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Input VAT newsletter

Deduction of VAT on aborted deal costs by holding companies

17 October 2018

On 17 October 2018, the Court of Justice of the European Union (CJEU) ruled that a company could recover VAT on costs relating to an aborted acquisition of shares in another company to the extent that, based on objective elements, this company had the intention to provide management services subject to VAT to the acquired company (RyanAir, C-249/17). The decision of the Court is certainly an important evolution in its jurisprudence and should be examined with attention by Luxembourg holding companies that might be in a similar position even if each individual situation must be examined taking all relevant elements into account.

The deduction of the VAT incurred on the issuance[1], purchase[2] and sale[3] of shares by companies is a long story and was the source of some of the most famous VAT decisions of the CJEU. The RyanAir ruling is new step in a long story.

Background

RyanAir is an operational company. RyanAir made a formal takeover bid with the aim of acquiring the entire share capital of Aer Lingus. The European Commission declared that the concentration was incompatible with the common market. For that reason, Ryanair was only able to acquire slightly less than 29 percent of the shares in Aer Lingus.

In connection with the takeover bid, Ryanair availed itself of services subject to VAT. Ryanair claimed that VAT as deductible input tax. However, the Irish tax authorities refused this deduction.

The Irish Supreme Court referred the case to the CJEU and requested that it address two questions:

1. Can a future intention to provide management services subject to VAT to a takeover target, in the event that the takeover is successful, be sufficient to establish that the potential acquirer of shares in the target company is engaged in economic activity enabling him to deduct the VAT on his acquisitions costs?

2. Can there be a sufficient "direct and immediate link", between the acquisition costs and the potential provision of management services subject to VAT to the acquisition target?

The referring Court thus bases its questions on the traditional CJEU jurisprudence regarding the deduction of VAT by "active" holding companies, i.e. holding companies that also provide services, financing or rent properties to the companies in which they own shares.

It is important to highlight that RyanAir did not charge management services to Aer Lingus but argued that it will do should the takeover be successful.

Conclusions of the Advocate General

In her conclusions rendered on 3 May 2018, the Advocate General, Mrs Kokott, diverted from the traditional holding jurisprudence to focus on a "functional analysis".

Even if the Court has not followed the Advocate General's opinion, it is worth summarizing it.

She firstly notes that although, in this instance, the takeover of a competitor is intended to be achieved by acquiring shares in the company, the case is much closer to the situation where an undertaking plans to buy up all of a competitor's physical equipment and facilities than to the situation where an undertaking wishes to purchase shares merely to generate dividends.

The Advocate General adds that strategic takeover of an undertaking by which the acquiring company pursues the aim of extending or modifying its operating business is to be regarded as such a direct, permanent and necessary extension of a taxable activity.

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Consequently, the Advocate General considers that costs incurred by the acquiring company in connection with achieving such a strategic takeover have a direct and immediate link with its taxable activity with the result that the company might deduct VAT in accordance with that activity.

Decision of the Court

As already mentioned the Court does not follow the conclusions of the Advocate General but rather follows her jurisprudence regarding the acquisition of shares by "active" holding companies.

The Court first examines whether the future intention to provide management services subject to VAT to a takeover target is enough to consider that RyanAir effectively incurred the acquisition costs for an economic activity examining his jurisprudence regarding preparatory activities4.

The Court rules that it is effectively the case: *"Furthermore, since economic activities (…) may consist of several consecutive transactions, the preparatory acts must themselves be treated as constituting economic activity. Thus, any person with the intention, as confirmed by objective elements, of independently starting an economic activity, and who incurs the initial investment expenditure for those purposes must be regarded as a taxable person (…).*

The Court continues *" (…) it is apparent from the file before the Court that, by the planned acquisition of shares in the target company, Ryanair's intention was to provide the target company with management services subject to VAT".*

Regarding the deduction itself and the link between the VAT on costs and the taxable activity, the Court rules that *"a taxable person also has a right to deduct even where there is no direct and immediate link between a particular input transaction and an output transaction or transactions giving rise to the right to deduct where the costs of the services in question are part of his general costs and are, as such, components of the price of the goods or services which he supplies".*

Based on these developments, the Court decides that *"a company, (…), which intends to acquire all the shares of another company in order to pursue an economic activity consisting in the provision of management services (…)" subject to VAT has "(…) the right to deduct, in full, input VAT paid on expenditure relating to consultancy services provided in the context of a takeover bid, even if ultimately that economic activity was not carried out, provided that the exclusive reason for that expenditure is to be found in the intended economic activity".*

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We have also to mention that on 8 November 2018, the Court will have to rule on the deduction of VAT on costs incurred in relation, this time, to the sale of shares5 in the C&D Foods affair. The story of the deduction of VAT on the acquisition and sales of shares is therefore not yet closed.

The decision of the Court is certainly an important evolution in her jurisprudence and should be examined with attention by Luxembourg holding companies that might be in a similar position even if each individual situation must be carefully examined taking all relevant elements into account .

[1] Kretztechnik AG, C-463/05, 26 May 2005 and Securenta, C-437/06, 13 March 2008

[2] Cibo Participations SA, C-16/00, 27 September 2001 ; C-29/09 Larentia + Minerva mbH & Co. KG and Marenave Schiffahrts, C-108/14 and C-109/14, 14 November 2015 and Marle Participations SARL v France, C-320/17, 5 July 2018

[3] Wellcome Trust, C-155/94, 20 June 1996; BLP group plc v UK, C-4/94, 6 April 1995 and AB SKF, 29 October 2009

[4] Rompelman, C-268/83, 14 February 1995, Inzo, C 110/94, 29 February 1996, Breitsohl, ç-400/98, 8 June 2000 and Ablessio, C-527/11, 14 March 2013.

[5] C&D Foods Acquisitions ApS, C-502/17.

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