

KINGDOM OF BAHRAIN

**VAT TRANSFER OF A GOING CONCERN
GUIDE**

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الجهاز الوطني للإيرادات

National Bureau for Revenue

Preface

This guide sets out general principles relating to the concept of VAT on transfer of a going concern.

This guide is intended to provide general information only, and contains the current views of the National Bureau for Revenue (NBR) on its subject matter. This Guide is not a legally binding document, and does not commit the NBR or any other person, including a VAT payer, in respect of any transaction. This document should be used as a guideline only and is not a substitute for obtaining competent legal advice from a qualified professional.

The main principles of the VAT system in the Kingdom of Bahrain are set out in the VAT General Guide issued by the NBR which is available on the NBR's website, www.nbr.gov.bh. This document should be read in conjunction with the VAT General Guide.

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1. Introduction to TOGC concept

1.1. Introduction

The sale of the assets of a business by a VAT registered person will normally be subject to VAT. VAT will apply at the appropriate rate on the consideration payable for each asset sold.

The VAT Law and Executive Regulations contain provisions on the VAT treatment of the surrender by a VATable person of his economic activity (or part of his economic activity) to another VATable person.¹ Where certain conditions are met, such a surrender is treated as being outside the scope of VAT and any assets transferred as part of the surrender will not be subject to VAT.

Any VAT payer intending to sell or otherwise transfer a business to another person should read this Guide with a view to determining whether the transfer may be the surrender of an economic activity for VAT purposes, resulting in the transaction being outside the scope of Bahrain VAT.

1.2. Terms used in this Guide

The surrender by a VATable person of his economic activity is often referred to as “a transfer of a business as a going concern” or “TOGC”. In this Guide:

- The surrender of an economic activity is referred to as a TOGC;
- Where such a surrender meets the conditions in Article 11 of the Bahrain VAT Law and Article 12 of the VAT Executive Regulations (the “TOGC provisions”) to be treated as outside the scope of VAT, it is called a “Qualifying TOGC”;
- The person surrendering the economic activity / making the transfer of the going concern is called the “Transferor”; and
- The person receiving the surrender of the economic activity / going concern is called the “Transferee”.

1.3. Purpose of TOGC Provisions

The purpose of the TOGC Provisions is to eliminate what could otherwise be a large cashflow cost to the parties of having to pay VAT on the surrender / transfer of a business. Further, where there is a Qualifying TOGC, the Transferor does not need to individually value the assets being transferred for VAT purposes in order to apply the correct VAT treatment (e.g. 5%, exempt).

¹ Article 11 of the Bahrain VAT Law, Article 12 of the VAT Executive Regulations

The TOGC Provisions also protect government revenue by avoiding a situation whereby one party who acquires a business claims input VAT, but the seller has not actually paid the output VAT on the transfer (e.g. due to liquidation, insolvency etc).

2. Economic activity / going concern

In order for there to be a TOGC, there must be a transfer of an economic activity. An economic activity is defined as:

An activity that is conducted in an ongoing and regular manner for the purposes of generating income, and includes commercial, industrial, agricultural or professional activities or services or any use of tangible or intangible assets, and any other similar activity.²

A business which is a “going concern” is one which, at the time of transfer, is operational, and has all parts and features necessary to keep it in operation.

Further details on what constitutes an economic activity, can be found in the VAT Economic Activity Guide.

² Article 1(16) of the Bahrain VAT Law

3. Conditions to be a Qualifying TOGC

3.1. Introduction

In order to be a Qualifying TOGC, certain conditions must be met by the Transferor and the Transferee. These are discussed below.

When applying the below rules to determine whether a transaction is a Qualifying TOGC, the substance of the transaction should be considered, not its form. All relevant circumstances must be considered, but ultimately the most important factor is whether the transaction results in the Transferee having a going concern which he can carry on without any disruption or interruption.

There are factors that are relevant in determining whether the Transferee receives a going concern that he may carry on. The following are relevant in this regard:

- An explicit transfer of goodwill of a business is an indicator that a business has been transferred. However, if there is no such explicit transfer, this does not mean that a business has not been transferred.
- If business premises, stock or customer contracts are not transferred, this does not mean that a business has not been transferred if the Transferee is still able to carry on the business of the Transferor.

The use to which assets are put following a transfer of a business can impact whether a transfer is a Qualifying TOGC. A transaction treated as a Qualifying TOGC by the Transferor and Transferee could ultimately be held by the NBR to be a VATable supply of goods and services, subject to VAT. In such circumstances, the associated liability (together with penalties) would ultimately become payable by the Transferor. For this reason, the parties may wish to consider including appropriate clauses in the legal agreements to protect their position.

