

VAT's up

CJEU hearing on the management
of real estate funds

March 2015



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On March 4, 2015, the hearing on the VAT group X case was held at the Court of Justice of the European Union. This case concerns the VAT treatment of the management of real estate funds, but is also relevant for other investment funds. It is, for example, interesting that the European Commission considers that the exemption for the management of special investment funds must be broadly interpreted.

The case

The taxpayer concluded management agreements with three companies that invest in real estate. The taxpayer's activities consist of the administration and management of the companies, attracting investors, sales and purchases of real estate (fund and asset management) and the exploitation of the real estate (property management).

Pursuant to VAT legislation, the management of special investment funds is exempt from VAT. The Supreme Court requested a preliminary ruling from the Court of Justice of the European Union ("CJEU") on whether investment companies that invest in real estate qualify as a special investment fund. The Supreme Court also wanted to know whether the actual exploitation of the real estate is covered by the term 'management' within the meaning of the abovementioned exemption.

Position of the VAT group

With regard to whether this involves a special investment fund, the taxpayer elaborated on the three conditions from the CJEU's ATP case. According to the taxpayer, the investment fund is (i) financed by its participants, (ii) the risk is spread and (iii) the risk is borne by the participants.

The taxpayer argued that risk is spread because different categories of real estate (e.g. residential and commercial real estate) are invested in, and there is a geographical spread as well.

The taxpayer further believes that the actual exploitation of the real estate is specific and essential to investment in real estate. In this respect, the taxpayer noted that it follows from CJEU case law that the management does not necessarily have to result in legal or financial changes. The taxpayer therefore considered that the actual exploitation of real estate qualifies as 'management' within the meaning of the exemption.

Position of the Netherlands

We find it surprising that the Dutch Ministry of Finance indicated that it has no preference for a narrow or a broad interpretation of the term 'special investment fund'. With respect to the term 'management', the Netherlands advocates a strict interpretation, with the actual exploitation of real estate not qualifying as management within the meaning of the exemption.

Position of the European Commission

The European Commission answered the two questions raised by the Supreme Court in the affirmative. It also addressed the interpretation of the term 'management'. The Member States already have some discretion in determining the scope of the term 'special investment fund'. During the hearing, the European Commission stated that in its opinion the Member States have this freedom with regard to the term 'management' as well.

Position of the United Kingdom

According to the United Kingdom, investment funds must invest at least 90% in financial assets in order to qualify as a special investment fund. In this respect, the United Kingdom referred to the UCITS (Undertakings for Collective Investment in Transferable Securities) Directive. This Directive has previously been addressed in CJEU case law on the management of special investment funds. According to the United Kingdom, investing in real estate is not comparable with investing in securities and other financial assets, so that a real estate fund should not be regarded as a special investment fund. The United Kingdom also believes that the risk spreading condition is not satisfied because investments are only made in the real estate sector.

Position Sweden

Sweden currently does not include investment funds that invest in real estate under the term 'special investment fund'. Sweden considers that a narrow interpretation should be given to the exemption and that only the management of investment funds that invest in securities or similar products can be included under the exemption. In addition, Sweden wonders, like the United Kingdom, whether risk is indeed spread if investments are only made in real estate.

Other comments

The United Kingdom and Sweden, which both advocate a narrow interpretation of the term 'special investment fund', also addressed the purpose of the exemption for the management of special investment funds. In a number of previous judgments by the CJEU it was pointed out that the purpose is to make investment more attractive for small investors. However, other judgments refer to investors in a general sense. The aforementioned countries distinguish between institutional investors (no exemption) and 'retail investors' (exemption applicable). In response, the taxpayer argued that in the CJEU's recent ATP case (concerning the qualification of a pension fund as a special investment fund), the term 'small investor' is no longer mentioned.

The CJEU made a number of comparisons during the hearing. With regard to the term 'special investment fund', the United Kingdom was asked whether an investment fund that invests in wine instead of real estate may indeed fall under the exemption. The United Kingdom answered this question negatively as it believed that financial assets should be involved.

With regard to the term 'management', the European Commission was asked about investment in the shares of a listed company. The Court wanted clarification about the management at different levels (i.e. the management of an investment fund and the management of a business in which is invested). The European Commission seemed to have some difficulty with this question, but replied that in this case the management of the real estate was part of the activities of the investment fund itself.

The Opinion of Advocate General Kokott in this case will be published on May 20, 2015.

Impact

There are several reasons why this case is relevant to the real estate funds practice. In Denmark the practice is not clarified. We expect this case to shed light on the interpretation of the VAT exemption in regard to real estate funds. The question as to which activities fall within the scope of the term 'management' also needs to be answered. If the term 'management' also covers property management of real estate funds, then it could be the case that more activities would fall under the exemption.

The tax advisors of the Indirect Tax Financial Services of KPMG Acor Tax would be pleased to help you identify any consequences these proceedings may have. They can also advise you on how to deal with and anticipate amendments to VAT legislation, policy and case law, as they have extensive experience in these matters. Feel free to contact one of these tax advisors or your regular contact for more information.

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