

Remarkable Opinion by Advocate General to the CJEU in VAT pension fund cases

On March 14, 2024 the Opinion issued by Advocate General to the Court of Justice of the European Union ('CJEU'), Ms. J. Kokott, in the pension fund cases was published. She addressed the request for a preliminary ruling submitted by the Gelderland District Court regarding whether management services provided to Dutch pension funds are VAT-exempt. For this to be the case, the pension funds must qualify as 'special investment funds'. The Advocate General believes that Dutch pension funds are not sufficiently comparable to a UCITS for them to be regarded as a special investment fund. Unfortunately, her Opinion raises a lot of questions. The Opinion is discussed in more detail below.

1. Comparability with a UCITS

The first question is whether Dutch pension funds can be regarded as a special investment fund. To determine this, a comparison with a UCITS (Undertaking for Collective Investment in Transferable Securities) has to be made: funds that display identical characteristics as a UCITS or are at least sufficiently comparable for them to be in competition with a UCITS, are also regarded as a 'special investment fund'. The Advocate General found that the characteristics constituting the basis for this comparison do not clearly follow from CJEU case law. According to her, there are five specific characteristics to the comparability test. She – rightly – concludes that two of those five characteristics, i.e., investment on the principle of risk-spreading and specific State supervision, are not disputed by the parties. She therefore does not address these further.

According to the Advocate General, the remaining three characteristics are that:

1. the capital must be raised from the public;
2. there must be a redemption or repurchase obligation; and
3. the unit-holders must bear the investment risk.

The Advocate General concluded that the Dutch pension funds do not display the first two characteristics. According to her, the pension funds involved here are only open to a limited public, i.e., the employees in the relevant sector, occupational group or undertaking. Moreover, participation in the pension plan is mandatory, which she believes precludes competition. The Advocate General does not consider the redemption or repurchase obligation that is characteristic of a UCITS, to be sufficiently present to a comparable extent at pension funds, because redemption is only possible in exceptional cases. In our view, these two characteristics are new to the comparability test. The question is not only whether these are relevant characteristics in the comparability test, but also how this relates to previous decisions by the CJEU, such as in the ATP case (C-464/12), where a Danish pension fund was regarded as a special investment fund. Moreover, this concerns 'comparability' with a UCITS, while the test applied by the Advocate General is rather about 'being the same as' a UCITS.

The final characteristic of a UCITS is that unit-holders bear the investment risk. This is the main issue at stake for qualifying pension funds as a special investment fund. It is also the essence of the requests for a preliminary ruling submitted by the Gelderland District Court. According to the Advocate General, it must be examined whether there

is a guaranteed pension commitment that primarily depends on the length of service and of the amount of the salary. The fact that the pension benefit or entitlement also depends indirectly, to a limited extent, on the investment returns, is not sufficient to conclude that there is a comparable investment risk. On the other hand, if the commitment is first and foremost dependent on the performance of the invested capital, then the participants do bear a sufficiently comparable investment risk. The character of the commitment must be established based on the retirement pension contract: is there firstly a guaranteed pension *commitment* or is the pension *commitment* dependent on the fluctuations in the return?

It is in our view remarkable that Advocate General's focus is on the contractual terms and conditions of the underlying retirement pension contract. She considers the actual financial situation of a pension fund, and thus the actual pension benefits, irrelevant. This means that she disregarded what parties put forward about the uncertainty of the benefit for participants in the pension funds. After all, there is no actual guarantee in the plans of the pension funds involved, but rather a targeted pension benefit, whereby the participants in the pension funds run the investment risk.

2. Comparability with Dutch pension funds with a DC plan (tax neutrality)

The second question of the request for a preliminary ruling is whether the pension funds in these proceedings are comparable with Dutch pension funds that execute an individual defined contribution plan ('DC'). Under guidance of the Dutch Ministry of Finance, these pension funds are regarded as a special investment fund. It is clear that these are not a UCITS. However, the Advocate General believes that Member States may extend the VAT exemption to such pension funds. If there is comparability between the pension funds in these proceedings and Dutch DC pension funds, then the Netherlands must treat the pension funds in these proceedings the same based on the principle of tax neutrality. This test must be performed by the referring court. Nevertheless, the Advocate General presented her views on this comparability:

1. Confusion about Dutch pension system: the Advocate General wrongly assumes that the individual DC plans belong to the third pillar in the Dutch pension system, for which participation is voluntary. That's why she has doubts as to comparability. However, Dutch DC plans are not aimed at supplementing other pension benefits on a voluntary basis, but simply belong in the second pillar, just as the pension funds in these proceedings. In that respect, we also refer to the facts in the Danish ATP case of the CJEU. That case also concerned company pension plans in the second pillar, whereby employers, in principle, pay the pension contributions to a pension fund on behalf of their employees.
2. Guarantee: the second characteristic where the Advocate General does not see sufficient comparability with DC plans is that the participants in the pension funds in these proceedings run a different investment risk. The reason why she argues this, is because she assumes that the pension commitments are guaranteed pension commitments. The question is whether the Advocate General's assumption is correct. In its order for reference, the District Court established that the pension amount is in no way fixed. Therefore, there is no

guarantee. The pension funds noted that this concerns targeted pension benefits, where the participants run the investment risk. This was also clearly raised during the hearing before the CJEU on October 5, 2023.

3. Next steps

This case is critical for Dutch pension funds and service providers. It appears that the Advocate General has stipulated new conditions for being regarded as a special investment fund. She makes a near one-to-one comparison with a UCITS. The question is whether this is not an overly strict test that is moreover not in accordance with previous case law, in particular the CJEU judgment in the ATP case. The cautious conclusion by the Advocate General is that the investment risk that participants in pension plans bear is not comparable to the investment risk born by unit-holders in a UCITS. As stated above, the Advocate General wrongly assessed the investment risk on the basis of commitments in the pension contract, without including the uncertainty of the benefits in her considerations. Ultimately, the Advocate General has left much to the referring court (Gelderland District Court) to definitively decide on in this matter. On a number of points, the Advocate General also seems to have used incorrect facts and an incorrect understanding of the Dutch pension system.

It is now up to the CJEU to render a final judgment. We hope that the CJEU, in performing the comparability test, includes the uncertainty pension participants face about their pension benefits, and rules that the participants bear the (collective) investment risk. After that, it's the turn of the Gelderland District Court.

As far as we are concerned, the Advocate General's Opinion must be understood in the specific context of Dutch pension funds. If the CJEU follows the Advocate General, the judgment might however also become important for interpreting the concept of 'special investment fund' outside the pension sector.

The advisors of the Financial Services Indirect Tax Group of KPMG Meijburg & Co would be pleased to help you with any questions or comments you may have. Feel free to contact one of them or your regular advisor.

KPMG Meijburg & Co
March 15, 2024

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