The recovery of VAT on costs for acquiring shares in constant evolution

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In brief

The Court of Justice of the European Union (CJEU, "the Court") released its decision on 5 July 2018 in the case Marle Participation SARL v Ministre de l'Economie et des Finances (C-320/17). This case relates to the recovery of VAT on costs incurred for acquiring a subsidiary.

In its judgment, the Court ruled that the letting of immovable property by a holding company to a subsidiary constitutes an involvement of the holding in the management of its subsidiary and, if the letting of the property is subject to VAT, the holding company is entitled to recover VAT incurred on the costs for acquiring the concerned subsidiary.

This is another favourable decision of the CJEU for holding companies that provide services to their subsidiaries, not only because the Court confirms that the letting of property is sufficient to qualify as "active management of the subsidiary but also because the Court seems to confirm that the recovery of VAT on acquisition costs is not dependent upon a minimum level of taxable turnover earned by the holding company.

The VAT recovery position of Luxembourg holding companies should be reviewed at the light of the recent European case-law.

In detail

Background

The French company Marle Participation SARL ("MP") is the holding company of the Marle group, active in orthopaedics manufacturing. In 2009, MP went through some restructurings by which it sold shares and acquired shares. MP recovered VAT incurred on transaction costs relating to that restructuring. The French VAT authorities, as well as the lower tier tribunals refused the recovery of the VAT on the grounds that the transaction costs would not pertain to an economic activity of MP. Before taking a decision, the *Cour de cassation* referred a question to the CJEU, to clarify if the output operations of MP (which were limited to the letting of immovable property to the acquired subsidiary) constituted active involvement of MP in the management of that subsidiary. The answer to this question was essential to determine whether the holding of shares constituted a non-economic activity for MP or not.

Based on previous case law released by the Court, the mere holding of shares (with no involvement in the management of subsidiaries) is not an economic activity, and therefore VAT on acquisition costs is irrecoverable. On the contrary, a holding company actively involved in the management of its subsidiaries performs economic activities.

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As a result, a holding company can recover VAT incurred on acquisition costs, to the extent that its involvement in the management of the acquired subsidiary consists of taxed activities. The Court had already reached this conclusion on 16 July 2015 in its joint decisions Beteiligungsgesellschaft Larentia + Minerva mbH & Co. KG v Finanzamt Nordenham (case C-108/14) and Finanzamt Hamburg-Mitte v Marenave Schiffahrts AG (case 109/14), confirming previous decisions (notably Cibo Participations SA v Directeur regional des impôts du Nord-Pas-de-Calais, decision C-16/00 dated 27 September 2001).

In those previous decisions, the Court stated in substance that the holding of shares accompanied by a direct or indirect involvement in the management of a subsidiary (such as the supply of administrative, financial, commercial and technical services) must altogether be considered as an economic activity carried out by the holding company.

The concept of "involvement in the management" has never been clear-cut and is subject to interpretation, more or less restrictive, depending on the administrative practice in the EU Member States. A clarification on the scope of this concept was needed. In substance, the Court was requested to conclude on whether the letting of immovable property to a subsidiary is sufficient to constitute an active involvement in the management of that subsidiary or not.

Decision of the Court

The Court clarified that the list of services mentioned in the previous cases (administrative, financial, commercial and technical services) is not exhaustive, and that the notion of "involvement in the management" of a subsidiary includes any transactions constituting an economic activity performed by the holding company for its subsidiary.

The letting of immovable property to a subsidiary is a service that constitutes an involvement by the holding in the management of its subsidiary, says the Court. Consequently, VAT incurred by the holding company on goods and services purchased for acquiring that subsidiary is recoverable, if:

- the services are rendered to the subsidiary on a continuing basis;
- the services are rendered for remuneration;
- the services are taxable (i.e. not exempt) transactions;
- a direct link exists between the services rendered by the holding company and the consideration received from the subsidiary.

The Court reminds that acquisition costs incurred by a holding company are part of its general costs if they are incurred for the acquisition of shares in an undertaking in the management of which the holding company is subsequently involved. VAT on such costs is therefore in principle recoverable (if the holding does not also provide VAT exempt services to the concerned subsidiary).

The CJEU adds that "[…] *it must be noted that, for the purposes of assessing the deduction granted to a holding company that involves itself directly or indirectly in the management of its subsidiaries in which it has bought shares, no account can be taken of the turnover achieved by that company from the letting services supplied to those subsidiaries and the income that it draws from its stake in the capital of those subsidiaries, in order to prevent that right from being invoked for fraudulent or abusive ends.*"

Nonetheless, the Court reminds that the recovery of VAT can be refused where objective elements demonstrate that the VAT recovery is claimed with abusive or fraudulent ends.

Practical implications

The recovery of VAT on costs incurred for acquiring shares in a subsidiary is still an important area of challenge and discussions with the VAT authorities in the EU Member States (including in Luxembourg). This is notably true in situations where a holding company claims for the recovery of VAT on acquisition costs that are higher than the holding company's turnover derived from taxable services rendered the acquired subsidiary.

This new decision should provide more comfort to VAT payers that provide taxable services to their subsidiaries, and provide arguments against restrictive positions taken by their VAT authorities.

In Luxembourg, few written guidance exist about VAT recovery methods for holding companies. In the Circular 765-1 dated 11 June 2018, the Director of the VAT authorities reminds that partial VAT payers (which carry out both economic activities and non-economic activities) cannot recover input VAT incurred on the cost of goods and services used for the needs of their non-economic activities. The Circular extends the scope of Circular 765 dated 15 May 2013 to partial VAT payers, which clarifies that input VAT recovery must be determined by appropriate methods, including notably objective keys of allocation between the activities performed by the taxpayer.

This decision could also provide arguments for recovering input VAT on recurring costs (through the life of the investment) and disposal costs (when the subsidiary is sold).

The Court is expected to release soon its decision in at least two other cases relating to acquisition costs (Ryanair Ltd v The Revenue Commissioners, C-249/17) and the concept of general costs (Morgan Stanley & Co International plc v Ministre de l'Economie et des Finance, C-165/17).

Let's talk

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