

Chapter 13 Imports and Exports

Part A Goods imported before the delivery of an import entry

This part not yet allocated

Part B International Collaboration (Defence) Arrangements

Section 1 Background to the relief

1.1 Coverage

This guidance covers the relief available under Item 2 of Group 13, Schedule 8 to the VAT Act 1994. It explains the conditions relating to the zero-rating of supplies in connection with International Collaboration (Defence) Arrangements (ICDAs). In cases where relief is not applicable under Item 2 Group 13 you will need to consider whether other zero-rating provisions apply, particularly those covered by Groups 7 and 8 of Schedule 8.

1.2 Background to the relief

The relief for ICDAs has existed since the introduction of VAT. The terms of an arrangement are contained in the Memorandum of Understanding (MOU) or supplement thereto - see Section 3 - which contains a mutual tax waiver clause unequivocally committing all participating governments to ensure that their national taxes do not bear on the project or, failing that, to bear them themselves. The provisions of Item 2, Group 13 give a proper basis for such relief in terms of UK VAT law, without which any cost of UK VAT to other participants would fall as an additional burden on the Ministry of Defence (MOD).

1.3 HQ responsibility

The HQ section responsible for this area of the tax is the Government and Education Branch.

Section 2 EC and UK Law

2.1 European VAT law

There is no specific reference to International Collaboration Defence Projects (ICDPs) in EC law. However, the UK's authority to zero-rate supplies in connection with these projects is derived from EC Sixth Directive Article 28 paragraph 2(a) and EC Second Directive Article 17 (which allows zero-rates in force on 31 December 1975 to be retained). We accept that the conditions set out in these Articles are satisfied.

2.2 UK VAT law

ICDPs are eligible for zero-rating by virtue of Item 2 of Group 13, Schedule 8 of the VAT Act 1994:-

2. The supply to or by an overseas authority, overseas body or overseas trader, charged with the management of any defence project which is the subject of an international collaboration arrangement or under direct contract with any government or government-sponsored international body participating in a defence project under such an arrangement, of goods or services in the course of giving effect to that arrangement.

The main point to remember here is that relief only applies to supplies made to or received from either:

- (a) an overseas authority or body responsible for managing a qualifying project:
or
- (b) an overseas authority, body or trader under direct contract to a UK or overseas authority or body responsible for managing a qualifying project.

Note (1) defines an international collaboration arrangement:-

(1) An "international collaboration arrangement" means any arrangement which-

- (a) is made between the United Kingdom Government and the government of one or more other countries, or any government-sponsored international body for collaboration in a joint project of research, development or production; and
- (b) includes provision for participating governments to relieve the cost of the project from taxation.

The form of this arrangement is contained in a Memorandum of Understanding (MOU) (see section 3).

Note 2 defines an overseas authority:-

(2) "Overseas authority" means any country other than the United Kingdom or any part of or place in such a country or the government of any such country, part or place.

The term "overseas body" is explained in Note (3):-

(3) "Overseas body" means a body established outside the United Kingdom

Note (4) explains the term "overseas trader":-

(4) “Overseas trader” means a person who carries on a business and has his principal place of business outside the United Kingdom.

Section 3 What is an International Collaboration (Defence) Arrangement (ICDA)?

3.1 Introduction

ICDAs are arranged between the UK Government and one or more other governments or government sponsored agencies such as NATO. They can cover collaboration in research and all phases of equipment procurement and in-service support from design through development and production to post design services and the provision of spares, repair and maintenance. The legal definition of an ICDA is contained in Note 1, Group 13, Schedule 8 of the VATA 1994. The note identifies the two elements which must be present for a project to be eligible for zero-rating:-

- the arrangement must be made at government level;
- the project must be relieved from the effects of any taxation.

In this guidance ICDAs will be referred to as “ICDAs” initially then as “collaborative projects”. ICDAs can be complex and involve the use of highly technical jargon. Although it is not necessary to be an expert in the technical terms used, you will need a basic understanding of the structure of a typical ICDA project to ensure that the relief is properly applied.

Collaborative projects are agreed between national governments. They have a number of organisational levels:-

