



Friday, 18th December 2015

European Court widens VAT exemption for fund management services

Management of Real Estate Funds is now capable of falling within the exemption – other types of fund may be affected too.

In a potentially far-reaching decision, the Court of Justice of the European Union (CJEU) decided on 9 December 2015 in the *Fiscale Eenheid* case (C-595/13) that real estate funds could fall within the definition of "special investment funds" ("SIFs") for the purposes of the VAT exemption for the management of such funds ("the VAT Exemption"). In laying down broad criteria for what constitutes a SIF, this decision could pave the way for the VAT Exemption to apply to other types of funds which are regulated as Alternative Investment Funds ("AIFs").

More detail is given below, but please give us a call if you have any questions on how this decision has the potential to impact your fund.

WHAT WAS THE POSITION BEFORE THIS JUDGMENT?



The EU's VAT Directive provides that member states shall exempt "management of SIFs" from VAT. What constitutes "management" is a matter of EU law and includes - in addition to portfolio management - administration, advice and accounting tasks. However, the definition of a SIF was left to member states.

The UK takes a narrow view of what qualifies as a SIF. Here, broadly speaking, UCITS funds, VCTs, Investment Trusts and defined contribution pension schemes are SIFs, but not other funds.

WHAT DID THE JUDGMENT SAY?

WHAT CONSTITUTES A SIF?

To qualify as a SIF, a fund must have the following characteristics:

1. capital is pooled by several investors;
2. those investors bear the risk connected with management of the assets; and
3. the fund is subject to specific state supervision.

The court noted that where there is EU-wide regulation, such as the UCITS regime, member states do not have discretion to define a SIF. It said UCITS is not the only relevant EU-wide supervisory law and highlighted AIFMD as a comparable regulation which necessarily results in specific member state supervision. It noted that Real Estate Funds can be AIFs and, by virtue of being subject to state regulation, are in direct competition with UCITS funds. The court did not explicitly say all AIFs are SIFs, because the facts of the case meant it did not need to, but the strong suggestion from the court was that where AIFs satisfy the three criteria (see inset), they will be.

What is "management" in the context of a real estate fund?

On the second question it had to answer, the court held that, while portfolio management – deciding on assets to buy and sell – would be an exempt service, the day-to-day property management (such as rent collection or maintenance) does not fall within the VAT exemption because it is not an activity specific to the management of a special investment fund.

WHAT ARE THE CONSEQUENCES OF THIS JUDGMENT FOR FUNDS?

What must the UK do?

The UK will be obliged to accept that fund management services supplied to real estate funds which satisfy the criteria for qualification as a SIF as outlined above should be exempt from VAT.



What might HMRC do?

We will have to wait and see how HMRC reacts this time but until now, HMRC has sought to keep the definition of a SIF as narrow as possible and has only changed it piecemeal following specific CJEU judgments. It may thus try to restrict the impact of this judgment to real estate investment funds which meet the criteria outlined by the CJEU. However, based on the breadth of these criteria it may be difficult to justify this: the judgment has potential ramifications for private equity funds, debt funds and infrastructure funds which are AIFs.

If the management of AIFs is brought within the VAT exemption, this could have a significant impact on current fund structures, with both VAT winners and losers.

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We will provide an updated briefing note once HMRC have reacted to this decision, but in the meantime, please get in touch if you have any questions.

FOR FURTHER INFORMATION, PLEASE CONTACT

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