

5% VAT on builder services for dwellings

(Lecture B1205 – 12.34 minutes)

Background

The 5% rate of VAT applies to some builder services carried out on residential properties. As a lot of income generated from residential properties is exempt from VAT (eg rental income), it is important that property owners are clear about when the 5% VAT rate might apply instead of the usual 20%. The rate applies to materials provided by the builder as part of his work, a further potential VAT saving.

Residential conversion projects

Builder services that relate to the conversion of a non-residential building into dwellings are subject to VAT at 5% rather than 20%.

Example of residential conversions:

- Office block is converted into apartments;
- Barn is converted into a house.

Example of project which does not qualify: A bungalow is built on land next to a farmhouse but the two properties can only be sold together as a single purchase – the bungalow fails one of the conditions of a ‘new dwelling’ – the building work is standard rated.

Legislation – VATA1994, Sch 7A, Group 6.

There is often concern amongst advisers that in the case of a conversion to dwellings, the builder must be given a signed certificate from the developer confirming the creation of dwellings – and this should be available to HMRC in the event of a compliance visit. This is not necessary – and is confirmed by VAT Notice 708, para 17.1, which states that certificates are only needed when 0% or 5% VAT supplies are being made in connection with a building used for a ‘relevant residential purpose’ (eg elderly persons home) or for a ‘relevant charitable purpose’ (eg a place of worship).

Note - the 5% rate never applies to ‘professional services’ such as architects, surveyors, project managers, solicitors – their services are always standard rated.

Existing dwellings

The 5% rate applies to construction services for an existing dwelling under 2 circumstances:

1. Change number of units - after the building work has been carried out, there is a different number of dwellings than when the project started eg a detached house is converted into two semi-detached houses or vice versa. For this purpose, the conversion of a house into HMOs falls within the 5% rate;

2. Property empty for at least two years - work is carried out on a residential property that has not been lived in for at least two years at the time when the work starts. The builder will need third-party evidence of the empty period eg council tax data, electoral register information etc.

Recent tribunal case

Gareth Bertram (TC7524) supplied construction services in relation to 25 residential properties that were assets of a separate property company that he owned. These properties were mainly semi-detached houses which had adjacent land capable of building another dwelling. The houses were converted into HMOs (Houses of Multiple Occupation) and, in 14 cases, a new dwelling was created on the adjacent land. In 11 cases, the existing property was extended to create bigger HMOs. The property company then rented out the HMOs via a letting agency.

The taxpayer's approach was simple: he claimed that his work for his property company was subject to 5% VAT. This made his record-keeping simple ie there was no need to worry about which jobs might be subject to 0%, 5% or 20% VAT, as HMRC felt was the case.

HMRC's position was more complicated:

- The conversion work to HMOs was subject to 5% VAT but Mr Bertram could produce no evidence that he had created HMOs so the work was standard rated;
- The extensions were subject to 20% VAT because the building had not been empty for at least two years;
- In the case of a new dwelling built on adjacent land, the work would be standard rated until the point when planning permission had been received from the local authorities, and then subsequent services could be zero-rated ie the conditions for a new dwelling had been met.

HMRC raised an assessment for £59,184 for periods 12/14 to 3/17 based on a straight-line apportionment between the 25 properties.

The decision

It was difficult for the taxpayer to prove the conversion of the house into HMOs had taken place because neither statutory planning consent nor building control approval was needed. But the judge accepted that £1,000 per property was spent on certain basic works, such as fitting locks to each bedsit, and this work should be subject to 5% VAT. The appeal was dismissed on all other issues.

Learning points

If your clients are involved with building work on residential property projects, there are two main situations:

Project 1 – create an extra new dwelling on adjacent land and improve the existing dwelling – building work will be zero-rated in relation to work carried out on the new dwelling. It must meet all of the conditions of a dwelling specified in VAT Notice 708, para 14.2. Work on the existing dwelling will be standard rated unless it has not been lived in for at least two years, in which case 5% VAT will apply.

Note – the new dwelling must be capable of being sold in its own right, ie not only as part of a package that includes the original dwelling.

Project 2 – convert an existing dwelling into two or more dwellings eg a house is converted into a ground floor and first floor flat. As long as each newly created dwelling meets the conditions of a dwelling, then 5% VAT will apply to builder services.

Contributed by Neil Warren