

VAT brief | Transfer of a going concern

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Bahrain's National Bureau for Revenue (NBR) released its VAT guidelines on transfers of going concerns (TOGCs) on 17 August 2020. In this brief, we highlight key clarifications and interesting points raised in the guide.

What is a transfer of a going concern?

A transfer of a going concern is essentially where one person transfers all that is required to run an operating business to another person. Where these requirements are met, a TOGC is out of scope for VAT, preventing a large amount of VAT being charged on a business sale and so limiting any impact on cash flow or any risk that the seller fails to pay output VAT.

TOGCs are outside the scope of VAT if:

- The transferor is VAT-registered.
- The transferee is VAT-registered (or is liable to be registered as a result of the TOGC).
- All or part of a business that constitutes an economic activity capable of being operated on an independent basis is transferred.
- The transferee immediately uses the acquired assets to conduct the same or a similar economic activity.
- Both the transferor and the transferee notify the NBR of the transaction within 30 days.

A transfer of only business assets may not constitute a TOGC. TOGCs normally comprise the transfer of:

- Tangible assets – such as real estate, vehicles, machinery, inventory and cash
- Intangible assets – such as goodwill, intellectual property, software and customer lists
- Liabilities – including the assumption of an obligation to pay any debts

The transfer of a commercial registration is not necessarily indicative of a TOGC. However, the transfer of goodwill is normally a strong indicator of a TOGC. Equally, the non-transfer of premises, stock or customer contracts does not necessarily mean a TOGC has not taken place.

The NBR says that **immediately** after any TOGC, the transferee must use the transferred goods services to carry out the **same or a similar economic activity**.

- The NBR may accept some delay in use (for example, for refurbishment) but ultimately this depends on the facts.
- The same or similar economic activity essentially means that the assets must be used in a similar industry as previously operated by the transferor.
- Consider how the transferee intends to use the assets on acquisition – if the intention is to only carry on the same economic activity for a short time before changing the activity, the TOGC provisions may not apply.

If both the transferor and the transferee do not notify the NBR within 30 days of the transfer, the TOGC provisions do not apply and the transferred assets may be subject to VAT.

Areas to be carefully considered

- The **progressive transfer of assets** does not preclude the application of the NBR's TOGC provisions but may raise issues.
- Any **assets transferred that will not be used in the ongoing business** are not covered by the TOGC provisions.
- Following a TOGC, a customer may **return goods** which were initially supplied by the transferor. The NBR seems to suggest that any adjustment to a supply made before the TOGC should be a matter between the transferor and the third-party. However, this may contradict the intent of the TOGC provisions (that is, the transferor has transferred its rights to all business assets, including debts, to the transferee). The NBR is allowing transferees to issue credit notes in these circumstances - and when repairs are provided under warranty.
- Transferees are technically not entitled to claim **bad debt relief** for supplies made by the transferor. However, the NBR allows transferee to claim bad debt relief when all other requirements are met.
- Transferees are liable for VAT on the **deemed supply of assets** where the assets were transferred as part of a TOGC and the transferor originally reclaimed input VAT on their purchase. This may clash with the spirit of the TOGC provisions and could cause an administrative burden for taxpayers.
- The transfer of **occupied real estate** as part of a business may qualify for TOGC. Where the only economic activity is rental income, the TOGC provisions are unlikely to be met as the parties are unlikely to be registered for VAT.
- A **transfer of shares** in a company is an exempt supply. However, the transfer of a holding company that is actively involved in the management of its subsidiaries may qualify for TOGC.
- Consultancy costs and legal fees related to TOGCs are considered general overhead costs and **input tax may be recovered by the transferor** in accordance with the normal rules. Where part of a business is transferred, focus on the general overheads applicable to that part.
- Transferee's costs related to the TOGC are also considered general overheads and so **input tax may be recovered by the transferee**, subject to the normal input VAT recovery rules.
- Members of **VAT groups** can individually transfer assets to a transferee and satisfy the TOGC provisions. While VAT groups are treated as a single person for VAT purposes, they are still separate legal entities. A transfer into a VAT group can qualify for TOGC, providing the VAT group still makes supplies to customers outside the VAT group.

Transfers of going concerns are often complicated - particularly from a VAT perspective. If you are considering a TOGC, we strongly recommend involving an advisor before completing any transfer.

Disclaimer: This sector spotlight is based on our review of the NBR's TOGC guide, our understanding of Bahrain's VAT legislation and the GCC framework agreement and general VAT principles and is for general information only. Seek professional advice in relation to your particular circumstances.

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