

VAT recovery on Defined Benefit Pension schemes

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IDEAS | PEOPLE | TRUST

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BACKGROUND

- Management fees in relation to defined benefit pension schemes are subject to VAT at the standard rate (unlike for defined contribution pension schemes, which are usually exempt)
- DB pension schemes in the UK have to be set up as separate legal entities
- The relevant contracts with suppliers will often be between the scheme and the supplier directly, without the employer being involved
- The question arises: who is the recipient of the supply and who is entitled to claim input VAT?
  - Fully taxable employers would not want to lose out on the VAT
  - Pension scheme's own activities often do not allow for input VAT recovery

HISTORICAL POSITION

- HMRC's approach historically was to distinguish between the costs of:
  - setting up and day-to-day administration of occupational pension schemes
  - investment management relating to the assets of occupational pension schemes
- Admin costs
  - employer's overheads
  - VAT recoverable subject to having an invoice in the employer's name
  - no requirement to make payments to the supplier directly
  - recharges to the pension scheme without VAT
- Investment costs
  - pension scheme's costs
  - VAT not recoverable by the employer unless a recharge is made to the scheme
  - the recharge is subject to VAT

HISTORICAL POSITION

- If a third-party manager issued a single invoice for both admin and investment management services, the 30:70 split could apply:
  - 30% - assumed admin costs
  - 70% - assumed investment costs
- In 2013 the decision in Fiscale Eenheid PPG Holdings BV cs te Hoogezand (C-26/12) was published:
  - a taxable person who has set up a pension fund in the form of a legally and fiscally separate entity <…> in order to safeguard the pension rights of his employees and former employees, is entitled to deduct the VAT he has paid on services relating to the management and operation of that fund, provided that the existence of a direct and immediate link is apparent from all the circumstances of the transactions in question
  - No distinction between admin and investment costs

HISTORICAL POSITION

- HMRC issued a series of briefs, outlining their updated policy in light of PPG while also allowing employers to continue using the pre-PPG rules during the “transition period” (explicitly extended to 31 December 2017 and then in effect indefinitely) and reflected in the prior version of VAT Notice 700/17
  - HMRC accepted the PPG decision but interpreted it in such a way that investment costs, unlike admin, had “dual use”, i.e. related to both the activities of the employer and the pension scheme itself
  - HMRC introduced the “tripartite agreement” approach that could be used to evidence that the employer was the recipient of the services (including investment costs) - Revenue & Customs Brief 8/2015
  - HMRC also considered the VAT grouping option - Revenue & Customs Brief 17/2015

UPDATED POSITION

- 18 June 2025 - HMRC issues Revenue and Customs Brief 4/2025, confirming that it no longer views investment costs as subject to “dual use” and the employer could recover VAT subject to the normal rules. Further update was promised in autumn 2025.
- 4 June 2026 – HMRC updates its Internal Manual (VAT Input Tax)
- 9 July 2026 – HMRC updates VAT Notice 700/17 - Funded pension schemes
- September 2026 – further update to VIT45410 of the Internal Manual (VAT Input Tax)

UPDATED POSITION

VAT Notice

- Employer entitled to claim VAT on both admin and investment costs
- Required evidence – invoice in the employer's name (even if the trustee pays for the supplies)
- No VAT due on recharges to trustees if the employer pays the suppliers directly
- Silent on the contractual arrangements
- Most recently updated
- Aimed at taxpayers

Internal Manual

- Employer entitled to claim VAT on both admin and investment costs
- IF the employer contracts with the supplier directly and has an invoice in their name (including "care of")
- Invoices correctly issued to trustees should not be reissued to the employer
- Payment of the invoice can be evidenced by deduction from the pension pot
- Recharges from employer can be made without VAT if "used for the management of the pension scheme"
- Updated earlier
- Aimed at HMRC officers

UPDATED POSITION – POSSIBLE RESOLUTIONS AND CHALLENGES

- Registering the scheme for VAT and making taxable charges to the employer
  - Historical costs?
- VAT grouping the scheme and the employer
  - Joint and several liability?
  - Employers in the same corporate group but outside the VAT group?
  - Impact of the pension scheme's own supplies on the recovery position of the VAT group
- Multi-employer scheme arrangements – paymaster


Questions
and Thoughts?