

**EXPLANATORY MEMORANDUM TO**  
**THE VALUE ADDED TAX (SECTION 55A) (SPECIFIED SERVICES AND**  
**EXCEPTED SUPPLIES) ORDER 2019**

**2019 No. 892**

**1. Introduction**

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

**2. Purpose of the instrument**

2.1 The Value Added Tax Act 1994 ("the Act"), as a general rule, requires the supplier of goods and services to account for value added tax ("VAT") on those supplies. Section 55A of the Act requires VAT to be paid by the recipient of supplies ("a reverse charge") instead of the supplier if the supplies are of a type specified for that purpose in a Treasury order. This instrument imposes a reverse charge, with effect from 1 October 2019, on standard and reduced rate supplies of construction services.

**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 United Kingdom.

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

**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 Section 55A of the Act (customers to account for tax on supplies) provides that where a person registered for VAT makes a supply of goods or services to which that section applies, then it is for the recipient (if they are also VAT registered), on the supplier's behalf, to account for and pay the VAT on the supply.

6.2 This instrument makes provision for construction services to be specified under section 55A of the Act and makes exceptions to restrict the effect of the reverse

charge to supplies made by construction businesses to other similar businesses but not to non-construction businesses who are referred to in the instrument as end users.

## **7. Policy background**

### *What is being done and why?*

- 7.1 This instrument, with effect from 1 October 2019, applies a reverse charge to certain supplies of construction services in order to remove the opportunity for missing trader fraud in the construction sector.
- 7.2 Missing trader fraud is an organised criminal attack on the VAT system. The fraud is perpetrated through transaction chains in certain business sectors with the loss occurring when the VAT charged by the supplier is not paid to HMRC but is retained by the supplier.
- 7.3 This type of fraud has been used by criminals to steal billions of pounds in VAT from governments throughout the European Union, both in relation to domestic supplies such as construction services, and also in connection with cross-border intra-community trading in goods such as mobile telephones, computer chips and emissions allowances. A reverse charge for mobile telephones and computer chips was introduced with effect from 1 June 2007 and one for emissions allowances was introduced with effect from 1 November 2010. Further reverse charge measures were introduced for gas and electricity with effect from 1 July 2014 and for electronic communications with effect from 1 February 2016.
- 7.4 Construction services have been targeted by criminals because supplies with a high labour content do not incur any significant VAT on their costs but are liable to VAT on sales. Therefore fraudsters can receive high net amounts of VAT from their customers and then go missing, keeping the VAT for themselves. This instrument makes the reverse charge apply to construction services which, for these purposes, have been defined consistently with the activities covered in the Construction Industry Scheme. This is a statutory scheme which is concerned with tackling the risk of direct tax fraud in the construction industry.
- 7.5 The risk of fraud in the construction industry is principally centred on the supply of construction services between construction businesses in the supply chain and this instrument, therefore, does not require end user businesses to apply the reverse charge when receiving construction services. There is also no reverse charge requirement in relation to building and construction materials that are supplied separately and independently of construction services.
- 7.6 Reverse charge accounting makes it impossible for fraudsters to perpetrate missing trader fraud because the customer rather than the supplier accounts for the VAT direct to HMRC.
- 7.7 The introduction of the reverse charge in this business sector will mean that businesses will need to adapt their systems and manage their cash flow differently. Due to the large number of small businesses potentially affected by a reverse charge for construction services the government has given a long lead-in time to help businesses adjust, having announced in Autumn 2017 the intention to introduce legislation which will come into force in Autumn 2019. In addition, in order to minimise the impact on the smallest businesses, provision has also been made in this instrument to modify the effect of the rule in section 55A(3) of the Act (reverse

charge supplies to be treated as supplies made by the recipient for the purposes of the VAT registration limits). For construction services, therefore, the aggregation rule in section 55A(3) will not apply.

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

8.1 This instrument does not relate to the withdrawal from the European Union.

## **9. Consolidation**

9.1 There is no current plan to consolidate the various Treasury orders that specify the goods and services to which section 55A applies.

## **10. Consultation outcome**

10.1 HMRC consulted on options, including a reverse charge, to counter the fraud on 20 March 2017<sup>i</sup> and a summary of responses was published on 1 December 2017<sup>ii</sup>. 54 written responses were received from a variety of businesses from small to large, tax representatives and housing and trade associations. HMRC also held meetings with an external stakeholder group formed of representatives from large construction businesses, utilities businesses, tax bodies and trade associations.

10.2 Although the majority of respondents raised reservations about a reverse charge because of the size and complexity of the construction sector, it was recognised that there were few, if any, other policy options to a reverse charge that would be as effective at preventing missing trader fraud.

10.3 The government has acknowledged concerns of stakeholders by providing for a long lead-in time to allow businesses to make the necessary changes.

10.4 HMRC also carried out a technical consultation on the draft instrument and its impacts in June and July 2018. There were 27 written responses from a similar range of respondents as the 2017 consultation and HMRC continued to meet with the external stakeholder group and held face to face meeting with a variety of housing associations.