3.2. Transfer includes all or part of a business capable of being operated on an independent basis

The transfer must include all or part of a business that constitutes an economic activity capable of being operated on an independent basis.

The purpose of a TOGC is to put the Transferee (i.e. the purchaser) in possession of a business, rather than merely acquiring assets. Therefore, the assets and liabilities transferred must include those parts of a business that enable the Transferee to engage in an economic activity that is capable of being operated on an independent basis. This does not require the economic activity to be operated independently, merely that it must be capable of operating independently.

If part of a business is transferred, and that part would not put the Transferee in a position to operate a business independently, i.e. without those assets and liabilities being incorporated

into a larger business or other assets being acquired from a third person, the transfer will not be a Qualifying TOGC.

A simple transfer of assets may not constitute a business capable of being carried on independently. For example, a sale of the entire stock of a business or an empty warehouse previously used for the Transferor's manufacturing activities is unlikely to be regarded as a business capable of being carried on independently. This is because the stock or warehouse is only one component of a functioning business.

The parts of a business transferred generally include tangible assets, rights and other intangible assets as well as liabilities of the business:

- Tangible assets

Tangible assets are physical goods held by a VATable person and include fixed assets (such as real estate, vehicles, machinery and office equipment) and current assets (such as inventory and cash).

- Intangible assets

These are goods that are not physical in nature, but are recognized by a business. Examples of intangible assets include (but are not limited to) goodwill, patented technology, computer software, databases and trade secrets, trademarks, internet domains, video and audiovisual material, customer lists, mortgage servicing rights, licensing, royalty and standstill agreements, franchise agreements, customer and supplier relationships and marketing rights.

- Liabilities

Liabilities include bank loans, trade creditors and other payables (including debts due to the Transferor by the business being transferred). In many cases, there may not be a formal transfer of a debt (e.g. due to the difficulty in securing agreement from creditors), but the Transferee will assume the obligation to pay the debts on behalf of the Transferor. In such cases, the Transferor remains legally liable to pay the debts, but, under the legal arrangements between the Transferor and Transferee entered into to effect the TOGC, the Transferee pays the debts. Payment can be by way of a once off payment or by way of ongoing payments over an agreed period of time.

Whether a Commercial Registration is transferred along with the assets of a business will be relevant, but will not in itself determine whether a transfer includes all or part of a business capable of being operated on an independent basis. The following are relevant in this regard:

- If a Commercial Registration is transferred together with the constituent assets of the underlying business, it is likely that, for the purposes of the TOGC provisions, all or part of a business capable of being operated on an independent basis will have been transferred.
- A part of a business capable of being operated on an independent basis can be transferred without the Commercial Registration of the Transferor also being transferred.

- A Transferee could acquire part of a Transferor's business conducted under a Commercial Registration, without acquiring the Commercial Registration itself, and operate that business under the Transferee's existing Commercial Registration.
- Some businesses may operate without a Commercial Registration (e.g. one is not required, or the business owner has not complied with the obligation to obtain one). This does not mean that an economic activity does not exist or that a transfer of the business is not all or part of a business capable of being operated on an independent basis for the purposes of the TOGC Provisions.

Examples		Capable of independent operation?
	Assets etc. transferred	
1.	<i>The sale of an oil tanker used by the Transferor as part of its business of transporting oil.</i>	No
2.	<i>The sale of an oil tanker per 1 with assets enabling the Transferee to carry on an oil delivery business (e.g. office with telephones to take orders, storage tanks for oil).</i>	Yes
3.	<i>The sale of an oil tanker per 1 with the assignment of existing customer contracts to deliver oil.</i>	Yes
4.	<i>The sale of an oil tanker used in a business of leasing such tankers to third parties where the tanker is subject to a lease to a third party.</i>	Yes
5.	<i>The transfer of all of a business' stock in trade without any other assets.</i>	No
6.	<i>The transfer of the stock in trade, the fittings of a business together with the grant of a lease by the Transferor to the Transferee.</i>	Yes
7.	<i>The transfer of patent rights where licensing agreements have been signed with third parties to use the patents and the patent rights are transferred with the benefit of the agreements with the third parties.</i>	Yes

3.3. Transferor must be VAT registered

The Transferor must ensure that he is registered for VAT on the date the TOGC is effected. The effective date of registration per the VAT registration certificate should be on or before the date of transfer.