- **Level 1: Project definition, direction, control and funding**
The responsibilities at this level rest with the participating governments, with MOD representing the UK. The participants usually use a single body as a project management organisation (PMO). The PMO is funded by the participants and acts as contracting authority to procure the work required.
- **Level 2: Project management**
If there is a PMO, it may be an agency of one of the governments (e.g. UK’s MOD Procurement Executive) or a multi-national body which may be set up specifically for the purpose (e.g. the NATO Multi-Role Combat Aircraft Management Agency). It will be responsible to the participants and will employ one or more prime contractors which it will pay with funds provided by the participants. Any UK PMO will be registered for VAT. Participants’ funding of the PMO is consideration for supplies by the PMO to the extent that the supplies come within the scope of UK VAT. The PMO (or the individual participants if there is not a PMO) engages a prime contractor or prime contractors and each prime contractor may be expected to engage first level sub-contractors, who may engage second level sub-contractors and so on.
- **Level 3: Prime contractors**
At this level prime contractors from different countries will have been appointed to carry out specific technical responsibilities. (This is the highest level that you will encounter in the course of routine control visits).
- **Level 4: First level sub-contractors**
These will be appointed by the prime contractors and will have responsibility for specific technical parts of the project. (Item 2 Group 13 zero-rating cannot apply below the first level of transactions between a prime contractor and a first level sub-contractor. At this level prime contractors from different countries will have been appointed to carry out specific technical responsibilities).

- Level 5: Second and subsequent level sub-contractors
The number of parties involved as second and subsequent level sub-contractors may be quite large. Again they have specific technical responsibilities.

3.2 What is a Memorandum of Understanding?

The agreement reached by the different governments involved in the project is recorded in a *Memorandum of Understanding (MOU)*. This document determines whether the project is approved as an International Collaboration (Defence) Arrangement for the purposes of Item 2, Group 13 zero-rating. To be eligible for relief the project must involve international collaboration (i.e. a project undertaken by more than one nation) and it must be relieved from the burden of national taxes on other nations' shares of the cost. The MOU will have a clause stating that the project is relieved from taxes, customs duties and other charges.

Officers must contact the Government and Education Branch to confirm the status of collaborative projects. Not all MOUs relate to projects that qualify for Item 2 Group 13 relief (see Paragraph 4.2).

Section 4 Eligibility for zero-rating

4.1 Introduction

MOD is responsible for negotiating international collaboration MOUs on behalf of the UK. This process does not involve HM Customs and Excise either at Headquarters or local office level. But when MOD's General Finance Division identifies an MOU that meets the criteria for an ICDA for Item 2 Group 13 zero-rating, they will notify the Government and Education Branch. MOD have details of the participants, project management organisation (if any) and prime contractor(s) for the individual projects. Item 2 Group 13 zero-rating applies - in the absence of any other relief - to any supply by or to any of these bodies where one or other of them belongs overseas and the supply is in a chain that leads to the delivery to the participants of services or equipment in accordance with the objectives of the arrangement.

4.2 Relief from taxation and the extent of approval

An ICDA only qualifies for relief inasmuch as supplies follow the procurement chain prescribed in the relevant approved MOU. Not all MOUs in relation to a project will be approved for Item 2 Group 13 zero-rating. MOUs that are not will be excluded from the details in the project list. Any procurement in relation to a qualifying project but outside the approved MOU arrangements is not relieved. For example, for a project with a PMO, single nation procurement directly from the prime contractor would not be relieved if the relevant MOU prescribed the inclusion of the project management organisation in the supply chain.

A collaborative project does not have to run through all the stages of research, development, production and supply of the final product (including in-service support). In addition there is frequently more than one MOU in force for any one project. A collaborative project could be for research only or could take a proposal through to development but not include production. It is essential to confirm that the supplies with which you are concerned are properly covered by a valid MOU.

4.3 Supplies in the UK

All supplies made in the UK between the MOD and UK contractors follow the normal VAT rules. Relief under Item 2 Group 13 applies only to supplies made to or by an overseas body charged with the management of a collaborative project. Goods forming part of an ICDA may be delivered from one participating contractor to another within the UK for process or assembly.

4.4 United Kingdom Project Management Offices

A Project Management Office (PMO) based in the UK may be an agency of the UK MOD and under direct "contract" by the arrangement to the governments participating in the collaborative agreement. It may be a separate legal entity to the UK MOD and may make and receive its own supplies. As a result a PMO may require a separate VAT registration. Supplies by UK contractors to a PMO based in the UK are not covered by relief under Item 2. These supplies cannot meet the "supply to or by an overseas authority" criteria set out in Item 2. The relief available under Item 2 Group 13 also applies to charges made by a UK Project Management Office to an overseas government for managing a project on its behalf. If the PMO is established within MOD it is covered by MOD's VAT registration.

The Project Horizon programme Joint Project Office is the first and only example to date of a UK PMO established outside MOD. Supplies to MOD by such a separately registered UK PMO are not covered Item 2 Group 13 relief.

4.5 Final supply

Some difficulty has been experienced in defining the scope of Item 2 Group 13, in particular whether the relief extends zero-rating to the supply of the final product. Previously Item 2 had been interpreted as providing relief on supplies up to and including production of the equipment, but not on the final supply to the participating governments. This is because the law allows relief for the research, development and production elements of a project but did not specifically cover the supply of the finished product.

