C-231/19 - 1

IN THE UPPER TRIBUNAL **UT/2017/0163**

(TAX AND CHANCERY CHAMBER)

ON APPEAL FROM THE FIRST-TIER TRIBUNAL

(TAX CHAMBER)

BEFORE: MRS JUSTICE FALK

And JUDGE ROGER BERNER

BETWEEN

BLACKROCK INVESTMENT MANAGEMENT (UK) LIMITED

Appellant

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS

Respondents

ORDER

UPON the Appellant and the Respondents providing an agreed draft form of Order and Preliminary Reference in accordance with paragraph 5 of the directions of the Upper Tribunal dated 20 December 2018

IT IS DIRECTED THAT:

1. The question set out in the Schedule attached hereto shall be referred forthwith to the Court of Justice of the European Union for a preliminary ruling in accordance with Article 267 of the Treaty on the Functioning of the European Union.

2. All further proceedings in the matter be stayed until the said Court of Justice has given its ruling on the question or until further order.

SCHEDULE

REQUEST FOR PRELIMINARY RULING OF THE COURT OF JUSTICE OF THE EUROPEAN UNION

A. INTRODUCTION

1. In and by this reference, the Upper Tribunal (Tax and Chancery Chamber) (the "**Tribunal**") refers to the Court of Justice of the European Union ("**CJEU**") a question concerning the application of Article 135.1(g) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ 2006 L 347, p. 1) ("**the VAT Directive**"). Article 135.1(g) exempts supplies of the management of special investment funds ("**SIFs**") from value added tax ("**VAT**") ("**the Fund Management Exemption**").

2. The Appellant ("**BlackRock**") is the representative member of a VAT group that includes a number of companies which carry on business as fund managers. The Respondents are the Commissioners for Her Majesty's Revenue and Customs ("**the Commissioners**"), the national taxation authority for VAT purposes in the United Kingdom.

3. BlackRock receives supplies of services from BlackRock Financial Management Inc ("**BFMI**"), a US company in the same commercial group. BlackRock uses those services to manage both SIFs and other investment funds ("**non-SIFs**"). It is common ground that the supply is a single supply of services received by BlackRock from BFMI.

4. The broad issue before the referring Tribunal is whether and to what extent BlackRock needs to account for VAT under the reverse charge mechanism on the supply of those services. That issue depends upon the interpretation and application of the Fund Management Exemption.

5. The Tribunal (and, at first instance, the First-tier Tribunal) have concluded that the services received are supplies of "management" in accordance with the meaning of that term in Article 135.1(g) ("**the Management Services**").
6. The question referred to the CJEU, set out fully in Section G below, is whether, for the purposes of Article 135(1)(g), the consideration paid by BlackRock for the Management Services should be apportioned so as to reflect the extent to which those services are used to manage SIFs and non-SIFs respectively. If the consideration is to be apportioned, the Management Services would be exempt *to the extent* that they are used in the management of SIFs. If, however, such apportionment is not permissible, guidance is required from the CJEU as to the basis upon which the availability (or non-availability) of the Fund Management Exemption in the present circumstances is to be determined.

B. FACTUAL BACKGROUND

7. The following are established facts:

    a. Within BlackRock, the individuals responsible for managing the funds are the portfolio managers. Investment management follows a cycle of analysis, decision making, trade execution and post-trade settlement and reconciliation.
    b. The Management Services are provided through a software platform known as Aladdin and comprise a combination of hardware, software and human input.
    c. Aladdin's functions span the whole of the investment cycle. In general terms, Aladdin provides the portfolio managers with performance and risk analysis and monitoring to assist in the making of investment decisions, monitors regulatory compliance and enables the portfolio managers to implement trading decisions.
    d. BlackRock manages a range of different funds, some of which qualify as SIFs and some of which are non-SIFs.
    e. BlackRock uses the Management Services to manage both SIFs and non-SIFs.
    f. The majority of the funds currently managed by BlackRock using the Management Services are non-SIFs, both in terms of number of funds and the value of the assets under management.
    g. The Management Services are also supplied by BFMI to other (third-party) fund managers, some of which manage mainly SIFs.

C. RELEVANT UNION LAW

8. Article 131 of the VAT Directive provides:

> *"The exemptions provided for in Chapters 2 to 9 shall apply without prejudice to other Community provisions and in accordance with conditions which the Member States shall lay down for the purposes of ensuring the correct and straightforward application of those exemptions and of preventing any possible evasion, avoidance or abuse."*

9. Article 135.1 of the VAT Directive provides, so far as relevant:

> *"1. Member States shall exempt the following transactions:*
>
> ...
>
> *(g) the management of special investment funds as defined by Member States..."*

D. RELEVANT NATIONAL LAW

10. Section 31(1) of the Value Added Tax Act 1994 ("**VATA**") provides, so far as relevant:

> *"(1) A supply of goods or services is an exempt supply if it is of a description for the time being specified in Schedule 9..."*

11. Schedule 9 VATA includes, at Item 9 of Group 5, "the management of" a list of specified investment entities and types of funds. Those are the entities and types of funds which the United Kingdom considers to be special investment funds.