3.4. Transferee must be VAT registered or become liable to be registered as a result of the TOGC

In order for the transfer to be a Qualifying TOGC, the transferee must:

- Be registered for VAT at the date of the TOGC; or
- Become obliged to register as a result of the TOGC. This means that, as a result of the TOGC, the Transferee's annual supplies (as defined in Article 34 of the VAT Regulations) will exceed the mandatory registration threshold or will be expected to exceed the threshold.

See the section "VATable Persons and VAT registration" in the VAT General Guide for more information on the meaning of a "VATable person" and when a person is obliged to register due to exceeding the mandatory registration threshold.

3.5. The Transferee must immediately use the assets acquired to conduct the same or a similar economic activity

3.5.1. Immediate use of goods and services acquired

The purchaser must, immediately after the surrender, use the goods and services acquired to conduct the same or a similar economic activity. In certain circumstances, there may be some delay in using the goods and services (e.g. necessary refurbishment to a business premises). Where there is a delay between the date of the transfer and the date that the relevant assets, liabilities etc are used to conduct an economic activity, the delay needs to be considered in the context of the type of business concerned.

Example 1

The business assets (both tangible and intangible) of Burgers, a restaurant located in Bahrain, is sold to a global fast food company. Following the sale, the restaurant is closed for two months while the fast food company renovates and redecorates to bring the design of the restaurant in line with global branding. As this delay is due to works being carried out to enable the assets to be used to continue to operate an economic activity similar to that of the Transferor (Burgers), the requirement to immediately use the goods and services acquired will be met.

Example 2

Kick It, a sports complex located in Bahrain, is sold to a local entrepreneur, Ali, in June. Ali continues to run the business as a sports arena for people to play football outdoors. In July, Ali closes the business for three months because of high humidity during the summer months. The previous owner had also closed for the summer period. Despite this business not operating continuously, as the break in trading is part of the normal trading pattern of the business, the condition that the purchaser must immediately use the goods and services will be satisfied.

3.5.2. Same or similar economic activity

In order to satisfy this condition, the Transferee must ensure that the assets purchased from the Transferor are used to carry out an economic activity which is the same or similar (i.e. the assets are not fundamentally changed and are used in the same way) to the previous economic activity being performed by the Transferor. If the Transferee uses the economic activity acquired for another type of business, this condition will not be met and the transaction will not be a Qualifying TOGC.

Example 1

Gulf Clothing manufactures children's clothes in Bahrain. Gulf Clothing receives an offer from Manama Fashion, a women's clothing business, to sell its business (comprising all business assets). Following the transfer of Gulf Clothing's business, Manama Fashion uses these assets to manufacture women's clothing.

While the business assets transferred are now being used to make women's clothing rather than children's clothing, the purpose of the business remains the same, i.e. the manufacture and sale of clothing. Therefore, as the economic activity being pursued by the transferee (Manama Fashion) is the same as transferor (Gulf Clothing), the condition that the Transferee carries on the same or a similar economic activity will be satisfied.

Example 2

Bahrain Foods Co operates as a food wholesaler in Bahrain. It sells its entire business to Grocery Products Co which uses the business assets to sell food products to retail customers. The fact that the type of customer has changed will not change the fact that a similar economic activity is being carried on by Grocery Products Co as Bahrain Foods Co.

Example 3

Arabian Gulf Shipping Company ("AGSC") provides warehouse storage services to non-residents importing goods into Bahrain. AGSC is selling the warehouses to an entertainment company who will modify them to so they can run entertainment events. The sale of these warehouses represents the core of the AGSC's economic activities. However, as the transferee is not using the warehouses for the same purpose (i.e. as an entertainment venue rather than for storage), this transaction is not a continuation of the AGSC's economic activity. As such, this sale will not be a TOGC.

This condition does not require that the Transferee must have been carrying on the same type of business as the Transferor prior to the transfer. The Transferee could be carrying on an entirely different type of business, acquire the economic activity from the Transferor and then carry on two separate businesses.

Example

Bahrain Trading Co imports clothing into Bahrain and sells this clothing wholesale to clothes shops in Bahrain. It purchases a food production business from another Bahraini entity and carries on this business in addition to its clothing wholesale business.

The fact that Bahrain Trading Co had not been engaged in food production before purchasing the food production business will not impact the TOGC rules applying.