Following discussions with MOD we have accepted that governments would be unlikely to enter into such ICDA's without having access to the final product of the collaborative effort. Relief under Item 2 does therefore include the supply of the finished product (i.e. final supply) of a collaborative project.

4.6 Own variants

Own variant products from collaborative projects which, whilst researched, developed or produced jointly, include features specific to the requirements of an individual country, qualify for relief under Item 2, provided they are funded by the collaborative project.

In the MRCA Tornado project each of the three participating countries took a different variant of the basic aircraft. It is not necessary for the participating countries to take identical versions of the end product for the project to be eligible for zero-rating.

4.7 Imports eligible for relief

Goods imported by any UK contractor as the agent of an overseas authority, body or trader are zero rated under Item 2, provided:-

- the goods are imported to give effect to an ICDA with an approved MOU; and
- they include the following declaration in the supplementary information box of the Customs entry, box 44:

Zero rate Group 13 Item 2:-
The goods included in this entry are the property of (name of overseas customer) and are entered by (name of company) as agent, for the purposes of the (name and phase) International Collaboration Defence Project.

- include in box 47 of the Customs entry, the VAT rate as "VAX".

Note - all goods relating to an ICDA are the property of the PMO until the final supply is made to the respective governments. It follows that imports/acquisitions of goods by UK contractors are made in their capacity as agent of the PMO.

4.8 Import duty and the Ministry of Defence

The Duty on Defence Imports Memorandum (DODIM 77) allows the MOD to import defence related goods free of customs duty. Relief under DODIM 77 is also claimed where UK traders are importing goods on behalf of the UK MOD for defence contracts.

The UK MOD are shown as the consignee in box 8 of the C88 (Single Administrative Document). The UK MOD (not HM Customs and Excise) is the responsible authority to decide which goods qualify for this relief. Any enquiries as to eligibility should be referred to the UK MOD Defence Transport and

Movements Executive (DTMX Andover) for land and sea movements and to HQ Strike Command High Wycombe for air movements). In Customs and Excise TPG/SRT are responsible for policy on DODIM 77 imports.

4.9 Intrastat reporting arrangements - exceptions to the general rule

(i) Diversion of goods by MOD

If goods are diverted to a different EU member state, or to home use, by the MOD after supply by the manufacturer, no amending action should be taken. Under normal circumstances the declarant (in this case the manufacturer) would be required to make an amendment, however, it is considered that it would be impractical to require the MOD to inform the declarant of any diversion.

(ii) VAT/Intrastat mismatches

Tariff and Statistical Office (T&SO) consider that since both they and control officers are aware of traders who are involved in collaboration projects it will be possible to take this into account when dealing with discrepancies.

Section 5 Establishing that the conditions of the relief have been met

5.1 Supplies by the UK trader

Is the supply made by the trader (under contract) to an overseas authority, body or trader that is a participant in or project management organisation or prime contractor for an ICDA on the qualifying list?

Is the supply in a chain culminating in a supply to the participants under one of the MOUs (international collaboration (defence) arrangements) that are approved in respect of the qualifying collaborative project on the list?

