

Court of Justice of the European Union: pension funds possibly special investment funds

On September 5, 2024 the Court of Justice of the European Union (hereinafter: CJEU) rendered judgment in six cases concerning the question whether Dutch pension funds with a benefit scheme can qualify as 'special investment funds'. In that case, the management of these pension funds is exempt from VAT. The CJEU ruled that a pension fund is regarded as a special investment fund if the amount in pension rights and benefits primarily depends on the results of the investments of the pension funds. It is now up to the Dutch courts/Tribunals of Fact to determine whether this is the case. We believe there are good arguments for this.

The CJEU moreover ruled that, even if a certain pension fund does not meet this criterion, the fund must be regarded as a special investment fund if the legal and financial position of a unit-holder in that fund is comparable to that of the unit-holders in pension funds with a defined contribution plan. After all, the Netherlands already regards the latter as special investment funds.

The problem at the heart of the matter

Pension funds incur significant costs for purchasing fund management services. The Dutch tax authorities currently take the position that VAT is payable on this if there is a pension fund with a benefit scheme. The pension funds cannot fully recover that VAT, which means that this VAT increases the costs. The question that was asked in the proceedings was whether the pension funds must be regarded as special investment funds. In that case, the management is exempt from VAT.

In previous case law, the CJEU had formulated the criterion that the funds must be comparable with an undertaking for collective investment in transferable securities (UCITS) for this purpose. This requires, among other things, that the unit-holders bear a *comparable investment risk*. The Dutch tax authorities believe that this is not the case, because in benefit schemes the amount of the pension rights and benefits is not (only) calculated on the basis of the investment results, but in another way (often on the basis of employment income and length of service). The pension funds involved in the proceedings argue that the investment results of the pension fund ultimately determine the amount of the benefit payments. The proceedings thus mainly concerned the question how to determine whether there is a comparable investment risk. The Gelderland District Court asked the CJEU for a preliminary ruling on that question.

CJEU judgment

Comparable investment risk

The CJEU ruled that there is an investment risk comparable to that run by a UCITS if the pension rights and benefits primarily depend on the results of the investments of that fund. This is the case if the investment results have a significant impact on that amount and that amount is not largely determined in advance on the basis of other criteria (for example length of service and salary).

The CJEU has left the final decision on this to the Dutch courts. After all, they decide on the facts. The CJEU has however anticipated the answer by indicating that it seems to follow from the elements put forward by the District Court that the pension benefits

are mainly determined in advance, although it is not certain about this. The CJEU named several elements that could alter that conclusion:

- If all the features of a specific pension agreement show that the investment result constitutes the most important factor for the amount of the pension rights and benefits, then there is a comparable investment risk.
- If it is only the unit-holders who collectively (or individually) bear the risks of the investments of the pension fund, excluding, for example, the employers involved, and the results of those investments have more than a marginal impact on the amount of the pension rights and benefits, then there appears to be a comparable investment risk.
- Even if an employer partly acts as guarantor for the accrual of the pension rights, there can still be a comparable investment risk, depending on the impact that continues to be exerted on the investment results. Only if an employer fully acts as guarantor is this no longer the case (after all, there is then no investment risk for the unit-holders).

Advocate General's Opinion on other elements of comparability were not adopted

Advocate General Kokott had previously issued her Opinion in the same cases (see our [Tax Alert](#) about this dated March 15, 2024). She believed that elements other than the investment risk meant that pension funds were not comparable with a UCITS. Of particular relevance would be that pension funds are not open to the public and that commutation by unit-holders is only possible in exceptional cases. The CJEU did not address these elements, but we believe it implied that they are not part of the comparability test. After all, the CJEU noted that it is specifically about comparability with regard to the pooling of investments of multiple unit-holders in a fund.

This is important for other (pension)funds that are currently already regarded as special investment funds in the Netherlands. This qualification seemed to be open to question, but as far as we are concerned this is no longer an issue after the judgment of the CJEU.

This means, moreover, that under the new system of the Future Pensions Act (FPA) pension funds will be comparable with a UCITS and that the management of the pension funds can then take place exempt from VAT (as already confirmed in the parliamentary records on the FPA).

Comparability with pension funds with a defined contribution plan

In the Netherlands it has been confirmed that pension funds with a defined contribution plan (the DC pension funds) are currently already regarded as special investment funds. The CJEU therefore ruled that pension funds with a benefit scheme must not only be compared with a UCITS, but also with these other Dutch pension funds with a defined contribution plan. If the legal and financial situation of a unit-holder of a pension fund with a benefit scheme is comparable with that of a unit-holder of a pension fund with a defined contribution plan, then such a fund must be regarded as a special investment fund, even if the investment risk would not be comparable with that of a UCITS.

Our views and next steps

KPMG Meijburg & Co is, as authorized representative, involved in several pension cases pending before the courts, including two of the cases discussed above. Based on our experience, we believe that it will be possible for many pension funds to substantiate with convincing arguments that the pension rights and benefits primarily depend on the investment results.

The Dutch courts are now faced with the task of conducting a careful assessment in which all the characteristics of an individual pension fund are taken into account. It is no longer a question of *equating* the investment risk with that of a UCITS (such as the Dutch Supreme Court had previously wrongly applied as a test), but of an economic and legal determination about the extent to which investment results impact the amount of the pension rights and benefits.

Furthermore, we believe that in the Dutch pension landscape good arguments can be put forward that unit-holders of defined contribution plans and benefit schemes are in a comparable legal and financial situation. Also in that case the pension funds must be regarded as special investment funds.

Because there are currently many cases pending before the courts, it remains to be seen how long it will take before there is clarity. The referring court, the Gelderland District Court, will deal further with and rule on the cases for which the CJEU has rendered a preliminary judgment. The judgments by the Gelderland District Court can then still be appealed. We expect that the Dutch Supreme Court will also come to a decision on the meaning of the CJEU judgment in the other cases pending before it.

Many pension funds and their service providers have in the meantime filed notices of objection against the VAT on the management of the funds. In anticipation of the judgments by the Dutch courts, we believe that these notices of objection must be upheld in order to safeguard rights. We believe it would be a good idea for pension funds that have still not filed a notice of objection to do so as a result of this judgment. Furthermore, it is also important that all the parties involved ensure that they retain their records, so that it will be possible to determine the VAT positions for the past should it appear that the VAT exemption can indeed be applied.

Partly because of our involvement with the current cases, we have the right expertise and experience to help pension funds and their service providers. You can contact your designated advisor for this or one of the advisors on the list accompanying this Tax Alert.

KPMG Meijburg & Co
September 5, 2024

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