The Transferee may acquire the business with the intention to use the assets for a different kind of business in the future. If the Transferee uses the assets transferred to carry on the same activity as that previously carried on by the Transferor for a period of time, and then uses the assets for another type of business after a period of time, the transfer may still be a Qualifying TOGC. However, if at the time of acquiring the business, the Transferor has the intention of using the assets for a different type of business, but carries on the existing activity for a limited period with the sole purpose of availing of the TOGC provisions, the transfer will not be a Qualifying TOGC.

Example

Hotel Co owns a hotel building and uses it to operate a hotel business. Hotel Co sells its entire business (including the building) to DevCo. Following the sale, DevCo continues to operate the hotel for thirteen months and then shuts it down. It then redevelops the hotel into apartments. It is clear from DevCo's business plan that it had acquired the assets with the sole intention of redeveloping the property. On this basis, even though DevCo carried on the hotel business for a period of time, it will not be regarded as carrying on the same or a similar economic activity and the transfer will not be a Qualifying TOGC.

3.6. Notification

In order for a transfer to be a Qualifying TOGC, both the Transferor and the Transferee must independently notify the NBR of the transaction within 30 days of the sale / transfer. Notification should be on forms which can be obtained from the NBR.

Where a notification is not submitted by both the Transferor and Transferee within the 30 day period, the sale will not be considered as a TOGC and, in such circumstances, assets transferred by the Transferor may be VATable supplies subject to VAT. The Transferor would be required to pay any VAT arising to the NBR and to issue VAT invoices in respect of the supplies made.

4. Other considerations

4.1. Transfer of assets over a period of time

Usually, when a business is transferred, the business assets and liabilities will be transferred at the same time. However, there may be instances where assets and liabilities are transferred over a period of time. This does not, in itself, prevent the transfer from being a Qualifying TOGC. Where assets and liabilities are transferred over a period of time, both parties will need to consider whether each transfer is a separate supply or forms part of the TOGC.

Example

Knitwear Co is a knitwear manufacturer in Bahrain. It purchases stock which it uses to manufacture its products from Bahrain Distribution Co, a domestic wholesaler. Both parties are registered for VAT in Bahrain.

During April 2019, Knitwear Co purchased 1,000 units of stock from Bahrain Distribution Co. On 30 April 2019, Knitwear Co purchased all of Bahrain Distribution Co's business assets. This transaction meets the conditions to be a Qualifying TOGC.

The acquisition of the 1,000 units of stock can be seen to be consistent with the transfer of the business assets, which is the substantive transaction between Knitwear Co and Bahrain Distribution Co. Therefore, as this stock comprises a business asset of Bahrain Distribution Co, its transfer forms part of the Qualifying TOGC relating to the business assets and the supply of the stock is therefore outside the scope of Bahrain VAT under the TOGC Provisions.

If, however, when Knitwear Co purchased the stock, the parties had not formed the intention to enter into the transfer of the other business assets from Bahrain Distribution Co to Knitwear Co, the sale of stock would be a VATable supply and would not be regarded as forming part of the TOGC.

4.2. Assets not used to continue the business

Assets transferred that will not be used to continue the economic activity previously carried out by the Transferor will not fall within the TOGC Provisions.

Example

123 Construction W.L.L. transfers all of its assets to Century Builders W.L.L. Both entities are resident in Bahrain and are registered for VAT. Included in the assets transferred is a boat previously used by one of the owners of 123 Construction W.L.L. As the boat will not be used to carry out the economic activity previously carried out by the Transferor (as it was used for private purposes), its transfer will not form part of the assets to which the TOGC Provisions will apply. Hence, 123 Construction W.L.L. will need to account for VAT on the sale of the boat.

4.3. Successive transfers

The successive transfer of business assets between VATable persons will not meet the TOGC criteria. For example, where the sale of business assets from a Transferor to a Transferee, are immediately sold by the Transferee to a VATable third party, the TOGC rules will not apply. This is because the Transferee does not use the assets to carry on the economic activity acquired from the Transferor. In this case, both transactions will be subject to VAT at the appropriate rate.

4.4. Transactions after a Qualifying TOGC

4.4.1. Returned goods / discount or rebate

Following a Qualifying TOGC, a third party may seek to return goods supplied by the Transferor, or may claim a discount or rebate in respect of a supply made prior to the Qualifying TOGC.

