

VAT Alert

HMRC changes policy on Pension Schemes

VAT treatment of fund management services by insurers to change

Summary

HMRC has published a change of policy in relation to the VAT liability of fund management services provided by regulated insurance companies. The existing policy is for such services to be exempt from VAT and derives from a long-standing decision to exempt all insurance services (including pension fund management).

The new policy is to be introduced with effect from 1 January 2018 and will treat the supply of pension fund management services as taxable where the pension scheme in question does not qualify as a special investment fund. This change may have a significant impact on defined benefit pension schemes managed by insurance companies as VAT will now be chargeable.

HMRC has changed its policy in relation to the VAT liability of fund management services provided by insurance companies to certain pension funds.

Historically, HMRC has treated the supply of pension fund management services by a regulated insurance company as being exempt from VAT on the basis of the supply being a supply of insurance services as opposed to being a supply of fund management services. Insurance companies have therefore treated their supplies of fund management as being VAT exempt irrespective of the status of the pension scheme. EU VAT law stipulates that the provision of fund management services to a 'special investment fund' (a SIF), is the only fund management service that can qualify for VAT exemption.

The Court of Justice has (in the 'Wheels' and 'ATP' cases) distinguished which pension schemes qualify as SIF's and which do not. Only defined contribution schemes – which generally pool investments and spread investment risks etc. qualify as SIF's whereas defined benefit schemes do not. Consequently, fund management services to a defined contribution scheme qualify for VAT exemption whereas fund management services provided to a defined benefit scheme are liable to VAT at the standard rate.

HMRC's change of policy acknowledges that, in some cases, the insurance companies have provided fund management services to defined benefit schemes and, because of the application of the old policy, VAT is not charged on those services even though the pension scheme is not a SIF for VAT purposes. As such, there could be a breach of the principle of fiscal neutrality if the UK continued to allow insurance businesses to exempt those supplies.

Comment – it seems clear that this change of policy acknowledges that HMRC's historic treatment of fund management services by insurance companies as being exempt from VAT has been incorrect. VAT will become chargeable on such supplies to non-SIF pension schemes from January 2018. However, by such acknowledgment, it also seems clear that non-SIF pension schemes may have a valid claim under the principle of fiscal neutrality if, historically, they have been charged VAT by their fund managers. Compare their VAT position with a non-SIF pension scheme that received VAT free fund management services from an insurance company.

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