5.2 Supplies to the UK trader

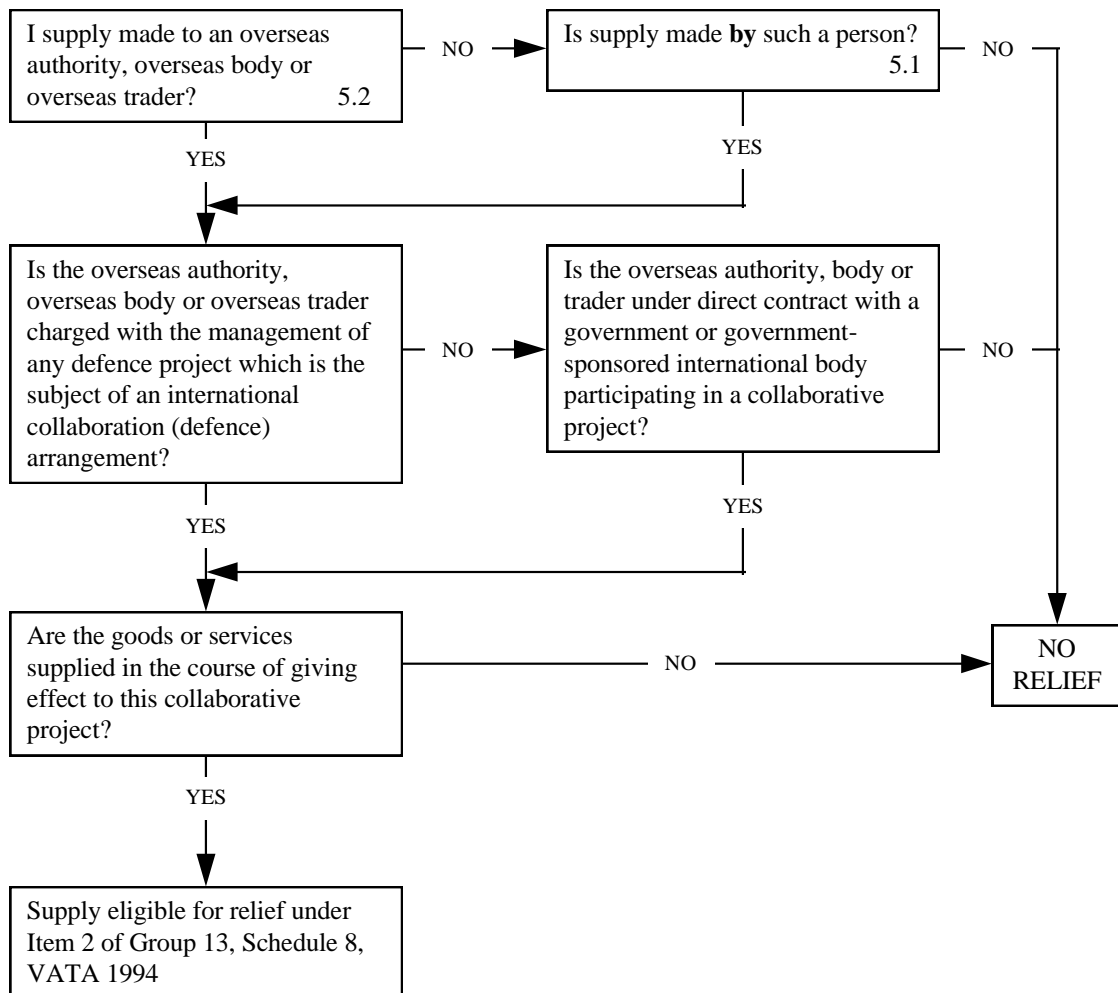
Is the supply to the trader made by an overseas authority, body or trader that is a participant in or project management organisation or prime contractor for a collaborative project on the qualifying list?

Is the supply in a chain culminating in a supply to the participants under one of the MOUs (international collaboration (defence) arrangements) that are approved in respect of the qualifying project list?

Item 2 Group 13 zero-rating only applies if the answer to both questions in Paragraphs 5.1 and 5.2 is yes.

Annex A Decision chart: Does the project supply qualify for relief?

This chart lists the factors which indicate whether a supply can be zero rated under Group 13 Item 2. At each stage of the chart you are cross referenced to the relevant part of this guide.



Annex B International Collaboration Defence Projects at 1 July 2002

AIRCRAFT

TORNADO (MRCA) - Multi-role Combat Aircraft
JAGUAR (Engine & Airframe)
EUROFIGHTER (TYPHOON) 2000
SPEY SM1A Support - Gas Turbines
CALF - Common Affordable Lightweight Fighter
FLA - Future Large Aircraft
JSF - Joint Strike Fighter

NAVAL EQUIPMENT

NATO VSHORADS/SHORADS - Very Short Range & Short Range Air Defence
Systems Programme
LR5 Submarine Radar System
NATO SINS - Ships Low Cost Inertial Navigation Systems
TALISMAN SSTD - Surface Ship Torpedo Defence
CNGF - Common New Generation Frigate (Project Horizon)
COBLU – Outboard Electronic System

HELICOPTERS

GAZELLE
PUMA
LYNX
EH 101

MISSILES/ORDNANCE

MILAN (improvement MIRA) - Weapon System
MLRS - Multi Launch Rocket System
M483A1 15mm Artillery Shell Sidewinder (AIM 9L) - Air to Air Missile System
TRIGAT (3rd Gen ATGW) - Anti Tank Guided Weapon
ACEATM - Aimed Controlled Effect Anti-Tank Mine
ASRAAM - Advanced Short Range Air to Air Missile
Goalkeeper CIWS - Close in Weapon System
PAAMS - Principle Anti-Air Missile System (formerly FAMS) including
Sampson Naval Radar
FH70 – Howitzer
NLAW – Joint Next Generation Light Anti-Armour Weapon System

ELECTRONICS

TACOMS 2000 - Tactical Communication Post 2000
Tech for Future Combat
EIFEL MOCRAT - Management Organisation for the Central Region Integrated
ADP System for Allied Tactical Operations Centre
COBRA - Counter Battery Radar Programme
MLS - Microwave Landing System
DATA - Demonstration of Aero-Engineering Technology
EUROACT - European Active Control Technology
NILE - NATO Improved Link 11
DIRCM CSM - Directional Infrared Countermeasures System

OTHER

MRAV – Multi-Role Armoured Vehicle