HMRC - VATSC10000 - Agreements With Finance Companies At Non-Standard Rates Of Interest

Certain traders, such as car dealers, have agreements with finance companies whereby the trader is allowed to offer a lower interest rate in agreements with their customers than that they would otherwise receive directly from the finance company. This is subject to a payment by the trader to the finance company based on the difference between original interest rate and the interest rate actually paid by the customer.

Liability of the payment

The payment by the trader to the finance company is regarded as part of the charge for credit incurred by the customer and is exempt under Group 5, item 2 of the VAT Act 1994. The same principle applies where personal loans or other advances are made to customers at a reduced rate of interest where the difference will be subsidised by the trader. In such cases, the consideration paid for the trader’s main supply must not be reduced by the interest charges paid by the trader.

Agreements at a higher rate of interest

A trader may negotiate with the customer to charge a rate of interest which is higher than the finance company’s standard rate. If the finance company refunds or allows the trader to retain the difference between the standard rate and rate paid by the customer, that sum represents an additional amount payable in respect of the supply of the trader’s services to the finance company. It is exempt under Group 5, item 3 of the VAT Act 1994.

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