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Case alert

The University of Cambridge

March 2018

Summary

The Court of Appeal has decided to refer this case to the Court of Justice of the European Union.

The issue – whether the University is entitled to reclaim VAT incurred on fund management fees – is, in a VAT sense, of great importance. The University has an endowment fund which is managed by a third party fund manager. The fund manager charges fees to the University for the services it provides and the question to be resolved is whether those costs are to be regarded as overheads of the University and, if so, whether the VAT on those costs is reclaimable by the University in accordance with its partial exemption special method.

The University argues that the operation of the fund is solely to further its overall activities which includes the making of both taxable supplies (giving a right of deduction) and exempt supplies.

HMRC takes the view that the fund manager's fees are 'consumed' by the investment activities of the fund and the VAT charged by the fund manager is not reclaimable.

Both the First-tier Tax Tribunal and the Upper Tribunal found in favour of the University and this is HMRC's appeal to the Court of Appeal.

Court of Appeal – Judgment released 27 March 2018

The University of Cambridge has a large endowment fund which generates in excess of £40 million per year from investment returns. The fund is managed by a third party fund manager and the case relates to whether VAT charged to the University by the fund manager in relation to the management of the fund can be reclaimed by the University as input tax. The University makes some taxable supplies but it also makes exempt supplies of education and has some non-business activities. It operates a partial exemption special method (PESM) and it argues that, following case law from the Court of Justice, it should be entitled to reclaim a portion of the VAT incurred.

The University relies on a number of CJEU judgments. Most importantly, it relies on the judgments in the cases of Kretztechnik AG (Case C-465/03) and Securenta AG (Case C-437/06). In both those cases, the Court of Justice looked beyond the specific exempt transactions (in those cases, sales of shares) and agreed that the costs in question were, in fact, attributable to the overall business activities of the taxpayer. As such, the VAT could be attributed to neither exempt nor taxable supplies and fell to be treated as 'residual' input tax that should be apportioned in accordance with Article 173 of the VAT Directive.

HMRC, on the other hand, rely on a different judgment of the Court of Justice in the case of Wellcome Trust (Case C-155/94). In that case, the Court ruled that the Trust was not entitled to reclaim input VAT it had incurred on the sale of some of its shares. In selling the shares, the Court took the view that Wellcome acted as a 'private' investor which is, in itself, not an economic activity from a VAT standpoint and, as such, the Trust was unable to claim the VAT it had incurred. HMRC argued that, in essence, there was no real difference between the facts pertaining to the University's position and the fact as found in the Wellcome Trust case.

The Court of Appeal has decided that it needs guidance from the Court of Justice on the correct interpretation of the VAT Directive. Is it entitled, as in Kretztechnik and Securenta, to look through the funds transactions to the general purpose of furthering the University's overall transactions or should it, as in Wellcome Trust, determine that the fund manager's costs have been 'consumed' wholly by the fund?

Comment – the answer to those questions will be of great interest in that the Court's judgment should go some way to settling whether one looks at the overriding purpose of the expenditure (as argued by the University) or whether one should attribute costs to the activity that immediately consumes the cost (as argued by HMRC). It is likely to be 18 months or so before the issue is resolved.

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