10.5 As a result of this consultation the legislation now links the reverse charge with the obligation to report payments for supplies through the Construction Industry Scheme under regulation 4 of the Income Tax (Construction Industry Scheme) Regulations 2005. This addresses concerns raised by respondents about potential difficulties in identifying whether construction services supplied to non-construction businesses would have to be subjected to the reverse charge, particularly in cases where the recipients might only be occasional purchasers of construction services.

10.6 Under the Construction Industry Scheme customers deduct money from payments to suppliers and pass it to HMRC. The deductions count as advance payments towards the supplier's tax and National Insurance obligations.

10.7 Businesses reporting payments under the Construction Industry Scheme are likely to be building contractors or other businesses and public bodies making regular large purchases of construction services (over £1m per annum on average over a 3 year period). They can therefore be expected to be familiar with how the reverse charge operates and be able to tell their supplier whether or not they are an end user if appropriate. Suppliers of construction services will also be familiar with when the

Construction Industry Scheme applies and therefore be able easily to determine whether the reverse charge should apply to their supplies.

- 10.8 Respondents to the consultation also identified technical issues relating to the treatment of certain transactions that should, consistently with the overall policy of the instrument, be excepted from the reverse charge, for example supplies between landlords and tenants.

## **11. Guidance**

- 11.1 Initial guidance concerning the introduction of the construction services reverse charge was published on 7 November 2018 so that businesses affected have the information they need to be able to adapt their accounting systems<sup>iii</sup>. Further guidance will be added in the run-up to the introduction of the reverse charge.

## **12. Impact**

- 12.1 The impact on business, charities or voluntary bodies is potentially significant for those supplying construction services because it is estimated that up to 150,000 businesses could be required to use it on supplies they make or receive. Only businesses that receive supplies where payments are reported through the Construction Industry Scheme will have to apply the reverse charge. In cases where a non-construction business falls within the scope of the Construction Industry Scheme because of the high value of its purchases of construction services, it may nevertheless come within the “end user” exception.
- 12.2 The impact on the public sector is negligible because, although some public sector bodies are required to report certain payments under the Construction Industry Scheme, they are likely to qualify for the “end user” exception.
- 12.3 A Tax Information and Impact Note covering this instrument was published on 7 November 2018 and is available on the website at <https://www.gov.uk/government/publications/vat-reverse-charge-for-building-and-construction-services/vat-reverse-charge-for-building-and-construction-services>. It remains an accurate summary of the impacts that apply to this instrument.

## **13. Regulating small business**

- 13.1 The instrument applies to activities that are undertaken by small businesses.
- 13.2 To minimise the impact of the requirements on small business (employing up to 50 people), the approach taken in this instrument to coordinate the VAT reverse charge with the Construction Industry Scheme will make it straightforward for small businesses to know when the reverse charge applies.
- 13.3 The basis for the final decision on what action to take to assist small businesses was the consultation which also included businesses or agents representing businesses employing up to 50 people. Participants in the consultation were clear that a close alignment with the Construction Industry Scheme would be much simpler for all businesses to operate instead of excluding some businesses on the basis of their turnover, or the transaction size. More information on the impact on small businesses can be found in the Tax Information and Impact Note published on the website at <https://www.gov.uk/government/publications/vat-reverse-charge-for-building-and-construction-services/vat-reverse-charge-for-building-and-construction-services>.

## **14. Monitoring & review**

- 14.1 The approach to monitoring of this legislation is that HMRC will monitor the impact of the changes introduced by this instrument as regards the construction industry and the effectiveness of its anti-fraud measures. HMRC will also continue to monitor whether fraud may spread to other supplies in other business sectors and what further measures may be appropriate.
- 14.2 This instrument falls with the statutory review exceptions under section 28(3)(a) Small Business, Enterprise and Employment Act 2015 as it relates to tax.

## **15. Contact**

- 15.1 Nick Chambers at HM Revenue & Customs, tel. 03000 585662, email: [nick.chambers@hmrc.gsi.gov.uk](mailto:nick.chambers@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.
- 15.2 Alice Dowswell, Deputy Director for VAT Serious Non-Compliance & Fraud at HM Revenue & Customs 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.

---

<sup>i</sup> Fraud on provision of labour in construction sector: consultation on VAT and other policy options – Consultation document published 20 March 2017

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/601034/Fraud\\_on\\_provision\\_of\\_labour\\_in\\_construction\\_sector-consultation\\_on\\_VAT\\_and\\_other\\_policy\\_options.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/601034/Fraud_on_provision_of_labour_in_construction_sector-consultation_on_VAT_and_other_policy_options.pdf)

<sup>ii</sup> Fraud on provision of labour in construction sector: consultation on VAT and other policy options - Summary of responses published 1 December 2017

[https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/663934/Fraud-on-provision-labour-construction-sector\\_consultation-VAT-otherpolicy-options-responses.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/663934/Fraud-on-provision-labour-construction-sector_consultation-VAT-otherpolicy-options-responses.pdf)

<sup>iii</sup> VAT reverse charge for building and construction services guidance note published 7 November 2018  
<https://www.gov.uk/government/publications/vat-reverse-charge-for-building-and-construction-services-guidance-note/guidance-note>