

**EXPLANATORY MEMORANDUM TO  
THE VALUE ADDED TAX (FINANCE) ORDER**

**2008 No. 1892**

**1.** 1.1 This explanatory memorandum has been prepared by the Commissioners for Her Majesty's Revenue and Customs (HMRC) on behalf of HM Treasury and is laid before the House of Commons by Command of Her Majesty.

1.2 This memorandum contains information for the Select Committee on Statutory Instruments.

**2. Description**

2.1 This Order varies Group 5 of Schedule 9 (VAT exemption for certain financial supplies) to the Value Added Tax Act 1994 (c. 23) ("the Act") by redefining the categories of special investment fund whose management is exempt under that Group. The management of authorised unit trust schemes and open-ended investment companies remains exempt. Trust-based schemes have been removed from the exemption. The management of funds recognised pursuant to sections 264, 270, 272 or 409 of the Financial Services and Markets Act 2000<sup>1</sup> ("the FSMA") has been included in the exemption. The management of closed-ended collective investment undertakings which fulfil certain criteria relating to their investment object, UK Listing status and trading of their shares on a regulated market has also been included in the exemption.

**3. Matters of special interest to the Select Committee on Statutory Instruments**

The explanatory note to this Instrument explains that:

"A full and final Impact Assessment has not been produced for this instrument as a negligible impact on the private or voluntary sectors is foreseen."

This is because the accepted Government practice is that no IA will be published for HMRC and HMT tax measures for which:

- The total effect of the changes across all UK business is less than £100,000 of administrative burden costs/savings and/or £3m of compliance cost in total; and
- The Department's Better Regulation and Policy team has confirmed that
  - there are no disproportionate impacts on any business or sector; and
  - there are no other issues which might make publication of an IA advisable.

This is such a measure.

HMRC are working with BERR to ensure that the next edition of the Statutory Instrument Practice reflects these changes.

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<sup>1</sup> 2000 c. 8

## **4. Legislative Background**

4.1 Article 135(1)(g) of the Principal VAT Directive (Council Directive 2006/112 EC)<sup>2</sup>, requires member States to exempt the management of special investment funds as defined by the member State in question.

4.2 Group 5 of Schedule 9 to the Act describes the finance supplies which are exempt from VAT and exempts the management of certain categories of investment funds. Section 31(2) of the Act provides that the Treasury may by order vary the Schedule by adding, deleting or varying any description of supply for the time being specified in it. Section 96(9) of the Act provides that Schedule 9 shall be interpreted in accordance with the notes contained in the Schedule and the powers conferred by the Act to vary the Schedule include a power to add to, delete or vary those notes.

4.3 Previously, Items 9 and 10 of Group 5 as amplified by Notes (6), (8) and (10) to the Group exempted services consisting in the management of authorised unit trust schemes, trust based schemes and open-ended investment companies. Relevant amendments to these provisions have been made by SI 1997/510, S.I. 2001/3649 and S.I. 2003/1569.

4.4 The amendments set out in article 2 of this Order, which apply to supplies made on or after 1 October 2008, redefine the investment funds whose management falls within the ambit of the exemption by substituting Items 9 and 10 and Note (6) of Group 5 and omitting Notes (8) and (10).

4.5 The new Items 9 and 10 retain the management of authorised unit trust schemes and open-ended investment companies but omit trust based schemes (which are schemes where the asset consists of a single real property). The description of an open-ended investment company has been qualified by the word 'authorised' and it has been defined by reference to section 237(3) of the FSMA.

4.6 The new Items also exempt the management of five new categories of funds. The new categories are those collective investment schemes which are recognised pursuant to sections 264, 270, 272 or 409 of the and closed-ended collective investment undertakings which fulfil certain criteria relating to their investment object, UK Listing status and trading of their shares on a regulated market.

4.7 This Order has been made under the affirmative procedure. Section 97(3) of the Act requires an Order to which that subsection applies to be laid before the House of Commons and provides that unless it is approved by that House within 28 days beginning on the date on which it is made it shall cease to have effect from the expiration of that period. Section 97(4)(c)(iii) applies subsection (3) to an order which varies Schedule 9 of the Act so as to abolish the exemption of a supply without zero-rating it. This Order considerably extends the category of funds whose management is exempted but it also removes the management of one category, trust based schemes, from the exemption and for this reason the procedure specified in section 97(3) has been followed.

## **5. Territorial Extent and Application**

This instrument applies to all of the United Kingdom.

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<sup>2</sup> OJ No L 347, 11.12.06, p1

## **6. European Convention on Human Rights**

6.1 The Financial Secretary to the Treasury, Jane Kennedy, has made the following statement regarding Human Rights:

In my view the provisions of the Value Added Tax (Finance) Order 2008 are compatible with the Convention rights.

## **7. Policy background**

7.1 The changes made by the Order are a consequence of the judgment of the European Court of Justice in *JP Morgan Fleming Claverhouse Investment Trust plc and the Association of Investment Trust Companies v The Commissioners of HM Revenue and Customs*.<sup>3</sup> The Court ruled that closed-ended funds, such as investment trust companies, are capable of definition as special investment funds for the purposes of the VAT exemption in Article 135(1)(g) of the Principal VAT Directive. It also made clear that, in exercising their discretion to define special investment funds in national law, member States must pay due regard to the purpose of the exemption, which is to facilitate investment in securities by means of collective investment undertakings by excluding the cost of VAT, and to the principle of fiscal neutrality.

7.2 The changes give effect to the principles expressed in the judgment by:-

(a) defining a new category of exempt fund which is a closed-ended collective investment undertaking fulfilling criteria relating to its investment object, investments, UK Listing status and trading of its shares on a regulated market; and

(b) extending the categories of open-ended collective investment schemes covered by the exemption.

7.3 The effect of the changes is to exempt the management of all similar collective investment schemes whose units or shares are made available for investment by the general public in the UK under comparable regulatory supervision.

7.4 The definition of closed-ended collective investment undertaking covers UK investment trust companies and venture capital trusts. It also includes similar off-shore investment funds whose shares are available for investment by the UK general public under the same conditions.

7.5 Open-ended collective investment schemes established in the UK which are authorised by the Financial Services Authority to sell their units to UK investors consist of authorised unit trust schemes and authorised open-ended investment companies and are covered by the exemption. Open-ended collective investment schemes established outside the UK are also included if they are recognised by the Financial Services Authority for the purposes of selling their units or shares to investors in the UK. If a fund is an “umbrella” consisting of a number of sub-funds and each sub-fund is a separate collective investment scheme, then only those sub-funds which have been recognised

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<sup>3</sup> Case reference C-363/05.

because their units are, or have been marketed to UK investors, fall within the scope of the exemption.

7.6 Trust-based schemes, which are schemes where the asset consists of a single real property, have been deleted as a category as there are none currently authorised to market their units and they do not sit with the principles expressed in the JP Morgan judgment.

## **8. Impact**

A full and final Impact Assessment has not been produced for this instrument as a negligible impact on the private or voluntary sectors is foreseen.

## **9. Contact**

Ted Castledine at HM Revenue and Customs Tel: 0207 147 0177 or e-mail: [ted.castledine@hmrc.gsi.gov.uk](mailto:ted.castledine@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.