

# Advocate General's opinion on VAT recovery and investment holdings

## *Securenta Göttinger Immobilienanlagen und Vermögensmanagement AG*

The Advocate General has issued his opinion in the *Securenta* (C-437/06) case, concerning the apportionment of input VAT to non-economic activity.

If the European Court of Justice (ECJ) follows the opinion in its judgment, it could signal a significant shift in the accepted input VAT recovery position of the private equity industry, infrastructure funds, private finance initiative (PFI), property limited partnerships, the life sector and cross-border investment structures.

The case is highly significant for all in the asset management and real estate industries and anyone dealing with share holdings and investment disposals.

The case involves a German taxpayer, a public company, which carried on the business of acquiring, managing and selling real estate, securities, financial holdings and investments of all types. It raised capital for investment by the issue of shares and "atypical silent partnerships" (similar to non-voting preference shares). The taxpayer generated 45% of its income from taxable leasing transactions and roughly 25% from dividend income and share disposals.

The German tax authorities disallowed recovery of 68% of its non-attributable input VAT as relating to the share issues and allowed 45% recovery of the remainder, giving an effective 15% residual recovery rate.

### The Advocate General's opinion

The Advocate General concluded that input VAT incurred on expenditure connected with the issue of shares or "silent partnerships" is only allowed to the extent that it is attributable to that person's economic activity.

Agreeing with the representations of the UK, the Advocate General considered that the method of apportionment to the non-economic activity was not prescribed by the

Sixth Directive and was a matter for the Member States. However, in line with the evolving jurisprudence of the ECJ any such discretion on Member States would be fettered by the principle of neutrality.

The paragraph of particular concern to the funds sector is paragraph 33, which says that "*It follows that the deduction of the input tax on the expenditure connected with the issue of financial holdings is not justified unless the capital thereby acquired is allocated to the applicant's economic activity. However, the expenditure connected with the issue of shares or atypical silent partnerships and attributable to the applicant's non-economic activity (that is to say, to its acquisition, holding and sale of interests in other businesses) does not entitle the applicant to tax deduction.*"

### Key implications

What constitutes an interest in an "atypical silent partnership" is of course unfamiliar to UK practitioners, but given the reference to *Kaphag* (C-442/01) the opinion is of potential application to investment structures utilising limited partnerships or LLPs.

The reference to the acquisition, holding and sale of interests in other businesses clearly

throws the spotlight on recoveries in the private equity sector. Taken to an extreme, this could include any type of equities fund and it is not clear where the line would, or should, be drawn.

Paragraph 33 is also of concern to corporate fund vehicles which own assets through a holding company structure (e.g. some Luxembourg SICAV and international real estate structures). If such fund vehicles were to be considered to be engaged in solely non-economic activities, it would throw into question the place of supply of cross-border management charges. The UK manager of such a fund may have to charge UK VAT. There is an clear tension here with the ECJ's earlier judgment in *Banque Bruxelles Lambert (BBL)* (C-8/03).

Further, this case may also have significant consequences for businesses operating outside the financial services arena.

### What should you do now?

All potentially affected taxpayers should keep the progress of this case under review as a matter of high priority. Consideration should be given to the impact on VAT recovery levels of the forthcoming ECJ decision, and what steps may be taken to mitigate the impact of an adverse ECJ ruling.

For further information, please call your usual PwC contact or any of the people listed below.

#### Contacts

Jamie Randell	<a href="mailto:jamie.t.randell@uk.pwc.com">jamie.t.randell@uk.pwc.com</a>	020 7213 8253
Stephen Coleclough	<a href="mailto:stephen.coleclough@uk.pwc.com">stephen.coleclough@uk.pwc.com</a>	020 7212 4911
Keith Moore	<a href="mailto:keith.t.moore@uk.pwc.com">keith.t.moore@uk.pwc.com</a>	020 7212 5582
Cathy Hargreaves	<a href="mailto:cathy.e.hargreaves@uk.pwc.com">cathy.e.hargreaves@uk.pwc.com</a>	020 7212 5575
Nick Skerrett	<a href="mailto:nick.skerrett@uk.pwc.com">nick.skerrett@uk.pwc.com</a>	020 7804 2054

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, PricewaterhouseCoopers LLP, its members, employees and agents accept no liability, and disclaim all responsibility, for the consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.