

## VAT update – Important changes for Pension Schemes

The treatment of VAT incurred on the cost of pension scheme management has for a long time been a source of some debate given that, by their very nature, pension schemes do not fit neatly into the VAT landscape.

In our experience a number of DB schemes are currently operating as follows in respect of scheme running costs:

- The scheme is paying the cost of actuarial, administration and other running costs either directly to the 3rd party suppliers or by recharge of the net (of VAT) cost from the employer who has in turn paid the 3rd party suppliers;
- The employer is recovering in full the VAT incurred on the above costs;
- The employer is paying any investment management fees (other than those which are built into the 'bid / offer' spread of investment pricing or which are deducted directly from the investment portfolio);
- The employer is not reclaiming any VAT incurred on investment management fees.

### HMRC previous policy

HMRC policy has always been to distinguish between costs incurred in relation to the:

1. Setting up and day to day administration of occupational pension schemes; and
2. Investment management relating to the assets of occupational pension schemes

HMRC allowed employers to recover VAT incurred in relation to the administration of an occupational pension scheme. This is on the basis that these costs were overheads of the employer and thus had a direct and immediate link to the employer's business activities.

However, in respect of investment management costs, HMRC considered these costs to relate solely to the activities of the pension scheme. Therefore, VAT on these costs, generally speaking, could not be recovered by the employer.

In some cases a single invoice may be received covering both the administration of the pension scheme and the management of the investments HMRC have allowed the employer to only reclaim 30% of the VAT incurred as relating to the administration of the scheme.

*During 2014 and 2015 HM Revenue & Customs (HMRC) updated its stance on VAT and defined benefit (DB) pension schemes following the decision of the European Court of Justice case involving PPG Holdings BV.*

VAT update

## **HMRC current policy**

HMRC has now revised its view on VAT and DB pension scheme management costs.

As a result of the PPG judgement there are now circumstances where employers may be able to claim additional VAT input in relation to pension schemes where they were not previously able to do so.

HMRC now accept that where VAT is incurred in relation to a pension scheme (irrespective of whether in respect of administration or investment services) that VAT may be recovered by the employer. If there is contemporaneous evidence that the services are provided to the employer

and, in particular, the employer is a party to the contract for those services and has directly paid for them additional input VAT recoveries may be possible. As a result in order to make a recovery of VAT the employer will require a valid VAT invoice addressed to it rather than the scheme.

If, having settled the suppliers invoice, the employer makes a recharge of the net (of VAT) cost to the scheme this is considered by HMRC to be a taxable supply by the employer to the scheme. VAT will need to be charged and in a lot of cases this VAT will not be recoverable by the scheme itself.

## **Practical Implications**

In order to remain compliant with VAT rules, and not suffer additional VAT costs, it will be necessary for some advance planning to be undertaken. This may include:

### **1. Scheme Administration / Actuarial / Accounting costs**

From 1 January 2017 VAT incurred on scheme administration, actuarial, legal, accounting and other service costs (if these services are contracted for or paid for or invoiced to the scheme) will no longer be recoverable by the employer.

In order to continue to obtain input VAT recovery it will be necessary for the contracts with the relevant supplier to be re-documented as tripartite contracts between the provider and both the scheme and the employer. In addition, such costs will need to be invoiced to and paid by the employer with no recharge of any of these costs to the scheme.

Clearly, a number of these changes may disturb what is currently set out in the Schedule of Contributions and these may also need re-consideration and revision.

Provided the appropriate documentation is put in place however in most cases there should be no additional VAT cost as a result of these changes.

### **2. Scheme Investment Management costs**

In respect of scheme investment management costs, these new rules may provide the opportunity for additional VAT recovery by the employer over and above what has been the case up until these changes. In addition it may be possible to make a retrospective input VAT claim for up to the previous 4 years.

The conditions for VAT recovery on investment management costs are now the same as those for administration costs and, providing these tests can be satisfied, a full recovery may be able to be made. However again the key is that the employer must be:

1. A party to the contract and be a recipient to the supply;
2. Making the payment of fees directly to the investment manager with no recharge to the scheme; and
3. Receive a valid VAT invoice from the investment manager addressed to the employer.

*In view of the significant practical changes that the new requirements may introduce HMRC have allowed a transitional period. This runs until 31 December 2016 and during this time the old rules can continue to be applied.*

### **Take the lead – it may well be in your favour**

Whereas it is undoubtedly necessary to ensure continued recovery of VAT on administration costs, we would also recommend considering whether any additional VAT recovery might be possible, either retrospectively in the past or in the future (or both), on investment management costs?

A pro-active, independent VAT review in respect of the effect of the pension scheme on the sponsoring employer prior to receiving any contact from HMRC would help you be on the front foot and understand the likely impact of the changes. It may also highlight opportunities for further recovery and possibly retrospective claims.

Our expert, specialist VAT team would be happy to assist in this respect on a fixed and / or contingent fee basis if that would be of interest to you. If you would like to set up a meeting of simply discuss the situation in more depth please contact Barry Gostling on 01473 220080 or email [barry.gostling@ensors.co.uk](mailto:barry.gostling@ensors.co.uk).

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