# Comments on Draft Guidance - VAT Deductibility for Holding Companies

## 1 Introduction

No Comment

## 2 General Principles in respect of deductibility

## 3 Entitlement to deductibility

At the top of page 4, there is a reference to the question of a “direct and immediate link” for VAT recovery purposes being “a matter of fact” requiring an objective evaluation of all of the circumstances. This is obviously a basic principle but it would be very helpful for the paper to include some examples/criteria which Revenue would consider applicable in the case of holding companies seeking VAT recovery. This should include some both positive and negative examples.

## 4 Deductibility and Apportionment

### 4.1 Economic and non-economic activity

The extract from the MVM judgment quoted in the paper confirms that it is for Member States to “establish methods and criteria” for apportioning between economic and non-economic activities, subject to the overall principles of the VAT system. While the paper confirms Revenue’s view that the method should be the one which “best reflects” how those costs are consumed, in our view, more detailed guidance and examples are required in this area.

### 4.2 Deductible and non-deductible economic activity (dual use)

This appears to be the appropriate place to comment regarding "general costs".

Throughout the paper there is reference to "general costs", "general expenditure" and "general overheads". Subject to potential very limited exceptions, we understand this to mean expenditure is not directly attributable to non-economic activities, vatable activities, qualifying activities or exempt activities. The paper appears to acknowledge that a taxable person fully engaged in vatable activities and/or qualifying activities is entitled to fully recover VAT incurred on such expenditure. Also the paper appears to acknowledge that a taxable person engaged in vatable activities and/or qualifying activities and also engaged in non-economic activities and/or exempt activities is entitled to partial VAT recovery in relation to such expenditure.

However in some places the paper also suggests that there is a need to demonstrate a link to the overall economic activity in order to recover VAT incurred on such expenditure. In practice this is causing problems. In some cases, Revenue officers are not acknowledging that VAT incurred on what is clearly a general overhead (such as the annual audit) qualifies for partial recovery in a "mixed holding company" scenario. They are insisting on somehow proving a link to the economic activity but not explaining what this means.

The paper would greatly benefit from a separate heading for "General costs", examples of what such costs include and an explicit statement confirming full recovery entitlement or partial recovery entitlement where general costs are incurred by a taxable person engaged in in vatable activities and/or qualifying activities. In our view such costs include the following: audit services, rent, utilities, IT, regulatory matters, compliance matters, banking matters, insurance matters, employee matters, day to day dealings and engagement with shareholders. In the context of a passive holding company which is a member of a VAT group we would consider it to include all day to day expenditure.

## 5 Holding Companies and Share Acquisition Costs

The introduction confirms that *"This section deals with holding companies whose sole activity is the holding of shares in other undertakings or the holdings of shares together with the provision of taxable management services to those undertakings."* However, there are also holding companies which undertake other economic activities (i.e. supply goods and services other than management services to their subsidiaries or their third party) and the guidance should take these scenarios into account. We comment further on this under section 5.2 (Active holding companies).

### 5.1 Passive holding companies

No comment

### 5.2 Active holding companies

The current draft of the paper seems to define an active holding company solely based on the provision of management services which in our view is overly restrictive.

In our view, this definition of active holding companies is too restrictive as an active holding company is a company engaged in any economic activities. The management of subsidiaries is an example of an economic activity but is not exclusive. As an example of another economic activity of a holding company (and this is explicitly addressed in the UK guidance on holding companies and in a number of CJEU cases such as Ryanair and EDM), if a shareholding is acquired as a direct, continuous and necessary extension of a taxable economic activity of the holding company, the VAT incurred should also have a direct and immediate link to taxable supplies and be recoverable. In these circumstances, there is no need for the holding company to provide management services to the acquired business for the VAT to be deductible. It would be helpful for the paper to clarify that management services are an example of the economic activities of a holding company and to confirm with examples that where a shareholding is acquired as a direct, continuous and necessary extension of a taxable economic activity of the holding company that the VAT incurred on such costs is deductible.

#### 5.2.1 Intention and Consideration

While CJEU VAT case-law has confirmed that a tax authority is entitled to seek objective evidence of a taxable person's intention to make taxable supplies, it has also been confirmed (for example in the High Court decision in *Crawford v. Centime Limited* [2005 No. 62R) that these requirements should not go beyond what is necessary for the purposes of establishing whether the taxpayer's intention is genuine. In this context, it is important that the statement "Where a taxpayer does not have objective evidence of an intention to supply taxable management services at the time the costs are incurred there is no right to deduction" is not interpreted in such a way that makes it extremely onerous to establish the right to deduction. Rather, where taxpayer can establish that based on the facts and circumstances they have a genuine intention to provide taxable management services, the right to deduction on share acquisition costs should arise.

This section should also confirm that where a company has a genuine intention to acquire a target and provide taxable management services (or other taxable goods and services) to the target, but that acquisition is unsuccessful and as a consequence no management or other goods and services are provided to that target, the company remains entitled to deduction of VAT on the aborted bid costs. This was confirmed in the Ryanair case (C-259/17).

