HMRC - IPT04760 - Contracts Relating To The Provision Of Financial Facilities

The Finance Act 1994 Schedule 7A paragraph 15(1) and (2) exempts a contract:

(1) …. if it relates only to the provision of a relevant financial facility and the conditions mentioned in sub-paragraph (2) below are satisfied.

(2) The conditions referred to in sub-paragraph (1) above are that-

(a) the person to whom the relevant financial facility is provided is an overseas customer;

(b) it is provided in order that he may comply with a legally binding obligation to receive a relevant supply of goods, or a supply of services, or both, from a person carrying on business; and

(c) the contract of insurance insures against risks arising from or in relation to either or both-

(i) credit,

(ii) suretyship.

Class 14 of Schedule 1 part I of the RAO 2001, covers losses of creditors arising from the insolvency of their debtors or from some other failure of debtors to pay their debts when due. Class 15 covers losses by insureds having to pay out under contracts of guarantee, fidelity bonds, administration bonds, bail bonds or customs bonds or similar contracts of guarantee they have entered into. The exemption applies to insurance taken out by a UK finance house or bank to protect repayments on a financial facility it has provided to an overseas customer so that the customer can receive a relevant supply.

Definition of ‘relevant financial facility’

Paragraph 15(3) of Schedule 7A defines a “relevant financial facility” as:

(a) the making of an advance;

(b) the issue of a letter of credit or acceptance of a bill of exchange;

(c) the giving of a guarantee or bond; or

(d) any other similar transaction entered into in order to provide a customer with the means to pay, or a supplier with the right to call upon a third party for, the consideration for goods or services.

Definition of ‘relevant supply’ and ‘overseas customer’

The exemptions for contracts of insurance relating to credit, exchange losses and the provision of financial facilities each refer to “relevant supply” and “overseas customer”. Paragraph 16 of Schedule 7A defines these terms as follows:

Sub-paragraph 16(2) defines ‘relevant supply’ as:

… any supply of goods where the supply is to be made outside the United Kingdom or where the goods are to be exported from the United Kingdom.

Thus, intra UK supplies are not regarded as relevant supplies. Therefore, an insurance premium taken out by a UK bank to cover repayments on a loan made to a Scottish firm to enable it to buy goods from a company in London will not be exempt under Paragraph 15.

Paragraph 16(3) defines an ‘overseas customer’ as:

… a person who-

(a) does not have any business establishment in the United Kingdom but has such an establishment elsewhere;

(b) has such establishments both in the United Kingdom and elsewhere, provided that the establishment at which, or for the purposes of which, the goods or services which are to be supplied to him are most directly to be used is not in the United Kingdom; or

(c) has no such establishment in any place and does not have his usual place of residence in the United Kingdom.

The exemptions at Paragraphs 13 and 14 of Schedule 7A require the underlying supply of goods or services to be made by “a person carrying on business in the UK”. Even if the physical supply of the goods takes place outside the UK, e.g. they move from France to Germany, the underlying supply must be made by a person in business in the UK in order for exemption to apply.

The exemption at Paragraph 15 requires the relevant financial facility (a loan for example) covered by the insurance to be made to an overseas customer, but the supply of goods or services which the loan enables them to buy can be made by any supplier, not just a UK supplier. For example, insurance supplied to a UK bank to cover repayments on a loan it has made to a German customer, who uses the loan to buy goods in France from a French supplier, will be exempt under Paragraph 15, even though the risk (the bank) is in the UK, since:

the loan is a relevant financial facility;

the loan is provided to an overseas customer;

it is provided to enable them to receive a relevant supply (in this case, one made outside the UK).

If the exemption under Paragraph 15 only applied where the underlying supply was made by a UK business, IPT would be charged to UK banks in situations such as that involving the German customer described above. The IPT would probably be passed on to the client by the bank, which could make the UK bank’s service uncompetitive.

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