# EXPLANATORY MEMORANDUM TO

# THE VALUE ADDED TAX (AMENDMENT) (No. 2) REGULATIONS 2014

# 2014 No. 1497

1. This explanatory memorandum has been prepared by Her Majesty's Revenue and 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 Parts 4A (reverse charge sales statements) and 5 (accounting, payment and records) of the Value Added Tax Regulations 1995 (S.I. 1995/2518) ("the Principal Regulations").

*Regulation 3*

2.2 The amendments to Part 4A ensure (by amending the definition of "relevant supply" in regulation 23A) that persons who make supplies of gas and electricity to which the Value Added Tax (Section 55A) (Specified Goods and Excepted Supplies) Order 2014 (S.I. 2014/1458) ("the Order") applies are not required to make reverse charge sales statements.

*Regulation 4*

2.3 The amendments to Part 5 provide for an additional category of excepted persons who will be authorised to use the paper return system and allow the Commissioners to approve a new form of electronic filing system (telephone filing) for use by authorised categories of taxpayers.

3. **Matters of special interest to the Select Committee on Statutory Instruments**

None.

4. **Legislative Context**

4.1 This instrument amends the Principal Regulations.

*Regulation 3*

4.2 Council Directive 2006/112/EC ("the Principal VAT Directive") establishes a common system of value added tax applicable throughout the European Union. As a general rule, the Principal VAT Directive requires the person who makes supplies of goods or services to account for and pay the VAT on those supplies. However, in certain circumstances, the VAT may be required to be accounted for and paid by the recipient of those supplies. This charge is referred to as a "reverse charge".

4.3 The Principal VAT Directive was amended by Council Directive 2010/23/EU which inserted Article 199a. Article 199a permits Member States to apply a reverse charge in certain circumstances. Article 199a was itself amended by Council Directive 2013/43/EU which extends the circumstances in which Member States may apply a reverse charge to combat missing trader intra-Community fraud. In particular, it permits Member States to apply a reverse charge until 31 December 2018 and for a minimum period of two years to supplies of gas and electricity to a taxable dealer as defined in Article 38(2) of the Principal VAT Directive.

4.4 Section 55A(6) of the VAT Act 1994 ("the Act") provides that, if a taxable person makes a supply of goods or services to which section 55A applies and which is not an excepted supply and the recipient of that supply is a taxable person and supplied in connection with the carrying on by him of any business, then it is for the recipient on the supplier's behalf to account for and pay tax on the supply.

4.5 Section 55A(9) and (10) confer power on HM Treasury to make an Order specifying the goods or services to which section 55A applies and the description of supplies which are to be "excepted supplies" for the purposes of section 55A.

4.6 Those powers have been exercised to make the Order, which has been made and laid at the same time as this instrument.

4.7 Part 4A of the Principal Regulations imposes obligations on those who make supplies to which section 55A of the Act applies. However, for reasons set out under the "Policy background" heading below, HMRC has decided not to impose such obligations on those who make supplies to which the Order applies.

## 5. Territorial Extent and Application

This instrument applies to the whole of the United Kingdom.

## 6. European Convention on Human Rights

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

## 7. Policy background

*What is being done and why*

*Regulation 3*

7.1 This is a consequential measure which will prevent suppliers of gas and electricity to which the Order applies from having to make reverse charge sales statements.

7.2 The sales statements provide HMRC with details of supplies made and to whom they were made so that HMRC can monitor those sales to establish that the recipient of the supply has accounted for the corresponding output tax due to HMRC.

Where the risk of that VAT going unpaid is significant, sales lists can be an important compliance tool in trying to ensure that losses are minimised or prevented. Where there are a large number of recipients of such supplies or where the recipients are small businesses with an inherently higher risk of business failure there is a more significant risk that the VAT will go unpaid.

7.3 As the Order will only affect a small number of businesses (estimated to be less than 1000) who are in the main large or very large in size and turnover and are participants in a closely regulated market, the very low risk of the VAT being lost under this reverse charge (combined with HMRC's compliance activities) is not considered to merit requiring additional reporting requirements in the form of sales lists.

*Regulation 4*

7.4 Following changes to the law with effect from 1 April 2012, virtually all VAT registered businesses are required to submit their VAT returns online using an electronic return system in a form approved by HMRC in a direction issued under the Principal Regulations. The only exceptions are businesses who object to using electronic communications on religious grounds and insolvent businesses. For those businesses who HMRC accept have difficulties in filing online using the approved electronic return system, HMRC currently offer a range of options to help them meet their legal obligations including a filing by telephone service ("telephone filing").

