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REAL ESTATE ALERT

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ISSUE

IMPACT OF THE VAT RATE INCREASE ON FIXED PROPERTY RENTALS

The VAT rate increase impacts all taxable transactions, including fixed property rentals. Therefore, lessors and lessees of fixed property should carefully consider the implications of the VAT rate increase from 14% to 15%, effective 1 April 2018, on existing or soon-to-be-concluded lease agreements.

IMPACT OF THE VAT RATE INCREASE ON FIXED PROPERTY RENTALS

The VAT rate increase will not impact on residential rentals, although utility charges such as water, electricity, sanitation and refuse removal charges will increase as a result of the VAT rate change.

The VAT rate increase will, however, impact on all fixed property rentals other than residential dwellings.

The VAT rate increase impacts all taxable transactions, including fixed property rentals. Therefore, lessors and lessees of fixed property should carefully consider the implications of the VAT rate increase from 14% to 15%, effective 1 April 2018, on existing or soon-to-be-concluded lease agreements.

Residential property rentals

The supply of a dwelling for a private individual under an agreement for the letting and hiring thereof is an exempt supply for VAT purposes. Consequently, the VAT rate increase will not impact on residential rentals, although utility charges such as water, electricity, sanitation and refuse removal charges will increase as a result of the VAT rate change.

The VAT rate increase will, however, impact on all fixed property rentals other than residential dwellings. The implications of these rentals are dealt with below.

Rental charges for rental periods before, on or after 1 April 2018

Rental charges for periods of rental prior to 1 April 2018 are subject to VAT at 14%, while rental charges for periods commencing on or after 1 April 2018 will be subject to VAT at 15%. These rules apply irrespective of whether the lessor issues an invoice for the rental charges or if the lessee makes payment before or after 1 April 2018.

Rental charges for rentals commencing before and continuing after 1 April 2018

Where rentals are charged for a rental period commencing before and ending after 1 April 2018, the lessor is required to apportion the rental on a fair and reasonable basis between the period before 1 April 2018, and the period on or after 1 April 2018.

The portion of the rental payable which is attributable to the period before 1 April 2018 will attract VAT at 14%, whereas the portion of the rental payable for the period on or after 1 April 2018 will attract VAT at 15%. The lessor will be required to prove that the apportionment was done on a fair and reasonable basis.

The apportionment of the rentals will be required irrespective of whether an invoice is issued before or after 1 April 2018, or whether payment is made before or after that date.



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IMPACT OF THE VAT RATE INCREASE ON FIXED PROPERTY RENTALS

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The 'new' rental amount payable is calculated by multiplying the current VAT inclusive rental by 1.0087719, rounded off to the nearest cent.



Property rates

Although property rates are subject to VAT at the rate of zero per cent when charged by the municipality to the lessor, such property rates are considered to form part of the rental consideration for the use of the property when on-charged by the lessor to the lessee. Such on-charged 'property rates' are therefore subject to VAT at the standard rate, and the same rules described above that apply to the rentals, equally apply to the property rates which are on-charged to lessees.

Rental agreements entered into before 1 April 2018

Section 67 of the VAT Act governs the situation where a lease agreement was entered into before 1 April 2018. It entitles the lessor to recover from the lessee, in addition to the amounts payable by the lessee to the lessor as per the lease

agreement, the additional amount of VAT that becomes payable on or after 1 April 2018 as a result of the VAT rate increase.

The lessor is therefore entitled to increase the rental by the additional VAT amount payable as a result of the VAT rate increase. The 'new' rental amount payable is calculated by multiplying the current VAT inclusive rental by 1.0087719, rounded off to the nearest cent.

However, the lessor will not be entitled to recover the additional VAT amount payable from the lessee, if the lease agreement specifically excludes the entitlement of the lessor to recover the additional VAT amount from the lessee. In such instances the lessor will nevertheless be liable to account for output tax at 15%.

*Gerhard Badenhorst and
JD van der Merwe*



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