with wines and a liquor licence of the previous business. He also failed to take into the account the seasonal nature of a café in a seaside town and therefore extrapolating by multiplying the summer trade by four, is not good judgement. The Tribunal found on the balance of probability that there was no transfer of a going concern.

The new business which Ms Cargo and Ms McWilliams commenced was quite different from the previous trader who had sold alcoholic liquor, had fine dining and remained open until late each evening whereas the café shut at 18.00.

The verbal advice given by HMRC officers was wrong and Ms Cargo, a young and inexperienced lady, had been misled into registering voluntarily.

There was a separate rental arrangement with the owner of the premises and the new business had far more stringent lease terms than the previous one, as well as not being able to obtain a liquor licence.

The trade which commenced was significantly different from the trade previously conducted by the now bankrupt previous trader. There was no transfer of a going concern and therefore the new business was not obliged to charge VAT. This would have been a significant additional cost to a café business selling teas, coffees, cakes and high teas.

**Input VAT tax denied because it was a TOGC rather than a purchase of assets.**

In **H Q Graphics Ltd v Revenue & Customs [2013]** UKFTT 226, the burden of proof lies with the appellant to show there had been a supply between the vendor of the machinery, Nowelle, and the appellant and that the supply was not part of a transfer of a business as a going concern (TOGC).

The vendor Nowelle had ceased to trade and owed VAT of £10,028.91

Nowelle's business was printing and in particular it serviced retailers providing them with large format and high quality banners advertising sales and promotions. Its customers included Selfridges and Marks & Spencers. Printing was digitised and different printers were needed to produce the different sizes of materials. The company employed staff who were skilled in operating the machines and also staff who involved in boxing / packaging materials and carrying out administration.

The company was registered for VAT and its business address was Unit 6, IO Centre, Hatfield, AL10 9EW. The claimant H Q Graphics Ltd operated from the same premises employed mainly the same skilled printing staff (15 out of 21 staff) and had common ownership and directors.

The Nowelle invoice was headed "Sale of Machinery" and was for £78,000 which included £13,000 VAT. The assets specified were various printers including a number of "hp Designjet 5500" printers, and a "Vutek PV UV 320" printer. The invoice also referred to "other assets, office equipment, computers, printers and racking as agreed which included "various Apple Mac Computers, Accessories & Software."

The unpaid VAT of Nowelle Ltd is £9,314.90 but Nowelle claimed it had accounted for and paid in full the VAT on the sale of the printing machinery to H Q Graphics Ltd. There is a suspicion that Nowelle may have owed other taxes and HMRC were not willing to grant the concession that might have netted the debts and allowed at least a partial repayment of VAT. The tribunal ruled in favour of HMRC's argument that what had occurred was a TOGC when they said at paragraph 150:

In our view the combination of these circumstances points towards there being a transaction between Nowelle and the appellant which amounted to a transfer of Nowelle's business as a going concern. Without labour, machinery and equipment or premises, Nowelle was not able to and did not continue with other business after the transaction.

Cases cited in this podcast that are useful in deciding whether a TOGC has occurred include

McGregor v Adcock 51 TC 692

Atkinson (HMIT) v Dancer and Mannion (HMIT) v Johnston [1988] BTC 364

Jarmin (HMIT) v Rawlings [1995] BTC 3

Gargo and McWilliams t/a The Pende Café v HMRC, 2009 UK FTT 381

In H Q Graphics Ltd v Revenue & Customs [2013] UKFTT 226