

“VAT on IFA services”

11th September 2014



AW Financial Management LLP

Financial Planning
Independent Financial Advice
Investment & Wealth Management

River House, 1 Maidstone Road, Sidcup, Kent, DA14 5RH
Tel: 01322 669 059 www.awfm.co.uk

HMRC attempted to clarify their position on Financial Services and VAT in the run up to the start of the FSA's Retail Distribution Review (RDR), which became effective on 1st January 2013. However, over the last year and a half various issues have arisen in regards to VAT and Financial Services which has led to court cases with HMRC and therefore further guidance from HMRC and professional bodies was necessary. Having analysed all of the information made available by HMRC and our professional body, the PFS we have further defined our VAT position. This Fact-File outlines our current stance with regard to VAT on our services which may be subject to change in the future.

Fees in place of Commission

As from 1st January 2013 all financial advisers must charge *fees* (ongoing and initial) for their services as *new* commission arrangements are now banned, with the exception of Life Insurance product intermediation. VAT has therefore become an issue for Financial Services firms, where previously commission was always deemed to be VAT exempt.

The key points relating to VAT on fees are:

- Financial Services firms can provide VAT exempt services for a client but only if the services they provide qualify as “Intermediation” where the client has a desire and willingness to *purchase* a Retail Investment Product (RIP!).
- General Financial Advice is not *Intermediation* and is therefore subject to VAT. If a firm has sufficient supplies to exceed the VAT threshold, they must be registered for and charge VAT.
- Any services provided through a Discretionary Fund Manager are not exempt from VAT because HMRC deem that discretionary investment management is a VAT-able service that does not fall within the financial services exemptions.

AWFM's VAT position

AWFM provides client services which according to HMRC's definition will mostly be subject to VAT and our supplies are in excess of the VAT threshold. For this reason, AWFM was required to register for VAT as of 1st January 2013. This coincides with the effective date of the new Retail Distribution Review (RDR) rules.

Exempt Supplies

In some cases, we will still be able to provide some services that are exempt from VAT. In order to qualify for VAT exemption we would need to clearly evidence that there has been client specific interaction between us and the product provider in relation to the sale of exempt products. In other words the client must be seeking the arrangement of a Retail Investment Product. Discretionary Fund Management services do not qualify as a Retail Investment Product. Retail Investment Products would normally be classed as:

- A life policy
- A stakeholder pension scheme
- A personal pension scheme
- An interest in an investment trust savings scheme
- A security in an investment trust
- A structured capital at risk product
- An Annuity

Our Approach to VAT for new clients

At the earliest opportunity we will aim to establish with a new client whether the service they are seeking from us will be subject to VAT. This element will form part of our Fee Agreement with the client so that they know the *total* cost of our services, including VAT where applicable.

...Continued





In most cases, VAT will not apply to *initial* fees as most clients come to us with an expectation of purchasing some form of Retail Investment Product. This VAT exemption, in our opinion, includes regular initial fees that are taken from regular premiums or contributions. For clients who simply require financial planning or who require or are advised to take up the services of a Discretionary Fund Manager, VAT will need to apply to both initial and ongoing fees.

For clients who move to our Wealth Management Service, VAT will always apply to our regular percentage fee. This is because we provide a holistic financial advice service and it is therefore not possible for us to segregate which element of the fee relates to the exempt supply of *product intermediation* and the non-exempt supply of *general financial advice*. In practice this only increases the total annual costs by 0.10% and so will not have a significant effect on the overall performance of client portfolios.

Our Approach to VAT for existing ongoing clients

We prefer to continue, where possible to receive our income direct from the product provider rather than invoicing the client. As from 1st January 2013, we will be entering a transitional phase. The easiest way to break this down is to broadly set out the different product types:

Investment type 1: Investment ISA funds, Investment Bond, Personal Pension, Income Drawdown Fund, SIPP etc. except where DFM used

- In most cases, these funds will pay us 0.5% commission per annum.
- In some cases, where the underlying funds do not pay us the full 0.5%, we have agreed with our clients that additional units will be deducted from the fund to ensure that we receive 0.5% per annum of the funds we look after.
- Some providers appear to be suggesting that this “top-up” element to our fee is subject to VAT and some are saying it is not!
- Now we are post RDRs implementation date (1st January 2013), changes made to the investment may cause commission to cease (possibly only on the funds changed - for example, a fund switch). However, the changes that “trigger” the cancellation of commission varies significantly between product providers.
- If commission is cancelled, we will seek a new fee agreement with the client that will replace the commission with an ongoing fee for the same amount. In this scenario, the ongoing fee will then be subject to VAT. If we apply an initial charge to regular investments to replace lost initial commission, this will not be subject to VAT.

Investment type 2: Funds Managed by a Discretionary Fund Manager (DFM) (For example, Brewin Dolphin, Rathbones, WH Ireland etc)

- HMRC do not classify this service as a Retail Investment Product and therefore fees in relation to these funds are *not* exempt from VAT.

Product type 3: Life or Health Insurance policies, Endowment policies, Older style Personal Pension

- These type of Pure Protection policies may continue to pay us a small monthly commission based on the premiums paid. If clients cease to pay the premiums our commission ceases. VAT does not apply to these payments as they are commission and have always been VAT exempt.
- Some older Endowments and Personal Pensions pay us a commission based on the premiums paid into the plan rather than on the value of the fund. If a change is made to this type policy after 1st January 2013, the commission will cease. We will assess on a case by case basis what action we need to take, based on the clients’ requirements for an ongoing service.

Ongoing Clients fees

Clients who pay a fee by Standing Order or by an annual top-up fee will have VAT added to their fees, effective from 1st January 2013.

Summary

Each firm must assess the VAT position for themselves. The addition of VAT on many of our ongoing services is we believe an unintended consequence of the FSA’s Retail Distribution Review and for many clients this will increase the cost of the management of their finances which is regrettable.

The VAT position will be made clear on the specific client fee agreement for both new and ongoing clients.

