

In response to a decision of the Court of Justice of the European Union, HM Revenue & Customs (HMRC) has changed its position regarding an employer's entitlement to deduct VAT paid on services relating to the administration of occupational pension plans and the management of pension plan assets. [Sponsoring employers of defined benefit occupational pension plans should consider restructuring agreements with service providers to take advantage of this development and maximise VAT recovery going forwards. It may also be possible to claim refunds of input VAT for pension plan costs previously incurred.](#)

Background

For many years HMRC operated on the basis that employers could deduct VAT incurred on fees charged for the administration of an occupational pension plan, as these costs could be viewed as an overhead of the employer. However, the same could not be said of VAT incurred in respect of costs relating to the management of the pension plan's investments, as such costs were considered to relate solely to the activities of the pension plan.

Where the relevant services were commissioned by the pension fund trustees and a single invoice was issued to the employer (covering both the administration of the pension plan and the management of its investments) then the practice allowed by HMRC, as an "administrative simplification", was to attribute 30% of the invoice to administration services. As such, the employer could recover the VAT on this proportion of the invoice, if it was carrying on a VATable business. The remaining 70% of the invoice was deemed to relate to investment management costs. As a consequence, the VAT associated with the 70% would be predominantly irrecoverable because it is likely that the pension fund would be carrying on VAT exempt activities.

This longstanding practice was called into question by a decision of the Court of Justice of the European Union in *Fiscale Eenheid PPG Holdings BV cs te Hoogezand (C-26/12)* ("PPG"). On the facts of this case the CJEU held that both the administration and the investment management costs associated with a defined benefit Dutch pension plan could be treated as part of the employer's overhead. This created the opportunity for all of the associated VAT to be recovered by the Dutch employer to the extent to which it was fully VATable.

Following the PPG case, HMRC has reconsidered the treatment of VAT incurred on costs relating to the administration and management of investments of occupational pension plans. Its resulting change of position was publicised in November 2014, in [Revenue and Customs Brief 43 \(2014\)](#) ("Brief 43"). It has, more recently, provided further details about what employers need to do to be able to recover VAT on defined benefit pension plan costs in [Revenue and Customs Brief 8 \(2015\)](#) ("Brief 8").

What Has Changed?

Brief 43 and Brief 8 represent both good news and bad news for the sponsoring employers of defined benefit pension plans.

The Good News

Brief 43 makes it clear that it is now no longer necessary to differentiate between costs incurred in the administration of a pension plan and the management of its assets. VAT incurred in relation to both types of cost is recoverable by an employer carrying on a VATable business if it can be demonstrated that the services in question were provided to the employer. Particular considerations are that the employer is a party to the contract which has commissioned those services (the contract is therefore likely to be a tripartite agreement between the trustees, the employer and the service provider) and it has paid the service provider for the relevant services.

This creates a cost saving opportunity for employers to increase the VAT that they can recover on fees incurred in the running of their pension arrangements.

Brief 8 provides further detail on how a tripartite contract between the employer, the trustees and the service provider should be structured. As a minimum, HMRC expects the contract relating to a defined benefit pension plan to cover the following:

- That the service provider makes its supplies to the employer (albeit that the contract may recognise that the service provider may be appointed by, or on behalf of, the pension plan trustees).
- That the employer directly pays for the services that are supplied under the contract and in the event of non-payment the service provider will pursue the employer for payment and only in circumstances where the employer is unlikely to pay (for example, because it has gone into administration) will it recover its fees from the pension plan or the trustees.
- That both the employer and the pension plan trustees are entitled to seek legal redress in the event of breach of contract (albeit that that this does not result in the service provider assuming any additional liability, and any payments flowing from a breach of contract may be payable to the pension plan not the employer).
- That the service provider will provide fund performance reports to the employer on request (subject to the trustees being able to stipulate that reports are withheld, for example where there could be a conflict of interest).
- That the employer is entitled to terminate the contract, although this may be subject to a condition that they should not do so without the trustees' prior written consent (this can be in addition to any right that the trustees may have to terminate the contract unilaterally).

In addition to the above, HMRC has also stated that evidence that the pension plan trustees agree that it is the employer who is entitled to deduct any VAT incurred on the services will reduce the potential for disputes.

Brief 43 also creates potential opportunities to recover VAT paid in the past. It indicates that where an employer can demonstrate that it was historically the recipient of a supply of administration and/or investment management services provided in connection with its pension plan, then it will be able to claim a refund of input VAT previously paid in connection with such services. In other words, the restriction on VAT recoverability on investment management services imposed by the 70/30 split may be reversed in the right circumstances. However, claims for repayment can only be made for the four years leading up to the date the claim is made.

Finally, Brief 43 and Brief 8 both confirm that during a transitional period, which will last until 31 December 2015, where the pension plan receives the services, the pension plan and the employer may continue to agree to the 70/30 split for VAT purposes, as was previously the case.

The Bad News

The former practice of splitting relevant pension plan service provider invoices 70/30 for VAT purposes can only continue to be utilised by employers and pension plans until 31 December 2015. After this date, HMRC will not automatically assume that 30% of a relevant invoice will relate to administration services and allow an employer to recover the VAT paid on this proportion of the invoice. Instead, an employer will only be able to recover VAT incurred in connection with pension plan administration and investment management services if it can demonstrate that the employer is the recipient of those services (as described above). Employers should take action if they wish to continue deducting VAT paid in connection with these services.

What Actions Should Sponsoring Employers of Defined Benefit Pension Plans Take?

Employers wishing to preserve, and enhance, their existing VAT recovery position, should consider entering into tripartite contracts with the trustees and service providers of their pension plans, under which the employer pays for the relevant services. They should check that these contracts comply with the minimum requirements specified by HMRC in Brief 8 (see summary above).

In putting these arrangements in place:

- a) It will be necessary to ensure that the tripartite contract under which the service provider contracts with both the pension plan trustees and the employer does not result in the trustees failing to comply with any fiduciary duties that they are subject to, or breach any obligations under pensions legislation. Trustees will also wish to ensure that their own existing rights under the current contract are not weakened under a new contract. Legal advice should be sought.

- b) The employer must not recharge the service provider's costs to the pension fund, as this would constitute the making of a VATable supply by the employer to the pension fund (although Brief 8 does state that, in some circumstances, the normal adjustment of employer contributions resulting from the fact the employer not the fund is meeting certain costs will not amount to consideration for a supply by the employer to the pension fund, provided there is no specific reduction equal to the actual costs that were incurred in any given period).

Employers who have previously utilised the 70/30 split when establishing the VAT that they can deduct for pensions administration services should consider whether VAT paid on investment management services could also be recovered in respect of the last four years. This will depend on whether the services provided by the investment manager can be treated as having been made to the employer, as a question of VAT law, and will involve a detailed consideration of the evidence in each employer's case. In the first instance we recommend that a discussion with a tax lawyer would be beneficial, to establish whether a claim for a refund is worth pursuing.

And Finally... Watch This Space...

The position regarding VAT and the provision of pension plan services differs for defined contribution plans. HMRC generally views defined contribution plans differently, due to separate European case law that applies to this type of pension arrangement.

In Brief 8 HMRC has indicated that it will provide further guidance "in the summer" on the impact of the PPG decision on VAT recoverability relating to:

- Other types of service (such as legal, actuarial and accounting services).
- Other types of pension plans (such as defined contribution and hybrid plans).
- VAT Groups that include a corporate trustee and a sponsoring employer.
- Trustees that charge employers to run their pension plans.

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