**EXPLANATORY MEMORANDUM TO**

**THE ALTERNATIVE FINANCE (INCOME TAX, CAPITAL GAINS TAX AND CORPORATION TAX) ORDER 2022**

**2022 No. [XXXX]**

## 1. Introduction

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

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

## 2. Purpose of the instrument

2.1 This Order widens the scope of tax legislation applying to alternative finance arrangements. This will allow (i) Home Purchase Plan providers that are regulated by the Financial Conduct Authority (FCA) and (ii) certain alternative finance arrangements facilitated through FCA-regulated peer-to-peer platforms to access the rules.

## 3. Matters of special interest to Parliament

***Matters of special interest to the Select Committee on Statutory Instruments***

3.1 Arrangements entered into between the date of publication of the '*Autumn 2021 Tax Administration and Maintenance*' (CP 577) 30 November 2021 and the date the order comes into force will fall within the new rules, but only in relation to events occurring after the date the order comes into force.

## 4. Extent and Territorial Application

4.1 The territorial extent of this instrument is United Kingdom.

4.2 The territorial application of this instrument is United Kingdom.

## 5. European Convention on Human Rights

5.1 John Glen MP, the Economic Secretary to the Treasury has made the following statement regarding Human Rights:

"In my view the provisions of the Alternative Finance (Income Tax, Capital Gains Tax and Corporation Tax) Order 2022 are compatible with the Convention rights".

## 6. Legislative Context

6.1 This Order amends the alternative finance arrangements provisions contained in:

- Part 10A of the Income Tax Act 2007,
- Chapter 4, Part 4 of the Taxation of Chargeable Gains Act 1992, and
- Chapter 6, Part 6 of the Corporation Tax Act 2009.

6.2 Consequential amendments are also made to section 173A of the Income Tax (Earnings and Pensions) Act 2003.

6.3 This Order is made using the power provided by section 366 of the Taxation (International and Other Provisions) Act 2010.

6.4 The effect of this Order is to bring (i) FCA-regulated Home Purchase Plan providers and (ii) certain alternative finance arrangements facilitated through FCA-regulated peer-to-peer platforms into the scope of the alternative finance arrangement rules.

## 7. Policy background

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

7.1 Legislation applying to alternative finance arrangements provides rules on the tax treatment of Sharia-compliant financial arrangements. Such arrangements allow finance to be provided without the payment of interest. The effect of the legislation is that, where certain conditions are met, the return made by the provider of the finance is treated as if it were interest for tax purposes.

7.2 The current legislation imposes a number of conditions on arrangements for them to fall within scope of the provisions. One of these conditions is that, in most situations, at least one party to the arrangement must be a financial institution as defined in section 564B of the Income Tax Act 2007, or section 502 of the Corporation Tax Act 2009.

7.3 This means that, currently, Home Purchase Plans provided by firms that do not fall within this definition and alternative finance arrangements facilitated by peer-to-peer platforms are not within the scope of the alternative finance tax provisions.

7.4 For the purpose of the Stamp Duty Land Tax (SDLT) alternative property finance rules, changes were made in the Finance Act 2015 to include FCA-regulated Home Purchase Plan providers in the definition of a financial institution. They are also included in the definition of a financial institution for the purposes of the Land Transaction Tax alternative property finance rules.

7.5 This Order amends the alternative finance arrangements legislation to provide a similar level playing field for Income Tax, Capital Gains Tax and Corporation Tax purposes.

7.6 In particular:

- Home Purchase Plans provided by FCA-regulated providers that are not financial institutions will be able to come within the scope of provisions for alternative finance arrangements and receive the same tax treatment as similar products provided by financial institutions.
- Certain alternative finance arrangements facilitated by an FCA-regulated peer-to-peer platform will be able to come within the scope of provisions for alternative finance arrangements and receive equivalent tax treatment to conventional peer-to-peer lending facilitated by a regulated platform. This treatment can apply to purchase and resale arrangements and diminishing shared ownership arrangements.

## 8. European Union Withdrawal and Future Relationship

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

## 9. Consolidation

9.1 There are no plans to consolidate this instrument.

## 10. Consultation outcome

10.1 HMRC conducted a technical consultation on the draft order from 11 February 2022 to 11 March 2022. Seven written responses were received. There was general support for the changes.

10.2 Several respondents suggested providing an SDLT exemption for alternative property finance arrangements entered into by other regulated entities that do not fall within the current definition of financial institution.

10.3 Several respondents suggested enabling alternative finance arrangements to be held in Innovative Finance Individual Savings Accounts (ISAs).

10.4 It is not considered feasible to implement these changes as part of this Order. Separate consideration will be made as to whether these points should be addressed. As a result, no adjustment to the draft Order has been made as a result of the consultation.

## 11. Guidance

11.1 HMRC's Corporate Finance Manual contains pages explaining the alternative finance arrangements provisions.

11.2 They will be updated after this Order comes into force.

## 12. Impact

12.1 The impact on business is that this Order will allow regulated Home Purchase Plan products and certain alternative finance arrangements facilitated by regulated peer-to-peer platforms to be treated in the same way as conventional mortgages and loans for tax purposes. This will contribute towards providing a level playing field for alternative finance arrangements and conventional finance products. It is anticipated that those prevented from using conventional financing products due to their religion or beliefs will have more options to obtain finance as a result of this change.

12.2 There is no, or no significant, impact on charities or voluntary bodies.

12.3 There is no, or no significant, impact on the public sector.

12.4 A Tax Information and Impact Note covering this Order will be published on the government website at https://www.gov.uk/government/collections/tax-information-and-impact-notes-tiins.

## 13. Regulating small business

13.1 This Order applies to activities that are undertaken by small businesses.

13.2 To minimise the impact of the requirements on small businesses, HMRC's Corporate Finance Manual will be updated providing guidance to assist with understanding of the rules.

13.3 The basis for the final decision on what action to take to assist small business is that guidance will be sufficient to enable small businesses that enter into alternative finance arrangements or their advisers to compute their profits.

## 14. Monitoring & review

14.1 The approach to monitoring of this legislation is through normal compliance activity and regular communication with affected taxpayer groups.

14.2 In accordance with section 28(3)(a) of the Small Business, Enterprise and Employment Act 2015, this Order does not include a statutory review clause because it is made in relation to the imposition of a tax, duty, levy or other charge.

## 15. Contact

15.1 Liang Tang at HMRC, email: financialproductsbai@hmrc.gov.uk can be contacted with any queries regarding the instrument.

15.2 Richard Thomas, Deputy Director for the Financial Products and Services Team in Business, Assets and International at HMRC can confirm that this Explanatory Memorandum meets the required standard.

15.3 John Glen MP, Economic Secretary to the Treasury, can confirm that this Explanatory Memorandum meets the required standard.