Any adjustment to a supply made before a Qualifying TOGC should be a matter between the Transferor and the third party. However, the NBR will, on a concessional basis, permit the Transferee to issue a credit note and to make an adjustment on its VAT return in respect of such transactions provided there is no loss of revenue to the NBR. The credit note should meet all of the conditions for credit notes as described in the “Issue of a credit note” section of the VAT General Guide.

4.4.2. Goods under warranty

A Transferor may have made supplies of goods under warranty and, following a Qualifying TOGC, the customer may wish to return goods for repair or replacement. From a technical perspective, if a Transferee repairs or replaces the goods, it may not claim input VAT in respect of the cost of repair or replacement as the cost does not relate to VATable supplies made by the Transferee.

In these circumstances, the NBR will, on a concessional basis, permit a Transferee to claim input VAT on repair / warranty costs incurred in relation to supplies made by a Transferee provided the Transferor would have been entitled to claim such input VAT if it had not entered into the Qualifying TOGC and there is no loss of revenue to the NBR.

4.4.3. Bad debts

If, as part of a Qualifying TOGC, a Transferor transfers debts relating to the business, and these are subsequently determined to be bad debts, the Transferee is not entitled to bad debt relief under Article 30 of the VAT Executive Regulations. This is because the Transferee did not make the original VATable supplies to which the debts relate.

Where a debt has been transferred as part of a Qualifying TOGC and this debt subsequently becomes bad, the NBR will, on a concessional basis, allow bad debt relief to the Transferee, provided all of the conditions set out in Article 30 of the VAT Executive Regulations (as

explained in the “Bad debts relief” section of the VAT General Guide have been met and there is no loss of revenue to the NBR.

4.4.4. Deemed supplies

The Transferee will be liable for VAT on a deemed supply of assets where the assets were transferred to him as part of a Qualifying TOGC and the Transferor originally reclaimed input VAT on the purchase of those assets.

4.5. Transfer of exempt assets

4.5.1. Introduction

The transfer of certain assets are exempt from VAT. Such assets include real estate and shares. However, the transfer of assets that are normally exempt from VAT may form part of the transfer of a business (including other assets such as stock, furniture, machinery and intellectual property). In such a case, the transfer of the assets which would normally be exempt from VAT may form part of a Qualifying TOGC and their transfer may therefore be out of the scope of VAT.

The following sections discuss the circumstances when transfers of real estate and shares may form part of a Qualifying TOGC.

4.5.2. Real estate

The transfer, sale or lease of real estate in Bahrain is exempt from VAT. See the VAT Real Estate Guide for further information on the VAT treatment of real estate generally.

Real estate occupied for business purposes

Where real estate assets which are occupied for business purposes are transferred as part of a Qualifying TOGC, the transfer of the real estate will form part of the TOGC and will therefore be outside the scope of VAT.

Example

Bottling Co is a VAT registered drinks bottling company based in Bahrain. In the course of a transaction which meets the conditions to be a Qualifying TOGC, Bottling Co agrees to sell all of its business assets to SoftDrinks Co. These assets include Bottling Co’s freehold interest in a warehouse used by it as its main manufacturing plant.

Although the supply of real estate is normally an exempt supply, the transfer of the warehouse to SoftDrinks Co as part of a Qualifying TOGC will be out of scope of Bahrain VAT as it is part of the business assets forming the economic activity being transferred.

Investment / rental property

The mere ownership of real estate where that real estate does not provide an ongoing income stream is unlikely to be regarded as an economic activity. An example of such ownership is the holding of a freehold interest in an unoccupied villa where the owner makes no attempt to find a paying tenant (either short or long term), but merely holds the asset with an expectation that it may be sold at some future date for a profit, or holds it to give to a child in due course.

The ownership and exploitation of real estate used for investment purposes is an economic activity from a VAT perspective. For this purpose, exploitation generally involves renting the property on a short or long term basis. It could also involve granting rights to use or exploit the property such as a right to mine or farm the property in return for consideration. Where a property is temporarily vacant, but the owner is actively seeking a tenant to occupy it, this will not prevent that property from being part of an economic activity carried out by the property owner.

The transfer of real estate such as a rental property may fall to be treated as a Qualifying TOGC if all of the requirements as discussed in this Guide are met. Where, however, property rental is the only economic activity carried out by either or both of the Transferor or Transferee, the conditions for a Qualifying TOGC will not be met as either or both parties will not be registered for VAT purposes.