7.5 Following appeals against the requirement to file online, the First-tier Tribunal ("FTT") held that the failure of the Principal Regulations to take account of a person's ability to comply on account of age, disability, computer illiteracy (linked to age) or remoteness of location was a breach of the European Convention on Human Rights (ECHR). The FTT also held that telephone filing as currently operated did not remedy the breach as it had not been legislated for.

7.6 This regulation enables HMRC to make a direction to approve telephone filing as an alternative form of electronic return system that will be available for use by authorised businesses (businesses that satisfy HMRC that they meet certain criteria). Additionally, it provides that, where HMRC accepts that it is not reasonably practicable for a business to file its VAT returns using electronic communications (either using the current form of electronic return system approved by HMRC in the current direction or the new telephone filing form of electronic return system to be approved by HMRC in a new direction), that business will be authorised to file its returns on paper.

*Consolidation*

7.7 There are no projects presently on hand to consolidate the Principal Regulations.

## 8. Consultation outcome

*Regulation* 3

8.1 An informal consultation was conducted with the gas and electricity trading sector which was supportive of the introduction of a reverse charge to combat MTIC fraud without reporting requirements.

*Regulation 4*

8.2 HMRC initially consulted on these changes between 20 December 2013 and 14 February 2014. The purpose of the consultation was to explore potential amendments to VAT legislation to deal with the issues identified by the FTT. There were 30 responses which were carefully considered and summarised in a Summary of Responses document which is available on HM Government website at https://www.gov.uk/government/consultations/assistance-with-electronic-filing-of-vat-returns.

8.3 The Summary of Responses document incorporated a further technical consultation to establish whether proposed changes to VAT law would achieve the intended result. That further consultation period ended on 23 May and resulted in 5 responses from representative bodies. HMRC has considered those responses and will be publishing a further Summary of Responses document on HM Government website.

## 9. Guidance

*Regulation 3*

9.1 HMRC has published guidance to coincide with the introduction of the reverse charge so that affected businesses have the information that they need to be able to make the necessary changes to their systems.

*Regulation 4*

9.2 HMRC will issue further publicity and guidance to provide affected businesses with more information about the impact of the changes. Web guidance and public notices will also be updated to ensure that the changes are accurately reflected.

## 10. Impact

*Regulation 3*

10.1 The impact on business, charities or voluntary bodies is negligible.

10.2 The impact on the public sector is negligible.

10.3 A Tax Information and Impact Note covering this instrument was published at Budget 2014 and is available on the HMRC website at HM Revenue & Customs: Tax Information and Impact Notes (TIINs). It remains an accurate summary of the impacts that apply to this instrument.

*Regulation 4*

10.4 A Tax Information and Impact Note covering this instrument will be published on the HMRC website at http://www.hmrc.gov.uk/thelibrary/tiins.htm.

## 11. Regulating small business

*Regulation 3*

11.1 The legislation applies to small business. The changes do not discriminate between businesses but few, if any, small businesses are affected. The impact on small and micro businesses is negligible.

*Regulation 4*

11.2 The legislation applies to all businesses. Any business that experiences difficulties in filing its VAT return online using an approved electronic return system can contact HMRC to discuss its circumstances. If satisfied that the business is unable to file online using the current approved electronic return system, HMRC may authorise that business to use the new telephone filing approved electronic return system. If satisfied that a business is unable to file online using either the current approved electronic return system or the new telephone filing approved electronic return system, HMRC will authorise that business to file on paper.

## 12. Monitoring & review

*Regulation 3*

12.1 It is a requirement of exercising the option to apply the reverse charge under Council Directive 2013/43/EU that an evaluation is provided to the Commission by 30th June 2017. HMRC will continue to monitor whether MTIC fraud may spread to other goods or services and what further measures may be appropriate

*Regulation 4*

12.2 The take-up of alternatives to the current authorised method of online filing will be monitored and evaluated using information collected by HMRC contact centres.

## 13. Contact

*Regulation 3*

13.1 Nick Chambers at HM Revenue & Customs email: nick.chambers@hmrc.gsi.gov.uk can answer any queries regarding regulation 3.

*Regulation 4*

13.2 John Bryning at HM Revenue and Customs email: john.bryning@hmrc.gsi.gov.uk can answer any queries regarding regulation 4.