

Employer recovery of VAT on pension scheme services and VAT treatment of fund management services provided by insurers – updates on HMRC’s position

HM Revenue & Customs (“**HMRC**”) has updated its VAT Input Tax Manual (the “**Manual**”) to set out its finalised position on employer recovery of VAT charged on services provided to occupational pension schemes. Among other things, this confirms the indefinite extension of the concession allowing employers to recover 30% of the VAT charged on combined administration and investment services.

HMRC has also decided to delay withdrawal of the VAT exemption for fund management services provided to pension schemes by insurance companies until 1 April 2019.

Employer recovery of VAT charged on pension scheme services

HMRC’s policy regarding employer recovery of VAT charged on pension scheme services has been unclear since a Court of Justice of the European Union case in 2013 (the *PPG* case). Prior to the *PPG* case, HMRC allowed employers to recover VAT charged on administration services, but not VAT charged on investment services. Where an invoice covered both administration and investment services, an employer could treat 30% of the invoice as relating to administration and therefore recover 30% of the VAT (unless it could persuade HMRC that it should recover a higher percentage).

Since the *PPG* case, HMRC has published various pieces of guidance setting out its developing policy on employer recovery of VAT on pension scheme services in light of *PPG*. Although this guidance proposed a number of possible employer VAT recovery arrangements, each such arrangement raises potential regulatory and/or tax issues for the employer and/or the trustees. These arrangements include the use of a tripartite agreement between the employer, the trustees

and the service provider; VAT grouping; and the supply of scheme administration services to the employer by the trustees or a separate holding company or service company.¹ Further guidance finalising HMRC’s policy has been expected for some time. In the meantime, HMRC has operated a transitional period whereby employers can still use the 30/70 split, but this period was due to expire on 31 December 2017.

Instead of issuing the awaited guidance, HMRC has updated the Manual² to provide that:

- the 30/70 split will continue to be available to employers indefinitely; and
- the other proposed methods for employer recovery of VAT charged on pension scheme services will also be available, subject to the potential regulatory and/or tax issues that these may raise.

Fund management services provided by insurance companies

Currently, fund management services provided by insurance companies to pension schemes are exempt from VAT. In October, HMRC announced in Revenue and Customs Brief 3 (2017) (“**RCB3 (2017)**”) that this exemption will be discontinued, with the result that insurance companies will be required to charge VAT on certain of the pension fund management services that they provide.³ On 20 November, HMRC clarified that the exemption will be discontinued from 1 April 2019. We understand that HMRC accepts that not all fund management services provided by insurance companies will cease to be treated as exempt. The dividing line between those services that will continue to be exempt, and those that will be subject to VAT from 1 April 2019, is still to be clarified (this is discussed further below).

¹ For more information, please see our [November 2015 legal update](#).

² See sections VIT44600 – VIT45510.

³ For more information, please see our [October 2017 legal update](#).

What should schemes be doing

Employers can continue to deduct VAT charged on pension administration services, provided that the invoices are made out in the name of the employer.

Where investment services are concerned, the position differs depending on whether the scheme is a DB or DC scheme. Investment services provided to DC schemes should generally benefit from a separate VAT exemption, whether or not provided by insurance companies, and the question of employer recovery of VAT charged on such services should not therefore usually arise for DC schemes.

The position for DB schemes, however, is more complicated. Fund management services provided to DB schemes by insurance companies will continue to be exempt from VAT until this exemption is revoked in April 2019. We understand that HMRC also agrees that management services provided by insurance companies under arrangements taking the form of a contract of insurance will continue to be exempt after April 2019, although it is hoped that HMRC will amend RCB3 (2017) to make this clearer. Investment services provided by other entities to DB schemes (and fund management services provided by insurance companies once the exemption is revoked) will be subject to VAT, and the employer can either:

- use the 30/70 split to recover 30% of the VAT charged, provided the investment service provider also provides some administration services⁴; or
- use one of the other options for employer VAT recovery outlined in the Manual such as a tripartite agreement or VAT grouping.

⁴ Section 44750 of the Manual sets out a list of which services HMRC considers to be administration services, investment services, and both administration and investment services.

Should the employer wish to use one of these other options, we would advise the employer and the trustees to seek advice on the legal and tax implications of the chosen option to ensure that it delivers the VAT recovery outcome sought by the employer, and that any potential regulatory and/or tax issues are dealt with. Schemes and employers should also wait for further guidance from HMRC as to precisely which services provided by insurers will or will not be treated as exempt by HMRC in future, given that HMRC has now clarified that not all services provided by insurers will cease to be treated as exempt.

If you have any questions about this update, please get in touch with your usual Mayer Brown contact.

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