Example

Hamala Housing is a Bahraini VAT registered business which owns a diverse portfolio of Bahraini commercial and residential real estate. Hamala Housing is in the business of both selling and leasing this real estate. Hamala Housing has agreed to sell off its real estate portfolio to Middle East Manors, a VATable person in Bahrain. The following are included in Hamala Housing's portfolio at the time of sale:

- *Unoccupied properties for which Hamala Housing is seeking tenants;*
- *Rented properties where the lease agreements are due to expire before the sale to Middle East Manors is complete, but for which Hamala Housing is seeking to renew the leases or to source new tenants;*
- *Rented properties with lease agreements which will not expire until some time after the sale to Middle East Manors is complete; and*
- *Unoccupied properties where leases have been signed, but the term of these leases will not start until after the sale to Middle East Manors;*
- *Newly built properties in respect of which sale agreements have been signed, but where completion of the sales will not occur until after the sale to Middle East Manors.*

Middle East Manors will use the assets acquired to expand its own real estate rental portfolio in Bahrain. As all of the assets of Hamala Housing are being sold and all of them are used as part of its economic activity, the sale of the assets should be a Qualifying TOGC and thus outside the scope of VAT.

4.5.3. Shares

A transaction whereby one person merely transfers shares in an entity to another, without any other assets being transferred, will be exempt from VAT. This will be the case even where the entity is a trading company. It does not matter whether the shareholding being sold is a minority or majority interest. Such a transaction cannot be a Qualifying TOGC as the mere holding of shares is not an economic activity for VAT purposes.

Where the owner of shares (e.g. a holding company) is involved in actively managing entities in which he owns the shares, the management activity together with holding the shares may be an economic activity. A transfer of the management activity with the shares may therefore constitute the transfer of a business and may be a Qualifying TOGC if the conditions set out at section 3 of this Guide are met.

Example

HoldCo is a Bahraini company that holds shares in a number of trading subsidiaries. HoldCo has a number of employees that are involved in providing management and other services to the subsidiaries such as human resources and negotiating favorable terms with banks for financing. HoldCo charges a fee for these activities to its subsidiaries. HoldCo also incurs other operational costs and recharges these to its subsidiaries. HoldCo is registered for VAT and charges VAT on the fees charged to its subsidiaries.

HoldCo agrees to transfer the shares in its subsidiaries to GiltCo, another Bahraini company. HoldCo will also transfer the management activities it carries out in relation to the subsidiaries and its employees will also be taken on by GiltCo. GiltCo will continue to provide the services to the subsidiaries previously provided by HoldCo.

HoldCo will be regarded as conducting an economic activity. The transfer of assets, including the shares, will be a Qualifying TOGC and will be outside the scope of VAT.

4.6. Business records

A Transferor is required to comply with the requirements to retain records for VAT purposes, even where he transfers his entire business to a Transferee and ceases economic activity entirely. A Transferee must retain records relating to the business from the time he acquires it. See the “Record keeping” section of the VAT General Guide for further information.

The TOGC Provisions do not require a Transferor to provide the Transferee with business records relating to his conduct of the economic activity prior to the transfer. However, it is good practice for a Transferor to make available any business records relating to the business being transferred to a Transferee. These records may include:

- VAT liabilities outstanding on the date of the TOGC;
- Copies of accounting books and records, and VAT invoices, debit/credit notes issued and received;
- Copies of any correspondence with the NBR in relation to VAT;
- Details of VAT returns submitted and VAT payments made;

- Information on capital assets being transferred to enable the Transferee to comply with the requirements of the capital assets scheme; and
- All information necessary for the buyer to comply with his duties under the VAT legislation.

4.7. De-registration following a TOGC

Following the transfer of a business, a Transferor may be obliged to de-register for VAT. See the “Mandatory de-registration” Section of the VAT General Guide for the circumstances when deregistration is required. A Transferor should consider the mandatory de-registration rules on transferring a business as there is a 30 day time limit to de-register where the rules apply.

5. Input VAT incurred in relation to a Qualifying TOGC

5.1.1. Introduction

Where a sale or transfer of assets is a Qualifying TOGC, the transfer is outside the scope of VAT. However, this does not mean that input VAT on costs relating to the Qualifying TOGC cannot be recovered by the seller and / or purchaser. The principles for deducting input VAT on costs relating to a Qualifying TOGC are discussed below. See also the “Input VAT recovery” section of the VAT General Guide for guidance on the principles relating to input VAT deduction.