It would be helpful if Revenue could comment on whether they consider that a charge for management services which is less than the costs incurred to provide such services causes any issues in terms of VAT recovery by the holding company. It is important to note that it is not a requirement in any of the CJEU decisions that the level of management charges to equal or exceed

the costs in order for VAT to fully deductible on those costs, and indeed it was specifically confirmed in the Advocate General's Opinion in Ryanair that there is no such requirement.

Per the second last paragraph "Where a holding company provides management services to a subsidiary fees and the payment is contingent on the profitability or ability to pay of that subsidiary, such supplies are outside the scope of VAT. " Is it the position of Revenue that contingency fees not only in these types of cases but more generally contingency fees are always outside the scope of VAT?

5.3 Mixed holding companies

Per our comments at 4.1 above and as noted in the extract from the CJEU's judgment in Larentia + Minerva quoted on Page 9, the criteria for apportioning costs between economic and non-economic activities should be defined by the Member States. In our view Revenue should set out its criteria for apportioning such costs. It would also be helpful for the paper to include examples.

Direct and indirect management services

There are circumstances where the acquiring company does not provide management services directly to the target company but to its trading subsidiaries. It would be helpful if the paper could address this, perhaps by acknowledging (as outlined in Cibo) that direct or indirect management of subsidiaries is an economic activity and therefore the same VAT recovery principles should apply.

6 **Holding Company Ongoing Costs**

At the top of page ten there is a statement that reads: *"However, there may be circumstances where such general overhead costs can have a sole direct and immediate link to an exempt or non-economic activity and are not deductible".* However if a cost has a "sole direct and immediate link" to a specific activity it would not in our view constitute a general overhead. We would suggest that this be deleted or clarified (e.g. delete the words "such general overheads").

On page ten there is reference to scenarios which in Revenue's view may involve costs incurred in respect of certain activities for the benefit of its shareholders without having a link to taxable economic activities of a company.

In our view where a company is engaged in economic activities it is artificial to create distinctions between transactions/activities which benefit the shareholders and which benefit the company's economic activities. The shareholders and the company's economic activities are intrinsically linked. The company's very existence and engagement in economic activities are dependent on shareholder maintenance and satisfaction. Accordingly all events which have an impact on shareholder value also impact on the company's economic activity.

In the context of a share issue, the position set out above is supported by the Advocate General's opinion in "Kretztechnik" C-45/03, paragraph 26: "There can be no reasonable doubt that a commercial company which raises capital does so for the purposes of its economic activity."

Furthermore per the Advocate General's opinion in "Larentia and Minerva" (C -108/14):

- Conclusion: "Expenditure connected with capital transactions incurred by a holding company which involves itself directly or indirectly in the management of its subsidiaries has a direct and immediate link with that holding company's economic activity as a whole. Input value added tax on that expenditure should not therefore be apportioned between the economic and non-economic activities of the holding company."

The judgment in "AB SKF" (C-29/08) is also relevant:

- Paragraph 64: "it must be recalled that the Court has held, on numerous occasions, that there is a right to deduct VAT paid on consultancy services used for the purposes of various financial transactions, on the ground that those services were directly attributable to the economic activities of the taxable persons (see, inter alia, Midland Bank, paragraph 31; Abbey National, paragraphs 35 and 36; Cibo Participations, paragraphs 33 and 35; Kretztechnik, paragraph 36; and Securenta, paragraphs 29 and 31)."

Regarding share related transactions generally, in our view reference to the Advocate General's opinion in the "Ryanair" case (C- 249/17) is critical. The opinion supports VAT recovery entitlement based on a functional analysis approach. Essentially this distinguishes cases where transactions are carried out (i) for the benefit of an economic activity and (ii) for investment purposes. In the case of the former, the VAT incurred on related expenditure is recoverable to the extent that the economic activity is a vatable activity. In the case of the latter the VAT is not recoverable. This approach has direct relevance to the three scenarios mentioned on page ten.

In respect of the second last paragraph on page ten, it states that the costs listed (e.g. defending a takeover bid) “may not” have a direct and immediate link to the taxable economic activity of a company. To avoid potential confusion, we recommend that “may not” be replaced with “might not” (as “may not” could be interpreted to mean “cannot” which we understand is not the intention).

6.1 Passive Holding Company

No Comment

6.2 Holding Company Carrying on a Fully Taxable Activity of Remunerated Management Services

6.3

Regarding the second example, in our view restructurings that seek to create/improve shareholder value are also intended to benefit the economic activities of a company and accordingly related costs should be treated as general overheads.

If you consider the position to be otherwise, please clarify what you mean using examples.

