

PARLIAMENTARY DEBATES

HOUSE OF COMMONS
OFFICIAL REPORT

Third Delegated Legislation Committee

VALUE ADDED TAX (PLACE OF SUPPLY OF
SERVICES: EXCEPTIONS RELATING TO SUPPLIES
MADE TO RELEVANT BUSINESS PERSON) ORDER
2016 (S.I. 2016, NO. 726)

Monday 12 September 2016

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The Committee consisted of the following Members:

Chair: MIKE GAPES

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| † Allen, Heidi (<i>South Cambridgeshire</i>) (Con) | McCarthy, Kerry (<i>Bristol East</i>) (Lab) |
| † Barclay, Stephen (<i>Lord Commissioner of Her Majesty's Treasury</i>) | † McGinn, Conor (<i>St Helens North</i>) (Lab) |
| † Benn, Hilary (<i>Leeds Central</i>) (Lab) | † Mann, Scott (<i>North Cornwall</i>) (Con) |
| † Caulfield, Maria (<i>Lewes</i>) (Con) | † Offord, Dr Matthew (<i>Hendon</i>) (Con) |
| † Costa, Alberto (<i>South Leicestershire</i>) (Con) | † Paterson, Steven (<i>Stirling</i>) (SNP) |
| † Ellison, Jane (<i>Financial Secretary to the Treasury</i>) | Powell, Lucy (<i>Manchester Central</i>) (Lab/Co-op) |
| † Fysh, Marcus (<i>Yeovil</i>) (Con) | † Scully, Paul (<i>Sutton and Cheam</i>) (Con) |
| † Glen, John (<i>Salisbury</i>) (Con) | Fergus Reid, <i>Committee Clerk</i> |
| † Green, Kate (<i>Stretford and Urmston</i>) (Lab) | † attended the Committee |
| † Long Bailey, Rebecca (<i>Salford and Eccles</i>) (Lab) | |

Third Delegated Legislation Committee

Monday 12 September 2016

[MIKE GAPES *in the Chair*]

Value Added Tax (Place of Supply of Services: Exceptions Relating to Supplies Made to Relevant Business Person) Order 2016 (S.I. 2016, No. 726)

4.30 pm

The Financial Secretary to the Treasury (Jane Ellison): I beg to move,

That the Committee has considered the Value Added Tax (Place of Supply of Services: Exceptions Relating to Supplies Made to Relevant Business Person) Order 2016 (S.I. 2016, No. 726).

It is a pleasure, Mr Gapes, to serve under your chairmanship. The order introduces a change to the VAT place of supply rules for insurance repair services. Insurers who have structured their arrangements to receive such services free of UK VAT will be charged the tax from 1 October 2016. As is often the case with tax, this measure is somewhat technical. Supplies of insurance are exempt from VAT, which means that insurers do not charge VAT, but cannot reclaim the VAT that they pay on their costs. This measure is about the VAT that they are charged on repair services and aims to counter attempts by insurers to avoid incurring that VAT.

The VAT system includes place of supply rules that determine which country can collect the tax on any given supply. Under the normal VAT place of supply rules, repair services supplied from a repairer to an insurer are treated as supplied where that insurer is established. However, a small number of insurers have structured their arrangements to exploit the rule and avoid incurring VAT on costs that they are unable to reclaim. They do so by routing repair services to an associate offshore insurance firm located in a jurisdiction where no VAT applies, resulting, for example, in no VAT being charged on insured vehicle repairs carried out here in the UK. Such practices deplete public revenues and give avoiders a competitive advantage over those supplying similar insurance products.

We received complaints from UK insurers that such practices challenge fair competition and could force them to set up similar avoidance arrangements. In the summer Budget 2015, we promised to introduce a use and enjoyment provision in UK VAT law to address the issue. Following informal discussions with industry representatives, the Government consulted on a draft order in February 2016.

The order amends the place of supply to where the repair service is used and enjoyed, meaning that repairs carried out on goods used in the UK for UK policyholders will be subject to UK VAT, irrespective of where the insurance provider is based. The changes made by this order will end the tax avoidance by the few. It will yield approximately £5 million per annum from 2016-17 and

deter others from implementing similar arrangements, protecting significant revenue. The administrative cost of the change to UK repairers will be minimal, as they already charge VAT in the normal course of events to their UK customers.

In conclusion, the measure demonstrates that the Government will not tolerate tax avoidance. We will take strong action to make sure that we have a level playing field where everyone pays their fair share. This statutory instrument will, in particular, help to ensure that UK insurance businesses can operate on an equal footing with their overseas counterparts, that services are subject to VAT where they are consumed and that we remove an incentive to locate offshore to avoid tax. I therefore commend the order to the Committee.

4.33 pm

Rebecca Long Bailey (Salford and Eccles) (Lab): It is a pleasure to serve under your chairmanship, Mr Gapes. You will be pleased to hear that I will not detain the Committee for long.