E. POSITIONS OF THE PARTIES

(1) The position of BlackRock is as follows:

12. Whether apportionment is possible depends upon the proper construction of Article 135.1(g) of the VAT Directive.

13. It is settled law that the exemptions in the VAT Directive are to be interpreted strictly, but not in such a way as to deprive the exemptions of their intended effect: Case C-91/12 *Skatteverket v PFC Clinic AB* ECLI:EU:C:2013:198 at paragraph 23.

14. In construing Article 135.1(g), the relevant provision is to be interpreted "*having particular regard to the underlying purpose of the exemption which it establishes*": Case C-169/04 *Abbey National plc v Customs & Excise Commissioners* ECLI:EU:C:2006:289 at paragraph 59 ("***Abbey National***").

15. The CJEU has already provided detailed guidance on the *purpose* of the Fund Management Exemption:
    a. SIFs are collective investment schemes which are suitable for investment by small investors. The purpose of the Fund Management Exemption is to facilitate investment for small investors and to ensure that the system of VAT is fiscally neutral as between direct investment in securities and investment through collective undertakings: *Abbey National* at paragraph 62.
    b. It follows from the principle of fiscal neutrality that operators must be able to choose the form of organisation which, from the strictly commercial point of view, best suits them, without running the risk of having their transactions excluded from the Fund Management Exemption: *Abbey National* at paragraph 68 and Case C-275/11 *GfBk Gesellschaft für Börsenkommunikation mbH v Finanzamt Bayreuth* ECLI:EU:C:2013:141 at paragraph 31.
    c. The Fund Management Exemption is defined according to the nature of the services provided and not according to the person supplying or receiving the services: *Abbey National* at paragraph 66.

16. It is only through apportionment that the purpose of the Fund Management Exemption can be achieved.

17. Without apportionment, the purpose of the exemption is frustrated for the following reasons:
    a. Availability of the exemption is arbitrary, determined according to the mix of funds managed by the recipient of the services. The Management Services are excluded from exemption simply because the recipients of those services are

organised to manage both SIFs and non-SIFs, despite the CJEU having expressly recognised that the structure of an organisation should not have this result (see paragraph 15(b) above).

b. The exemption is restricted by reference to the person receiving the services, rather than the use to which the services are put, this results in a distortion of competition. Again, the CJEU has expressly rejected attempts to restrict the exemption in this way (see paragraph 15(c) above).

c. Capricious results will follow for other fund managers and investors. For example, a single supply of services might change repeatedly from exempt to standard-rated (and vice versa) as the volume and value of the SIFs and non-SIFs managed by the recipient of those services fluctuate. Furthermore, fund managers could manipulate their corporate and organisational structures in order to allow non-SIFs to obtain the benefit of the exemption, by managing some non-SIFs under the same entity as SIFs.

18. Moreover, apportionment by reference to use is not a novel concept within the VAT Directive. Indeed, the CJEU has already recognised that apportionment may be required to give effect to the cost-sharing exemption in Article 132.1(f): Case C-274/15 *EC v Grand Duchy of Luxembourg* ECLI:EU:C:2017:333 ("***Luxembourg***").

19. The cost-sharing exemption in Article 132.1(f) depends upon the services supplied by an independent group of persons (an "**IGP**") to its members being "directly necessary" for an activity carried on by the member which is not an economic activity, or for supplies made by it which are exempt from VAT. In circumstances where a member receives a supply of services from the IGP which are used by it for the purposes of both an economic and a non-economic activity carried on by it, or in order to make both taxable as well as exempt supplies (such as expenditure on overhead costs), the CJEU has suggested that the consideration paid by the member to the IGP should be apportioned, with the exemption applying in a manner which reflects the extent to which the services supplied to the member are "directly necessary" for the non-taxable activity carried on by it: *Luxembourg* at paragraphs 53 and 54.

20. Finally, it will be noted that this is not a case of carving out one element of a composite supply and applying a different rate to that element. It is accepted that to do so would

(generally) fail to reflect commercial reality, and thereby frustrate the proper functioning of the VAT system: C-463/16 *Stadion Amsterdam v Staatssecretaris van Financiën* ECLI:EU:C:2018:22 at paragraph 22. In the present case, apportionment both reflects commercial reality and promotes a commercially realistic division of labour and resources.

(2) The position of the Commissioners

21. A single composite supply, which is predominantly used for the taxable management of non-SIFs, cannot be apportioned. Rather, it is wholly taxable.

