Pension schemes and VAT: the Revenue speaks

After a long silence, HMRC has issued a Revenue & Customs Brief responding to last summer's decision of the Court of Justice of the European Union in the PPG case. This may provide an opportunity for employers with occupational pension schemes to reclaim VAT previously paid on certain investment-related activities.

Background

HMRC's existing VAT Notice 700/17 allows employers to deduct VAT incurred in relation to the general management of an occupational pension scheme, on the basis that these costs are overheads of the employer. However, HMRC's long-held view has been that when trustees make investments, this is not the employer's business and so employers cannot claim input tax on the costs of managing those investments.

In the PPG case, the CJEU appeared to challenge this approach. It held that a Dutch employer was entitled to deduct the VAT it had paid on administration and pension fund management services, so long as there was a "direct and immediate link" between those services and the employer's own supplies.

Moving the goalposts?

The Brief announces a change in policy, effective immediately. HMRC now accepts that investment-related services, which "go further than management of the investments", may be general costs such that VAT incurred on them is potentially recoverable by an employer.

However, HMRC warns that specific costs of investment management, such as the costs of managing a property within a pension fund, are not general costs of the employer and so cannot be recovered; and "a similar analysis can be applied to… financial investments." Nor will HMRC accept that VAT is deductible where the services are "*limited to investment management… only*".

HMRC emphasises that the supply must be received by the employer, and that whether the employer commissioned and paid for the services in question may be relevant to establishing this. If the employer receives the supply but the pension fund bears the cost, HMRC say they will require an equivalent amount of output VAT in respect of the amounts reimbursed to be accounted for by the employer.

Employers who receive supplies of services that fall within HMRC's revised criteria can make claims going back up to four years. Any claim must set out the basis of the change, and the amount now claimed. HMRC reserves the right to seek further background information.

No more 70/30

The Brief also signals the end of HMRC's 70/30 rule. Where it was not possible to break down an overall fee into elements paid for general management and investment activities respectively, employers would assume that 70% of activities were management and the remaining 30% were investment. Use of the 70/30 rule will still be allowed for a six-month transitional period. Employers will now have to give careful thought as to how fees are broken down.

DC schemes

The PPG decision concerned a defined benefit pension scheme. However, the Brief refers to a pending CJEU case, ATP, which will address the issue of VAT paid on investment management services under DC schemes. If the Court decides VAT should not have been charged on such services, HMRC will take "appropriate steps" in relation to input tax claimed by managers of DC schemes, including issuing assessments to recover any VAT that was incorrectly deducted.

Action points

Employers should consider with trustees and advisers the extent to which they may now be able to reclaim any VAT paid in relation to their pension schemes. Going forward, employers and trustees may also wish to review their VAT arrangements including fee structures, especially given the references in the Brief to which party commissions, and pays for, services. Note that HMRC is to formally amend its VAT Notice in due course, which may bring greater clarity as to its thinking.

The HMRC statement can be found at: http://www.hmrc.gov.uk/briefs/vat/brief0614.htm

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