6.4 Holding Company Carrying on a Mixed Activity of Remunerated Taxable Management Services and Holding of Shares

Regarding the third category of cost it would be helpful if Revenue would comment on and provide examples of how Revenue would consider it appropriate to apportion costs

7 **Deductibility and Share Transactions**

No Comment

7.1 Issue of shares by a company

No comment

7.2 Sale of shares by a company

No comment

8 **Single taxable person (VAT group)**

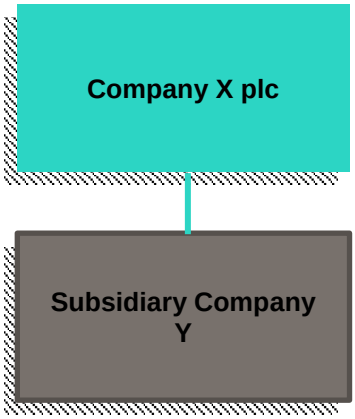
The inclusion of the additional paragraphs and examples is welcome and helps greatly to clarify the position.

A key issue is that VAT grouping can and frequently does impact on the VAT recovery entitlement position of the members. It is our understanding that this is common ground but we think the paper would benefit

from an explicit statement to that effect and the inclusion of some examples to illustrate the position. It is also our understanding that Revenue agree that where a holding company is a member of a VAT group, there is no specific need, for VAT recovery purposes, for it to provide services. We attach examples (scenarios 1 to 5) which would be helpful to include to illustrate the position.

We consider that the inclusion of the extract from the Advocate General's opinion (at the bottom of page 15) has potential to confuse the position. In our view the Advocate General was simply confirming that the normal VAT recovery rules apply to VAT groups. However, in our experience, some Revenue officers have interpreted this extract to mean that the VAT recovery position of members cannot change as a consequence of joining a VAT group. We think it would be helpful to delete this paragraph and avoid any such confusion.

**Scenario 1 – Holding Company and Subsidiary Company not VAT grouped**

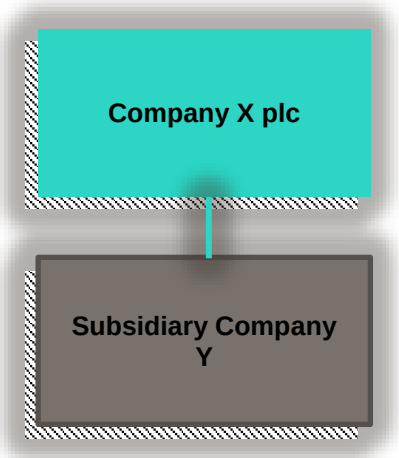



Company X plc is a holding company which provides vatable management services for consideration to Company Y.

Company Y is a bank which is fully engaged in exempt activities.

- **VAT treatment** – Company X plc has full VAT recovery entitlement and Company Y has no VAT recovery entitlement.

**Scenario 2 - Holding Company and Subsidiary Company VAT grouped**




Company X plc and Company Yare now members of a VAT group and are treated as a single taxable person.

- **VAT treatment of VAT Group** – No VAT recovery entitlement. This is because the VAT recovery entitlement is determined by reference to the external activities of the VAT group. The services provided by Company X plc to Company Y are ignored.

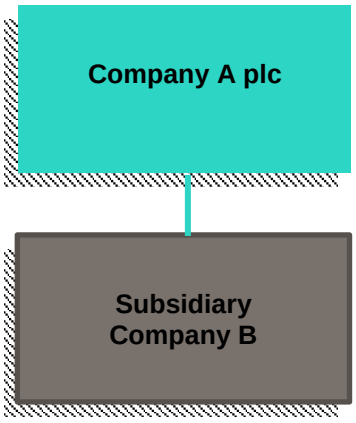
**Scenario 3 – Single public limited company**


Company A plc is fully engaged in vatable activities consisting of the manufacturing and distribution of desks.

- **VAT treatment of Company A plc** – Full recovery entitlement in respect of VAT incurred on expenditure which is directly attributable to vatable activities e.g. the purchasing of materials for the manufacture of desks.

Full recovery of entitlement in respect of VAT incurred on general overheads e.g. audit fees, maintenance of share register, investor relations and communications costs.

**Scenario 4 – Holding Company and Subsidiary Company not VAT grouped**

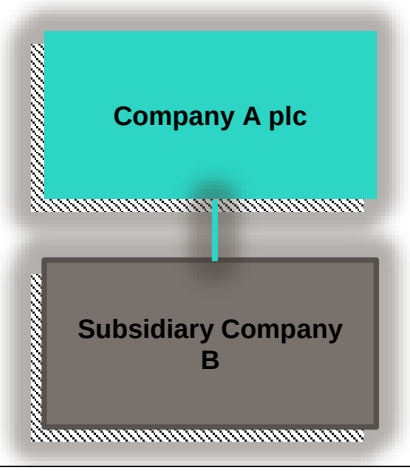



Company A plc is a pure holding company. It does **not** provide services to its subsidiary Company B.

Company B is fully engaged in vatable activities consisting of the manufacturing and distribution of desks.

- **VAT treatment of Company A plc** – No VAT recovery entitlement as it is a pure holding company.
- **VAT treatment of Company B** – Full VAT recovery entitlement, as is the case for Company A plc in Scenario 3.

**Scenario 5 – Holding and Subsidiary Company VAT Grouped**




Company A plc and Company B are now members of a VAT group and are treated as a single taxable person.

- **VAT treatment of VAT Group** - Full VAT recovery entitlement, as is the case for Company A plc in scenario 3.