5.1.2. Input VAT incurred by a Transferor

Generally, costs incurred by a Transferor in relation to a Qualifying TOGC (e.g. consultancy fees, legal fees) are considered to be a general overhead of the Transferor’s business. This has the following implications:

- Where the Transferor’s business is fully VATable (i.e. all supplies are subject to VAT at either the 5% or 0% rates, or would be if made in Bahrain), input VAT is recoverable in full on costs relating to the Qualifying TOGC.
- Where the Transferor’s business only makes exempt supplies, no input VAT is recoverable on costs relating to the Qualifying TOGC.
- Where the Transferor’s business makes VATable and exempt supplies, input VAT is partially recoverable in line with the Transferor’s apportionment method. See the “Apportionment of input VAT on residual expenses” Section of the VAT General Guide for more information.

Where, however, only part of the business of the Transferor is transferred, input VAT on expenses relating to the TOGC will be treated as a general overhead of the part of the business transferred and the rules above relating to the availability of input VAT will apply in relation to that part of the business.

Example

ActiveCo, a Bahraini company that is registered for VAT, sells sportswear. It also has a portfolio of rental properties. It considers selling all or part of its business to AcquireCo, another Bahraini company. It may wish to sell all of its business (sportswear and rental property portfolio), the sportswear business only or the rental property portfolio only. Assume that, in all the cases discussed below, the relevant transfer meets the conditions to be Qualifying TOGC.

a) *ActiveCo sells all business activities to AcquireCo*

Costs (such as legal and financial advice) relating to the sale to AcquireCo will be a general overhead of ActiveCo's business which comprises both VATable and exempt supplies. Hence, ActiveCo may claim back a proportion of the input VAT on these costs, based on the apportionment method used by it. Assuming ActiveCo used the standard apportionment method and its VATable sales comprise 40% of total supplies, it will be entitled to recover 40% of the input VAT on costs.

b) *ActiveCo sells its sportswear business only*

Costs relating to the sale to AcquireCo will be a general overhead of ActiveCo's business. However, as only the VATable business is being transferred, the general overhead will be regarded as relating to that VATable business only. Hence, ActiveCo may claim back all of the input VAT on costs incurred during the sale.

c) *ActiveCo sells its property rental portfolio only*

Costs relating to the sale to AcquireCo will be a general overhead of ActiveCo's business. However, as only the exempt business is being transferred, the general overhead will be regarded as relating to that exempt business only. Hence, ActiveCo may not claim back any of the input VAT on costs incurred during the sale.

Note: It is assumed that, in the above examples, there are no restrictions on the right to deduct input VAT on the costs incurred (e.g. input VAT disallowed by law).

5.1.3. Input VAT incurred by a Transferee

Costs incurred by a Transferee as part of a Qualifying TOGC will be regarded as a general overhead of the business. The associated input VAT incurred will be:

- Fully recoverable: where the acquired assets are used exclusively to make VATable supplies;
- Non-recoverable: where the acquired assets are used exclusively for exempt supplies; and
- Partially recoverable: where the acquired assets are used to make both VATable and exempt supplies, (in line with the purchaser's partial exemption input VAT recovery method).

Example

In the example at 5.1.2, the following will be the input VAT recovery position for AcquireCo on costs incurred by it in purchasing all or part of the business of ActiveCo:

In scenario a), AcquireCo will be entitled to partial recovery of input VAT incurred as the assets purchased will be used to make both VATable and exempt supplies. The amount recoverable depends on the recovery method to be used by the company.

In scenario b), AcquireCo should be entitled to full recovery of input VAT incurred as all of the assets purchased will be used to make VATable supplies.

In scenario c), AcquireCo will not be entitled to any recovery of input VAT as all of the assets purchased will be used to make exempt supplies.

5.1.4. Input VAT incorrectly charged by a Transferor

Where a transfer of business assets is a Qualifying TOGC, but the Transferor incorrectly charges VAT on the transfer, the Transferee is not entitled to recover this VAT as input VAT. This is because the transfer is deemed not to be a supply for VAT purposes. In such cases, the Transferee should request a refund of the VAT charged from the Transferor.

6. Application of TOGC rules for VAT groups

6.1. Transfer of business assets within a VAT group

A VAT group is considered to be a single VATable person for VAT purposes. All supplies between members of the VAT group are deemed to be made to and by the representative of the VAT group. Therefore, transactions between members of a VAT group, including those that may otherwise fall within the TOGC Provisions, will be outside the scope of VAT. The TOGC Provisions will not apply to any transfers of assets or businesses within a VAT group.

