

EXPLANATORY MEMORANDUM TO
THE VALUE ADDED TAX (INPUT TAX) (SPECIFIED SUPPLIES) (AMENDMENT)
ORDER 2018

2018 No. [XXXX]

1. Introduction

- 1.1 This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs on behalf of Her Majesty's Treasury and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

- 2.1 This Order amends article 3 of the Value Added Tax (Input Tax) (Specified Supplies) Order 1999 ('SSO') to restrict its application in certain circumstances in order to prevent avoidance. The SSO allows companies who export certain financial services from the European Union ('EU') to reclaim the VAT they incur while providing those services; when these services are supplied inside the EU, this VAT cannot be reclaimed.
- 2.2 The SSO is currently being exploited by companies that form arrangements with organisations outside of the EU to re-supply or 'loop' those services back to United Kingdom ('UK') consumers, allowing themselves to reclaim the VAT and thereby gaining a competitive advantage over purely UK based companies. This Order seeks to prevent this 'looping' by restricting the application of the SSO to cases where the final consumer is not in the UK, as was intended.

3. Matters of special interest to Parliament

Matters of special interest to the Select Committee on Statutory Instruments

- 3.1 None

Matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business (English Votes for English Laws)

- 3.2 As the instrument is subject to negative resolution procedure there are no matters relevant to Standing Orders Nos. 83P and 83T of the Standing Orders of the House of Commons relating to Public Business at this stage.

4. Extent and Territorial Application

- 4.1 This instrument applies to the whole of the UK.

5. European Convention on Human Rights

- 5.1 As the instrument is subject to negative resolution procedure and does not amend primary legislation, no statement is required.

6. Legislative Context

- 6.1 Article 3 of the SSO currently allows organisations, or intermediaries, involved in the export of certain financial services from the EU to reclaim the VAT incurred in making the supplies of these services.
- 6.2 This Order amends article 3 of the SSO to restrict its application in circumstances where the final consumer of the services belongs in the UK, in order to prevent avoidance.

7. Policy background

What is being done and why?

- 7.1 This Order will amend legislation to close down a VAT avoidance scheme which relies on VAT rules which allow recovery on exempt financial services supplied to recipients outside the EU.
- 7.2 Providers of financial services generally cannot reclaim the VAT they incur on their costs because their services are VAT exempt. An offshore loop is a cross-border structure that enables these VAT costs to be recovered by routing services primarily carried out in the UK via a body located outside the EU. Those services are then used to provide insurance (and other financial services) back into the UK market. This is contrary to the intention of the VAT system, and distorts competition to the disadvantage of domestic UK suppliers.
- 7.3 This measure addresses a particular version of off-shore looping which is currently found almost exclusively in the insurance sector and involves looping intermediary supplies via an overseas territory. The 'offshore looping' structure that this Order is intended to prevent was the subject of a First Tier Tribunal decision in a case concerning Hastings Insurance Services in favour of the taxpayer. Following this HMRC loss, other insurers have made it clear that, if this distortion is not addressed, they will have to adopt similar structures to compete. MPs have also criticised this avoidance and called for Government action.
- 7.4 As a consequence, this Order amends UK legislation to ensure that input tax recovery is limited to cases where the final consumers of the principal financial services supplies belong outside the UK, as intended

8. European Union (Withdrawal) Act/Withdrawal of the United Kingdom from the European Union

- 8.1 This instrument does not relate to withdrawal from the European Union / trigger the statement requirements under the European Union (Withdrawal) Act.

9. Consolidation

- 9.1 N/A

10. Consultation outcome

- 10.1 This draft Explanatory Memorandum is being published alongside a draft Statutory Instrument to consult on whether it has the intended effect.

11. Guidance

11.1 N/A

12. Impact

12.1 There is no, or no significant, impact on business, charities or voluntary bodies.

12.2 There is no, or no significant, impact on the public sector.

12.3 An Impact Assessment has not yet been prepared for this instrument. A Tax Information and Impact Note will be produced when further information is provided at budget.

13. Regulating small business

13.1 The legislation does not apply to activities that are undertaken by small businesses.

14. Monitoring & review

14.1 We will keep under review the impact of the SI and its success in countering the avoidance outlined. The Government is also examining further legislative options for closing other versions of avoidance schemes involving such arrangements.

14.2 The regulation does not include a statutory review clause.