The order seeks to prevent avoidance of VAT by some insurance companies, as the Minister outlined. Such avoidance is broadly achieved by the insurance company locating outside EU VAT jurisdictions, so that any repair services can be provided to them VAT-free, as the present legislation provides that the place of supply is where the recipient is based. The provisions of the order seek to close that loophole and, as such, the Opposition support the Government in this legislation.

As the explanatory memorandum sets out, the order “will require the service provider to charge VAT at the standard rate on the repairs they perform where the provider of the insurance cover for the goods is located outside the VAT territory of the EU”,

but where the supply of services would otherwise be treated as made in the United Kingdom and the services are effectively used and enjoyed outside the territories of the member states. The practical effect is that all UK repairs made under UK insurance contracts will be subject to VAT in the UK.

Generally speaking, the EU VAT system is designed to ensure that the tax is collected in the country where final consumption takes place. That is to ensure that UK VAT arises on consumption in the UK of goods and services. It also ensures that UK VAT is not charged in addition to other foreign VAT and taxes on consumption outside the UK. As the Minister highlighted, it appears that some insurance companies have been exploiting the system to avoid VAT on the provision of repair services specifically. Insurance companies have been setting up offshore so that such services can be supplied to them VAT-free.

The order creates an exception to the current VAT rules based on a provision in the EU principal VAT directive that permits member states to regard the place of supply as being where the services are “effectively used and enjoyed”, thereby ensuring that when the repair is undertaken in the UK, the tax is due in the UK, as the service is effectively used and enjoyed there, regardless of the involvement of offshore entities.

The Chartered Institute of Taxation broadly agrees with the principle that the Government have put forward, but it has some technical concerns about the definitions used in the order. It is specifically concerned about the

lack of a clear definition or guidance on the interpretation of “use” and “enjoyment”, which could leave the legislation open to dispute, creating uncertainty for taxpayers and the authorities. As far as I am aware, the terms “use” and “enjoyment” are not defined in the EU principal VAT directive or in UK legislation. The Chartered Institute of Taxation informs me that it has raised the issue directly with HMRC and has suggested that ideally there should be a definition in the legislation and, at the very least, clear guidance on how the terms are to be interpreted.

The final HMRC guidance has not been published yet, but the Chartered Institute of Taxation has been privy to a draft, and it told me that the guidance still does not explain how the terms “use” and “enjoyment” are to be interpreted. Perhaps the Minister could use this opportunity to provide clarification as to whether the Government will define the terms “use” and “enjoyment” in legislation. We certainly would not want any lack of clarification to provide a further loophole for insurers to avoid VAT.

The order was announced in the summer 2015 Budget. According to the corresponding policy costings, I understand that it is expected to save the Exchequer £5 million a year, which is fantastic. However, although we support the order, the money is minor when compared with the Treasury’s estimates of a tax gap of around £35 billion. The latest available figures for the VAT gap was £13.5 billion for 2014-15. That is 10.8% of the estimated net VAT total theoretical liability.

The Chair: Order. I would be grateful if the hon. Lady did not deal with the wider question of VAT and the tax gap, and confined her remarks to the order that we are debating.

Rebecca Long Bailey: Thank you, Mr Gapes. I was just trying to extract a little bit more information from the Minister. You will appreciate that we rarely have opportunities to do that.

The Chair: Order. Please confine your remarks to the terms of the order.

Rebecca Long Bailey: I apologise. To conclude my remarks on the order, the Opposition support the provisions introduced by the order to address VAT avoidance by

insurance companies located offshore. However, I hope the Minister can address some of the points I have raised and, in particular, the concerns of the Chartered Institute of Taxation.

4.39 pm

Jane Ellison: I am sure, Mr Gapes, that there will be opportunities in future to debate the wider issues. I will confine my remarks to the statutory instrument.

On the point about the relatively modest amount of money that will be saved by closing the loophole, as I said, we estimate that it will be £5 million. However, in closing the loophole we expect that we will prevent a far wider problem, which would amount to a considerable sum. To clarify, this is essentially pre-emptive action.

Reaction to the measure has generally been positive. The industry appreciates that we are trying to level the playing field. We involved industry representatives in discussions before the exposure of the draft legislation and they had the opportunity to comment. I note what the hon. Lady says about the definitions of “use” and “enjoyment”. The Government consider that that refers to where a service is consumed, so for insurance repairs, if the goods are to be used in the UK under insurance for a UK risk, the service is consumed in the UK and should be subject to UK VAT.

The measure comes into force on 1 October, and the Government will issue guidance. I make an undertaking, in particular, that officials will check with the chartered institute. If it has any further concerns we are interested in knowing them and in seeing whether we are able to reach a position with which it is entirely satisfied. However, those who have been consulted in the industry certainly feel that the terms are helpfully defined and that the measure will level the playing field.

As I said, the order is about ensuring that we do not have a significant loss of revenue in future and, at the same time, do not put those parts of the industry that are not trying to exploit the loophole behind those that are, acting early to ensure that the industry remains competitive and that everyone is playing by the same rules.

Question put and agreed to.

4.41 pm

Committee rose.

