VAT: HMRC update Internal Manuals relating to Holding Companies

Indirect Tax

01 June 2017

On 20 April, HMRC issued a number of updates to its 'VAT Input Tax' internal guidance manuals; specifically in relation to the VAT recovery position of holding companies and deal costs. This will therefore be of interest to many businesses; particularly those involved with merger & acquisition transactions.

Following a long period of uncertainty in this area, the CIOT welcomes the updates which publicly document HMRC's current policy on 'cost-components' against the background of recent CJEU and domestic case law (for example, the CJEU decision in *Larentia + Minerva and Marenave Schiffahrt* (C-108/14 and C-109/14)).

A number of different web pages have been updated including:

- Legal history: cases about holding companies
- When is VAT recoverable by holding companies?
- Specific issues: definition and VAT status of holding companies

The CJEU held that VAT incurred by a holding company on the costs of acquiring shareholdings in subsidiaries to which it also intended to provide taxable management services, must be regarded as belonging to the holding company's general overhead expenditure and is deductible (subject to any partial exemption restriction).

Prior to this decision, HMRC's policy was that VAT incurred on the acquisition costs of shares by a holding company was only deductible where it was directly attributable to the provision of taxable services. Additionally, HMRC had considered that VAT on costs incurred by a holding company was only recoverable if the intention was to recoup the expenditure from the income resulting from taxable supplies provided to subsidiaries within a reasonable time.

HMRC has confirmed they will no longer consider the timeframe within which the expenditure is recouped. The need for a link through to taxable supplies remains contentious however. The guidance reiterates that VAT grouping a holding company will not in itself make any VAT it incurs recoverable input tax. It suggests that the costs would still need to be traced through to external supplies by the group or else fall into a general category of ‘stewardship costs’ which the holding company might incur for the overall good of the group rather than its own non-economic investment activity (for example group audit fees). If the cost does not meet either of these two tests the implications are that the VAT is incurred in relation to non-economic activity and is not recoverable.

What is covered in the update?

- when a shareholding is used as part of an economic activity;
- whether the holding company is the recipient of the supply;
- whether the holding company is undertaking economic activity for VAT purposes;
- whether a shareholding is acquired as a direct, continuous and necessary extension of a taxable economic activity of the holding company;
- whether there is an intention to make taxable supplies;
- contingent consideration for management services;
- the effects of a holding company joining a VAT group;
- stewardship costs; and
- mixed economic and non-economic activities.

What is our initial reaction?

Published shortly before going to press, our initial view is that the guidance, whilst useful in places, still leaves significant scope for differing interpretations and at times appears internally inconsistent.

We hope that HMRC will agree to continue to refine and expand this guidance in order to clarify their views on this complex and contentious area of VAT so that all involved can benefit from a reasoned and consistent approach.

It will be important to ensure that officers following the guidance, practitioners and taxpayers all share a common view of the principles HMRC will apply in considering VAT recovery on holding company and deal costs.

We have previously commented on the draft guidance that was to feature in an RCB. You can read more at: *Deduction of VAT by holding companies – The Larentia and Minerva case*.

We will be seeking our member's views for further analysis. If you have any comments, please do send them to me or technical@ciot.org.uk