22. The general rule is that a single rate of tax should be applied to a single composite supply. The only exceptions to that rule are found in cases where there is clear authority in EU legislation for a different treatment - see Case C-251/05 *Talacre Beach,* which concerned a zero-rate, and Case C-94/09 *Commission v. France,* which concerned the conditions under which a Member State could apply a reduced rate to particular activities.

23. To allow an apportionment where a single supply is used for two purposes would be contrary to the Court of Justice's previous caselaw. In Case C-463/16 *Stadion Amsterdam,* the Court recently confirmed that a single supply, consisting of two distinct elements, must be taxed solely at the rate of VAT applicable to that single supply, which is determined according to the VAT liability of the principal element. That is so, even if one of the two elements would have been subject to a reduced rate of VAT if it had been supplied separately.

24. To allow an apportionment where a single supply is used for two purposes would also be contrary to the aim of the case law on composite supplies. Two elements are only to be regarded as a single supply if that is the case from an economic point of view and splitting the elements would be artificial. It makes no sense to find that there is a single supply economically, but nevertheless to split the consideration by applying an apportionment. This would risk distorting the functioning of the VAT system.

25. Furthermore, to allow an apportionment in the present circumstances would give rise to practical problems. If the apportionment was based on the assets under management of the funds managed by BlackRock, then the liability for the supply would vary continuously depending on the value of SIF and non-SIF funds which it manages.

26. The UK tax authorities' analysis is not altered by the principle of fiscal neutrality, which is a principle of interpretation which cannot override the general rule of VAT law that a single supply has a single VAT treatment. Indeed, in every case involving a single composite supply, the application of the VAT treatment of the principal element to the whole supply leads to a different VAT treatment for the ancillary element than if that element had been supplied separately. But that is nevertheless the effect of the doctrine of single composite supplies – see Case C-117/11 *Purple Parking/Airparks*.

27. Nor is the UK tax authorities' analysis altered by the Court of Justice's judgment in Case C-274/15 *Commission v. Luxembourg*. That case was an infraction proceeding concerning the exemption for cost sharing groups in Article 132(1)(f) PVD, rather than a reference concerning the particular facts of a case before the national courts. The Court does not state anywhere in its judgment in that case that it was dealing with a single supply by a cost sharing group, or that it was suggesting that the consideration for that single supply was to be apportioned on the basis of use.

F. REASONS FOR THE REFERENCE

28. Attached at **Annexes 1 and 2** of this Request are the respective decisions of the referring Tribunal (the Upper Tribunal) dated 20 December 2018 and the First-tier Tribunal dated 15 August 2017.

29. The referring Tribunal observes that, while it is a general principle that a single composite supply should be taxed at a single rate, that principle is not of itself determinative in this case. The issue that arises is not whether different rates can be applied to separate elements of a single composite supply. Instead the issue is the construction of Article 135.1(g) itself: whether it is to be properly construed so as to require apportionment of the consideration for the single supply on the basis of use.

30. In *Luxembourg,* the CJEU appears to have indicated that in applying Article 132.1(f) of the VAT Directive, it may be appropriate to apportion a single supply of services into exempt and taxable elements. If apportionment based on use has been accepted by the CJEU in order to determine the scope of one exemption, it must be open to argument that such an apportionment would be capable of applying to other exemptions, especially those which depend on the use to which the particular supply of services is put.

31. However, *Luxembourg* does not provide any clear signposts in this case. The views expressed by the CJEU on apportionment in relation to the cost-sharing exemption appear to be based on practicality and not on principle or purpose.

32. In summary, the referring Tribunal concluded that it is arguable that Article 135.1(g), properly construed, permits an apportionment of the consideration for a single supply of management services as between the use of those services for the management of SIFs and non-SIFs respectively. However, it is equally arguable that such an apportionment cannot apply, and that the single supply should be taxed according to its predominant or principal use.

33. The referring Tribunal accordingly considers that, in circumstances where services are used to manage both SIFs and non-SIFs, the correct approach to the interpretation of Article 135.1(g) cannot be determined by it with complete confidence and is not *acte clair*, and that resolving that question of interpretation is necessary to determine the dispute in the proceedings.

G. QUESTION REFERRED

34. The referring Tribunal accordingly seeks a preliminary ruling from the CJEU on the following question:

> On the proper interpretation of Article 135.1(g) of Council Directive 2006/112/EC, where a single supply of management services within the meaning of that Article is made by a third-party provider to a fund manager and is used by that fund manager both in the management of special investment

finds ("SIFs") and in the management of other funds that are not special investment funds ("non-SIFs"):

(a) Is that single supply to be subject to a single rate of tax? If so, how is that single rate to be determined? or

(b) Is the consideration for that single supply to be apportioned in accordance with the use of the management services (for example, by reference to the amounts of the funds under management in the SIFs and non-SIFs respectively) so as to treat part of the single supply as exempt and part as taxable?

Sarah Falk

Mrs Justice Falk

J M Richards

Judge Jonathan Richards

Dated 15 March 2019