

Input VAT newsletter

Decision of the Court of Justice of the European Union on the Blackrock case

3 July 2020

A service used for both funds eligible to receive VAT exempt management services and other funds is not specific to the fund management activity and, therefore, could not be VAT exempt as fund management services.

On 2 July 2020, the Court of Justice of the European Union (CJEU) delivered its ruling on the *Blackrock Investment Management UK Ltd (C-231/19)* case. The Court ruled that a single supply of management services—provided by a software platform for a fund management company that manages both special investment funds eligible for VAT exempt fund management services and other funds—does not fall within the fund VAT exemption.

Indeed, the Court considers that such a service is not “specific” to the exempt fund management activity, because it could be used by both eligible and non-eligible funds. This implies that, even if most of the funds benefitting from these services are eligible ones, the exemption would not apply.

With this narrow interpretation of the service specificity criterion, the approach of the Court seems rather restrictive and may affect other outsourced or delegated services. Concerned businesses should explore the potential impact of this case and review the contractual arrangements of services they render and receive.

Background

Blackrock Investment Management UK Ltd (Blackrock UK) manages a number of investment funds. Some of the funds qualify under UK law for the exemption provided by Article 135 (1) (g) of the EU VAT Directive for the “management of special investment funds” (Article 44.1.d of the Luxembourg VAT law). Blackrock UK also manages funds that are not eligible for the exemption. The portion of services rendered to non-eligible funds exceeds the services to eligible funds.

Blackrock Financial Management Inc. (BFMI), which is based in the US, provides Blackrock UK with so-called “Aladdin” services. Aladdin is a sophisticated and automated software application that assists asset managers in their entire cycle of activities. Therefore, we could regard Aladdin as “artificial intelligence”.

Blackrock UK uses Aladdin to render services to two fund categories, i.e., those eligible to receive VAT exempt services and non-eligible ones. The question is whether Blackrock UK should self-assess the VAT on these services, or only on the Aladdin services used to render services to funds that are not eligible for the fund VAT exemption.

The UK First Tier Tribunal in 2017 and the UK Upper Tribunal both decided that Aladdin services could, in principle, be VAT exempt under “management of special investment funds”. However, they considered Aladdin to be a single supply used for the management of funds that are both eligible and non-eligible for the VAT exemption. Therefore, this single service could not benefit from the VAT exemption.

In December 2018, the Upper Tribunal referred questions to the CJEU whether it is possible to allocate the charges for Aladdin, treated as a single supply, between eligible funds (exempt) and other funds (taxable).

Decision of the Court

The Court began its reasoning by stating that, based on the wording of the question referred, the Aladdin services must be understood as being a single supply and that a single supply should not be artificially split.

The Court emphasized that the fund management exemption is defined exclusively regarding the nature of the supply in question; in the present case, this supply is operations for the management of special investment funds. Therefore, the Court considers that such a single supply must be subject to a single tax treatment.

The Court also refused the argument that the Aladdin services for BlackRock UK should be taxed because the majority are used for the management of non-eligible funds because, following the same logic, if most of the funds managed are eligible, all of these supplies should be VAT exempt and that this could lead to an extension of the non-eligible fund exemption.

After the Court’s development on the single-service concept, it recalled that, in order to be VAT exempt, “(...) *the services provided by a third-party manager must, viewed broadly, form a distinct whole fulfilling in effect the specific, essential functions of the management of special investment funds* (...).

The Court denied that the Aladdin services could be seen as specific because they can be used in the same way for the management of eligible investment funds and other funds; therefore, that service cannot be regarded as specific for the management of special investment funds. Consequently, a supply of services similar to the one in the main proceedings does not meet the conditions to benefit from the exemption provided for in Article 135(1) (g) of the VAT Directive (Article 44.1.d of the Luxembourg VAT law).

Comments

The decision could be considered as a step back of the Court, as it refuses its Advocate General’s suggestion that the exemption could possibly apply to the services that are used for funds eligible for the VAT exemption if sufficient data is provided.

The Court’s strong focus on the service specificity criterion may affect any services that are not exclusively used for eligible funds. Therefore, the impact of the case may be broad, but may also depend on the different national VAT authorities’ attitudes and the precise nature of the services and contractual arrangements.

It is also worth noting that the Court has not examined *per se* if the exemption could be applied to a specialist software or “artificial intelligence” type of service. It will have the opportunity to do so in the case DBKAG (C-59/20) to be decided probably next year¹. Concerned businesses should review if the Court’s decision may affect them and to review the contractual arrangements of services they render and receive when those services are used or could be used by non-eligible funds..

¹ In the same period, the Court will also have to rule the Finanzamt N (K) (C-58/20) case regarding the possibility of applying the VAT exemption to services provided by a third party to assist the management company of a fund in its statutory duty to provide information to unit-holders to allow them to comply with their tax obligations.

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