6.2. Transfer of business assets out of a VAT group

The transfer of business assets from a VAT group to a person outside of the VAT group will be a Qualifying TOGC if it meets the conditions set out in Section 3 of this Guide. It is not necessary that the assets transferred come from one member of the VAT group. Assets can be transferred from different VAT group members provided that all of the assets transferred together comprise a going concern at the time of transfer and that this going concern is capable of being operated on an independent basis.

6.3. Transfer of business assets to a VAT group

The transfer of assets to a VAT group may be a Qualifying TOGC if the following conditions are met:

- The rules detailed in Section 3 of this Guide are met, and
- The member of the VAT group acquiring the assets uses them:
 - to make supplies to persons outside the VAT group; or
 - to make supplies to other VAT group members, who, in turn, make supplies to persons outside the VAT group.

As a VAT group is considered to be a single VATable person for VAT purposes, it is important that the assets transferred to a VAT group are used to make supplies outside the VAT group and are not merely consumed within the VAT group.

If, following an initial transfer of assets to a VAT group, the assets are transferred within the VAT group (to one or more members), the transfer can still be a Qualifying TOGC provided that the assets are ultimately used to make supplies outside of the VAT group.

Example 1

PG Hotels Group comprises a number of Bahraini entities engaged in the hotel business. All entities are owned by the same shareholder and they have registered as a VAT group.

One of the entities purchases a hotel from another VAT registered entity owned by a third party. This hotel comprises the entire business operations of the selling party.

The hotel will be rebranded as a PG Hotel and will continue to operate as a hotel open to the public. After three months, the hotel is sold to another entity in the PG Hotel VAT group, but its business remains unchanged.

The sale of the hotel to the PG Hotel group will be a Qualifying TOGC. The onward sale of the hotel to another member of the group will not impact this as the hotel will remain in the ownership of the same person from a VAT perspective.

Example 2

If, in Example 1, following the acquisition of the hotel from the third party and its transfer to the other group member, it is shut to the public and used for employee accommodation, as the hotel will not be used to make supplies to persons outside the VAT group, the acquisition from the third party will not be a Qualifying TOGC.

6.4. Transfer of business assets to a partially exempt VAT group

The transfer of assets into a partially exempt VAT group (i.e. a VAT group in which one or more members makes exempt supplies) can also be a Qualifying TOGC subject to the normal rules set out above.

7. The treatment of capital assets under a TOGC

Capital assets are tangible or intangible assets which constitute part of the assets of the business and which are assigned for long term use as a business instrument or as a means of investment.

Ordinarily, where a VATable person acquires capital assets, he can recover the input VAT incurred on their purchase in line with the normal input VAT recovery rules. However, the VATable person must monitor the use to which the assets are put over their VAT life. If the use of the capital assets changes during the adjustment period (e.g., the goods were purchased to make VATable supplies, but subsequently are used to make exempt supplies), the input VAT originally claimed must be adjusted. The VAT life of capital assets is:

1. Five years for intangible assets and moveable tangible assets
2. Ten years for immovable tangible assets

Where capital assets are transferred as part of the business assets under a Qualifying TOGC, these will continue to be subject to the capital asset rules (i.e. annual monitoring of use and input VAT adjustment if required) based on the remaining life of the capital asset.

The transferor's current adjustment year will end on the day preceding the date of the Qualifying TOGC and the transferor should make the necessary adjustment for that year in the VAT period during which the Qualifying TOGC is made.

The subsequent adjustment year shall start on the day of the transfer and the adjustment for this year shall be made by the transferee at the end of the twelve month period starting on the date of the Qualifying TOGC. The adjustment procedure shall continue for the remaining years in the adjustment period in the same manner.

Further information regarding the operation of the capital asset scheme can be found in the "Change in use - Capital assets scheme" Section of the VAT General Guide.

Example

Little Developments purchases a new machine for its business operations on 1 June 2019 for BHD 1,000,000, including VAT. As the new machine is a movable tangible asset, Little Developments is required to monitor the use of the asset over the following five years.

Little Developments sells its entire business assets (including the machine) to Big Developments on 1 December 2022. The transaction is a Qualifying TOGC.

Little Developments' capital asset assessments periods are:

1 June 2019 - 31 May 2020 (Year 1)

1 June 2020 - 31 May 2021 (Year 2)

1 June 2021 - 31 May 2022 (Year 3)

1 June 2022 - 30 November 2022 (Year 4)

Big Developments capital asset assessments periods will be:

1 December 2022 - 30 November 2023 (Year 5)

