

EXPLANATORY MEMORANDUM TO

THE VALUE ADDED TAX (FINANCE) (EU EXIT) ORDER 2019

2019 No. 43

1. Introduction

- 1.1 This explanatory memorandum has been prepared by Her Majesty's Revenue & Customs ("HMRC") and is laid before the House of Commons by Command of Her Majesty.

2. Purpose of the instrument

- 2.1 This instrument amends legislation to (1) extend the existing Value Added Tax ("VAT") exemption for the management of investment funds to the management of pension funds that satisfy certain conditions and (2) remove the current restriction on the type of assets that a close-ended collective investment undertaking can invest in for its management to qualify for exemption.

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 the 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 The territorial extent of this instrument is the whole of the United Kingdom.
4.2 The territorial application of this instrument is the whole of the United Kingdom.

5. European Convention on Human Rights

- 5.1 The Financial Secretary to the Treasury Mel Stride MP has made the following statement regarding Human Rights:

"In my view the provisions of the Value Added Tax (Finance) (EU Exit) Order 2019 are compatible with the Convention rights."

6. Legislative Context

- 6.1 Under European Union ("EU") law, the management of what is termed a special investment fund ("SIF") is VAT exempt. The investment funds which are SIFs for UK VAT purposes are listed in items 9 and 10 of Group 5 of Schedule 9 to the Value Added Tax Act 1994 ("VATA") and some of the terms used are defined in Note (6) to Group 5 of Schedule 9 VATA ("Group 5"). Pension funds are not currently included in Group 5.

- 6.2 This instrument inserts a new paragraph (k) into item 9 of Group 5 to provide for exemption for the management of what is termed a ‘recognised pension fund’ and further inserts a definition of this term and some of its constituent parts into the Notes to Group 5 (Note (6) and new Note (6A)).
- 6.3 This instrument also amends Note (6) to Group 5 to remove the requirement for certain funds to invest wholly or mainly in securities for the fund management exemption to apply.

7. Policy background

What is being done and why?

- 7.1 A number of Court of Justice of the European Union cases have determined that the current UK exemption for the management of SIFs is not as wide as is required under EU law. In the absence of changes to the scope of the UK exemption, HMRC policy has been to allow businesses to choose whether to exempt their fund management services by relying on the direct effect of EU law or to continue to tax them under UK VAT legislation. This includes fund management services to certain types of pension funds and state regulated property funds.
- 7.2 HMRC’s intention has always been that this would be a temporary solution, subject to a full scale review of the fund management exemption and a subsequent redrafting of the UK VAT provisions.
- 7.3 Given that the UK will be exiting the EU on 29 March 2019 and direct effect of EU law may not apply to such supplies in the UK after it exits the EU, the Government has decided to amend UK law with effect from that date to provide for exemption for the management of pension funds (as defined). This will provide certainty for businesses and ensure that the majority of businesses who currently exempt their supplies of fund management services can continue to do so after the UK leaves the EU.

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

- 8.1 This instrument relates to the withdrawal of the UK from the EU but is being made under existing powers in VATA as it implements HMRC policy to ensure that UK law fully reflects EU law in the area of financial exemptions. The amendments to UK law would have been made regardless of the withdrawal of the UK from the EU due to the need for legal certainty.

9. Consolidation

- 9.1 This instrument makes amendments to Group 5 and there are no plans to consolidate the legislation at this time.

10. Consultation outcome

- 10.1 The changes effected by this instrument were subject to an informal consultation with trade bodies and their representatives. The consultation confirmed that the vast majority of industry members prefer exemption and have been relying on the direct effect of EU law to exempt their fund management services.

- 10.2 With regard to the small number who currently tax their supplies and will now have to exempt them, the view of the industry representatives was that any impact on them would be minimal as any costs they would incur as a result of this change should be mitigated by no longer having to include VAT in their charges.

11. Guidance

The changes made by this instrument will be reflected in published HMRC guidance on the VAT liability of financial services. Guidance will be updated before 29th March 2019.

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 This instrument will be covered by an overarching HMRC impact assessment on VAT and services which will be published and available on the website at <https://www.gov.uk/government/collections/customs-vat-and-excise-regulations-leaving-the-eu-with-no-deal>

13. Regulating small business

- 13.1 The legislation applies to activities that are undertaken by small businesses.
- 13.2 No specific action is proposed to minimise regulatory burdens on small businesses employing less than 50 people as the rules are by necessity of general application within the sector.
- 13.3 However, it is not anticipated that many small businesses within the definition engage in the type of activity covered by this instrument.

14. Monitoring & review

- 14.1 This instrument will be kept under review through communications with key stakeholder groups, including the Joint VAT Consultative Committee (made up of a wide range of representatives), to ensure that it meets the policy objectives set out in section 7 above.
- 14.2 The instrument does not include a statutory review clause because it relates to tax and therefore meets the requirements of the exemption set out in section 28(3)(a) of the Small Business, Enterprise and Employment Act 2015.

15. Contact

- 15.1 Kerrie Croke at HM Revenue & Customs Telephone: 03000 585738 or email: Kerrie.croke@hmrc.gsi.gov.uk can be contacted with any queries regarding the instrument.
- 15.2 Eileen Patching, Deputy Director VAT Principles and Risk, Customs & Indirect Tax Directorate, at HMRC can confirm that this Explanatory Memorandum meets the required standard.
- 15.3 Mel Stride MP, Financial Secretary to the Treasury, can confirm that this Explanatory Memorandum meets the required standard.