

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

2018 No. 1328

1. Introduction

This explanatory memorandum has been prepared by Her Majesty's Revenue and Customs ('HMRC') 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 articles 2 and 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. In accordance with the European vires, the SSO allows businesses who export certain financial services to customers in countries outside the European Union ('EU') to reclaim the VAT they incur while providing those services. However, it does not allow companies to reclaim this VAT when these services are supplied within the EU.

2.2 The SSO is currently being exploited by some insurance companies who have entered into 'looping' arrangements whereby insurance intermediaries based in the United Kingdom ('UK') supply their services to insurance companies based outside the EU who then use those services to make supplies of insurance services back to customers in the UK. This allows these UK based companies to reclaim the VAT incurred on making supplies of insurance even though the ultimate customers (the insured parties) are based in the UK and thereby gain a competitive advantage over other UK based companies. This Order seeks to prevent this form of 'looping' by ensuring that there is no recovery of input tax where the final customer of the insurance services is based 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 The territorial extent of this instrument is the UK.

4.2 The territorial application of this instrument is 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 businesses involved in the export of certain financial services from the EU to reclaim the VAT incurred in making the supplies of those services.
- 6.2 This Order amends articles 2 and 3 of the SSO to restrict its application in circumstances where the final consumer of insurance services belongs in the UK, in order to prevent avoidance.

7. Policy background

What is being done and why?

- 7.1 This Order amends the SSO to close down a VAT avoidance scheme which relies on VAT rules which allow recovery of input tax incurred on exempt financial services supplied to recipients outside the EU.
- 7.2 Providers of insurance (and other 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 compliant 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 insurance 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 which ruled 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 there is no VAT recovery where the final customers of the insurance services belong inside 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 the withdrawal of the UK from the EU/ trigger the statement requirements under the European Union (Withdrawal) Act 2018.

9. Consolidation

- 9.1 The changes will be reflected in the revised published version of the SSO.

10. Consultation outcome

- 10.1 A draft Explanatory Memorandum was published alongside a draft Statutory Instrument to consult on whether it had the intended effect. In response to comments received from industry representatives, the measure has been further refined to target it more tightly on the known avoidance.

11. Guidance

- 11.1 The changes will be reflected in general HMRC guidance.

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 A Tax Information and Impact Note has been prepared for this instrument.

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 Order does not include a statutory review clause.

15. Contact

- 15.1 Barbara Farndell at HMRC Telephone: 03000 585917 or email: barbara.farndell@hmrc.gsi.gov.uk can be contacted with any queries regarding the instrument.
15.2 David Fairbrother at HMRC can confirm that this Explanatory Memorandum meets the required standard.
15.3 The Financial Secretary to the Treasury Mel Stride MP at HM Treasury can confirm that this Explanatory Memorandum meets the required standard.