

VAT Treatment of Fund Management Services Review

Summary of Responses

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Chapter 1

Introduction

1.1 At Budget 2020, the government announced a wide-ranging review of the UK fund regime, covering tax and relevant areas of regulation and including a VAT workstream. This was in response to stakeholder representations that suggested there were opportunities to enhance the UK's attractiveness for fund domicile and related entities.

1.2 In December 2022, the government published a technical consultation on the VAT treatment of fund management services. The consultation set out how the government intended to achieve the twin aims of: (i) improving policy clarity and certainty for all stakeholders on the application of the VAT exemption for fund management services and (ii) removing reliance on retained EU law. It proposed to:

- Codify in legislation what was meant by the term Special Investment Fund in respect of the VAT treatment of fund management, and
- retain the current list of exempt fund types, comprising Items 9 and 10 of Group 5, Schedule 9 of VAT Act 1994 (VATA), to which the fund management exemption applies.

1.3 The current UK regime for the VAT treatment of fund management depends on two elements: (i) UK law, which sought to implement the EU VAT directive while part of the EU, and (ii) direct effect of CJEU cases based on the application of Article 135 (1)(g) of the EU VAT Directive. UK law lists fund types eligible for exempt management in Items 9 and 10 of Group 5 of the VAT Act (VATA), effectively a 'whitelist'. CJEU caselaw has been distilled into five principles which a fund must meet to count as a 'Special Investment Fund' (SIF), and SIFs are also eligible for exempt management.

1.4 The approach outlined in the consultation aimed to support the UK fund management industry that currently utilises the VATA provisions and do not meet the SIF criteria, and those that do meet the SIF criteria but not the VATA provisions.

1.5 The consultation ran for eight weeks and closed on 3 February 2023. A copy of the consultation is available at:

[221130_VAT_on_fund_management_condoc.pdf](#)
([publishing.service.gov.uk](#)).

1.6 The government is grateful to all those who responded and took the time to provide their views as part of this consultation process and recognises the time and effort that went into the submissions. In total 37 written responses were received. Responses came from a variety of stakeholders, including suppliers and recipients of fund management services, law firms, as well as trade associations. To further clarify and supplement these written submissions, government officials met 9 industry stakeholders.

1.7 Other VAT policy reform options in relation to fund management did not fall within the scope of this consultation. However, the government keeps all taxes under review and welcomes representations to help inform future decisions on tax policy in this area.

Chapter 2

Summary of responses

1.8 Overall, respondents welcomed the government's approach, agreeing that retaining Items 9 and 10 would provide greater clarity and reduce uncertainty in the VAT treatment of fund management. However, they suggested there could be greater clarity on the application of the existing fund management VAT exemption by defining the term management.

1.9 Many respondents stated an interest in the opportunity to comment on any future proposals to legislate for SIF, which would help their understanding of any new legislation or guidance prior to it being enacted.

1.10 Below is a summary of responses received to the consultation questions:

Q1: Do you agree that the proposed approach to refine the UK law covering the VAT treatment of fund management, set out above, achieves its stated aims?

1.11 The majority of respondents agreed that the government's proposed approach went some way to achieving the aims of greater clarity.

1.12 However, respondents highlighted areas of uncertainty that would remain. A key concern included that the proposed SIF criteria were vaguer than Items 9 and 10, and that they may be difficult to apply to some fund types that currently fall within the scope of the VAT exemption under Items 9 and 10.

1.13 Respondents also expressed concerns that the proposed approach did not address issues that could arise relating to non-UK domiciled funds. They suggested that the government needed to ensure that any VAT treatment changes would not interfere or impact on the current input tax recovery position of firms providing fund management services to non-UK domiciled funds.

1.14 The call for a wider definition of 'management' was almost universal in written responses and follow-up submissions.

1.15 Although not within the scope of this consultation, several respondents suggested that a definition of fund management should include outsourcing and reflect current technologies, effectively widening the scope of the exemption. particularly for outsourcing various aspects of fund management and to ensure that any definition of 'management' reflects current technologies.

Q2: Do the proposed legislative reforms present any issues for your business?

1.16 Respondents raised some concerns that the proposed legislative reforms, in particular what would constitute a SIF, would impact their business.

1.17 Many respondents supported the government's proposal to retain Items 9 and 10, so that the fund management VAT exemption would continue to apply to all fund types listed, with a view that the government could extend that list as new fund types emerged.

1.18 Respondents stated the need for further clarity regarding proposed SIF criterion (d) i.e. Undertakings for the Collective Investment in Transferable Securities (UCITS).

1.19 Further clarity is also sought on the risk of litigation regarding proposed criterion (d). Respondents believed that it would be down to interpretation as to whether a non-UCITS fund type is subject to the same conditions of competition and appeal to the same circle of investors as UCITS. Respondents suggested that proposed criterion (d) should not be linked to the concept of a UCITS, as the attributes associated with this fund type may define the 'conditions of competition' and circle of investors' more narrowly than is appropriate.

1.20 The need to further clarify how a taxpayer should determine the competition and criteria for appeal was also highlighted.

1.21 The majority of respondents called for the government to broaden the proposed scope of the fund management exemption to permit other types of marketed funds.

Q3: Do you currently rely on Items 9 and 10 of Group 5, schedule 9 of VATA or exempt any transactions using that law?

1.22 24 of the 37 respondents confirmed that they rely on or extensively use Items 9 and 10 of Group 5, Schedule 9 of VATA. Most stated that their clients, business, and individuals, actively choose to invest in fund types listed in Items 9 and 10, where the

management services are subject to the VAT exemption. The fund types mentioned included, Open-Ended Investment Companies (OEICs), Authorised Unit Trusts, Authorised Contractual Schemes, and qualifying pension schemes where the fund management is exempt under Item 9; and: closed-ended investments, such as Investment Trust Companies, where the fund management is exempt under Item 10. Many of these respondents thought that relying exclusively on Items 9 and 10 provided them with greater certainty than the SIF principles.

1.23 5 respondents believed that they did not rely on Items 9 and 10 as they provide their fund management services to non-UK domiciled funds.

Q4: Would the legal definition for ‘Collective Investment’ in Financial Services and Markets Act 2000 (FSMA 2000) meet the intended aim of providing much greater certainty over correct application of the associated qualifying criteria?

1.24 Many respondents suggested that while the Collective Investment definition in FSMA 2000 provided some clarity, more could be achieved when considering fund management VAT exemption.

1.25 Most respondents highlighted that the FMSA 2000 definition left scope for interpretation and therefore uncertainty. Common issues that respondents raised included that the definition was complex, as there are many exclusions from the definition.

1.26 Respondents suggested that the ‘collective investment’ definition could be clarified by formalising the definitions of ‘management’ and ‘marketing’. They further suggested that clear and precise guidance, including worked examples, would enable greater certainty.

1.27 The majority of respondents suggested that the proposed approach did not contain any obvious territorial limitations to prevent the inclusion of every UCITS or similar fund, regardless of where they are domiciled, within the scope of the fund management VAT exemption.

Q5: If the answer to 4 is no, how might the government improve the definition [of Collective Investment] to attain that aim?

1.28 Respondents suggested that the Collective Investment definition be included as a 'standalone' definition within Group 5 or for the government to provide for a fuller definition within secondary VAT legislation.

1.29 They were broadly positive about the need to retain Items 9 and 10. They however sought to be kept informed of any future additions to the Items and provide their views as part of the consultative process.

1.30 The majority of respondents suggested that a list-based approach would provide greater clarity and leaves less room for interpretation.

1.31 There were some recommendations to broaden the definition of SIF to include Specialist Fund Segment (SFS) traded collective investment companies. Most felt that, despite the lack of a specific proposal at this stage, it may in principle provide further certainty. Given the scope of the current VAT exemption, a definition based on a principle of collective investment would likely create more litigation for the industry. Respondents predicted that there would be an extensive increase in litigation as taxpayers and HMRC attempted to apply a principles-based approach to specific funds.

1.32 Another key point raised was that the government should address wider certainty around what constitutes 'management'. Many felt that the definition of 'management' has been subject to a significant amount of litigation and would appreciate greater clarity in this area.

1.33 As part of this, some suggested a broader definition of 'management' for VAT purposes to reflect current technologies. For companies that outsource various parts of 'fund management' to third parties, particularly where outsourced service are partially automated or IT-enabled, it is unclear on how this should be taxed. Overall, there were calls for greater clarity on the extent to which outsourced fund management services qualify for a VAT exemption.

Q6: Are there any further VAT related modifications the government might introduce under these or future reforms to improve the fund management regime for taxpayers?

1.34 While this was not in the scope of this consultation, the majority of respondents set out their belief that the introduction

of a VAT zero rate for fund management of UK domiciled funds would increase UK fund domicile. They considered that such a change in the VAT treatment of fund management would put UK funds on the same footing as non-UK domiciled funds, making the UK funds environment more competitive and encouraging growth.

Chapter 3

Wider engagement

1.35 The public consultation ran between 9 December 2022 and 3 February 2023.

1.36 To better understand respondents' concerns, the government held a series of meetings between 7 June and 14 July 2023 to explore the various industry operating models and how they interacted with the proposed reforms.

1.37 The government also tested views in relation to the impact of the Retained EU Law (Revocation and Reform) Act 2023 coming into effect at the end of 2023. Therefore, government officials conducted further bilateral engagement with individual businesses and industry bodies over the autumn to ensure that its proposed legislative approach is clear, provides certainty, and is as simple as possible.

1.38 The majority of stakeholders understood the reasoning behind the government's proposal for a principled-based approach to determine if a fund type was exempt from VAT, but preferred a list-based approach in determining whether the fund management VAT exemption applied. Stakeholders felt that such an approach provided greater clarity and certainty. They believed that a principled-based approach left room for interpretation, would be time consuming for businesses to determine and could lead to greater litigation rather than less.

1.39 Although from the consultation it was clear that Items 9 and 10 were widely used, the government undertook further work with industry to determine whether Items 9 and 10 captured fund types which currently qualify as exempt. This engagement suggested that existing UK legislation covers the vast majority of fund types.

1.40 As with the written consultation, the majority of stakeholders called for a definition of 'management' of funds. They particularly sought a broad definition so that a VAT exemption in this area would capture various aspects of outsourced fund management activities and ensured that any definition would reflect current and future technologies.

Chapter 4

Government response

1.41 The government is grateful for the informative consultation responses. The respondents have illustrated a range of views and suggestions for how the VAT treatment of fund management could be improved.

1.42 The government thanks those respondents who also engaged in bilateral discussions with government officials over the course of the year to set out their operating models and further explore the relationship between EU and UK legislation.

1.43 Firstly, respondents raised concerns that the principles of what constitute a SIF caused confusion and required greater clarity. It was clear there is widespread reliance by industry on Items 9 and 10, with a strong preference among respondents to continue to rely on a single model based on these items.

1.44 After fully considering the consultation responses and the outcomes of the additional stakeholder discussions, the government has established that existing UK VAT legislation covers the vast majority of fund types for which management services should be VAT exempt. The government further considers that a list-based approach of Items 9 and 10 of Group 5 Sch. 9 of the VATA provides the industry with sufficient legal certainty. This approach is in line with industry preferences following extensive engagement with stakeholders, and meets the stated aims of providing clarity, certainty, and simplicity.

1.45 The government has considered the calls for the introduction of a definition of 'management' of a fund in legislation to provide greater clarity on the application of the existing exemption, especially in regard to Items 9 and 10. The government has concluded that the current position established by settled case-law provides sufficient legal certainty.

1.46 However, the government has noted the request for greater definition in this area and will take this forward as part of the review of current guidance. This work will be focused on providing additional clarity in relation to the current legal position and will not incorporate proposals from some respondents to widen the existing definition.

1.47 Several respondents made suggestions outside the scope of this consultation. The main proposal was to zero rate fund management services to UK domiciled funds to increase UK competitiveness in terms of fund domicile. There were also calls for expanding the scope of the VAT exemption. The government recognises that some respondents will be disappointed that such proposals are not currently being taken forward, but the government keeps all taxes under review.

Annex A: List of respondents

ABRDN PLC
ASSOCIATION OF PENSION LAWYERS
ASSOCIATION OF REAL ESTATE FUNDS
AVIVA
BDO LLP
BRITISH PRIVATE EQUITY & VENTURE CAPITAL ASSOCIATION
CHARTERED INSTITUTE OF TAXATION (CIOT)
DELOITTE LLP
EVELYN PARTNERS LLP
GRANT THORTON UK LLP
INREV
INVESTMENT PROPERTY FORUM
ISLE OF MAN INSURANCE ASSOCIATION TECHNICAL COMMITTEE
ISLE OF MAN WEALTH & FUND SERVICES ASSOCIATION
LEGAL AND GENERAL GROUP PLC
LLOYD'S OF LONDON
M&G PLC
MACFARLANES LLP
MANAGED FUNDS ASSOCIATION
MAZARS LLP
MELVILLE RODRIGUES CONSULTING LLP (MRC)
OSBORNE CLARKE LLP
PHOENIX GROUP PLC

PERSONAL INVESTMENT MANAGEMENT FINANCE ASSOCIATION (PIMFA)
PWC LLP
ROYAL LONDON
RSM UK TAX AND ACCOUNTING LIMITED
SCHRODER INVESTMENT MANAGEMENT LIMITED
SIMMONS & SIMMONS LLP
THE ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION (AIMA)
THE ASSOCIATION OF BRITISH INSURERS (ABI)
THE ASSOCIATION OF INVESTMENT COMPANIES
THE CHARITY LAW ASSOCIATION (CLA)
THE INVESTMENT ASSOCIATION (IA)
THE ZURICH GROUP
THE INVESTING AND SAVING ALLIANCE (TISA)
TRAVERS SMITH
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