

## **Advocate General at CJEU: VAT recovery limitation when preparing sale of a participation**

On September 6, 2018, Advocate General Kokott (hereinafter: AG Kokott or AG) at the Court of Justice of the European Union (hereinafter: CJEU) issued her Opinion in the C&D Foods case (C-502/17). The case concerns the recovery of VAT on professional expenses for a proposed but ultimately unrealized sale of shares. AG Kokott concludes that the professional services are related to a VAT-exempt share sale, which in principle creates a VAT recovery limitation on such expenses. The CJEU's final judgment in this case will have to show whether the Dutch practice, in which VAT on professional advisor fees is generally deducted, can continue to exist.

### **Brief outline of facts and AG Kokott's Opinion**

The Danish company C&D Foods is part of an international group. It indirectly holds all the shares in Arovit Petfood and performs management services for this company, corresponding to its payroll costs and a 10% mark-up. When the international group started to have a hard time economically, it was decided to examine whether restructuring the group could alleviate matters. C&D Foods decided to engage a law firm for the sale of the shares in Arovit Petfood, which drew up a draft agreement with an unnamed buyer. C&D Foods ultimately abandoned the sale as no suitable buyer could be found.

AG Kokott first confirms that C&D Foods performs a VAT taxable transaction by involving itself with the management of its sub-subsidiary Arovit Petfood in exchange for a fee. In such circumstances, she considers that the proposed sale of a company limited by shares falls within the scope of VAT. In principle, the sale of shares is exempt from VAT. It is remarkable that AG Kokott also regards the mere preparation of a share sale as a VAT-exempt service. The AG's approach means that the only question remaining is how VAT should be deducted on the preparation costs. There are two possibilities for this:

1. *Direct and immediate allocation to the share sale*  
AG Kokott believes that there is a direct and immediate relationship between the legal fees incurred by C&D Foods and the proposed VAT-exempt share sale. It is for the Danish national court to examine this relationship in more detail.
2. *Allocation to C&D Foods' entire business activity (general overhead)*  
Only if the above direct and immediate relationship cannot be established, should the legal fees be reviewed to see whether these are connected with the overall economic activity of the business. In the latter case, there would be a (partial) right to deduct in accordance with the usual VAT recovery right of the business.

### **Questions concerning the AG Kokott's Opinion**

We believe that AG Kokott's approach raises the following issues and questions:

1. We wonder whether a VAT-exempt transaction can be identified in the case of a proposed but unrealized sale of a participation. Within a group, it is inherent in

the normal activities of an actively involved and managing holding company to examine from time to time whether participations should be bought or sold, and whether a merger, division or other restructuring should take place. This partly depends on the financial situation of the group or one of its members, the prospects of certain divisions or as a result of a market strategy chosen by the group. Unlike the AG, we do not see a separately recognizable VAT-exempt service in the mere preparation for the sale of shares, but a more direct relationship with the normal and overall activities of the actively involved holding company. In this sense, a recovery in accordance with the normal VAT recovery right of such a holding company would make more sense.

2. In view of the major consequences for the VAT recovery right, we believe that a stricter definition of the VAT-exempt transaction in relation to regular economic activities would be desirable. In our view, the AG is too quick to assume that there is a VAT-exempt transaction and this assumption does not do justice to a number of uncertainties that play a role in such preparations for the sale of shares. For example, the AG's approach does not seem to take account of a (potential) sale of shares to a buyer established outside the European Union. In such a case, there is a full entitlement to VAT recovery.

#### **Dutch practice: what steps can you take now?**

If C&D Foods were the party selling the participation, under current Dutch practice there would generally be a right to recover VAT on the professional advisor fees in accordance with the usual VAT recovery right applying to general overhead (as elaborated in a Decree of the Deputy Minister of Finance). We believe that the same VAT consequences also apply in the case of a proposed but unrealized sale of shares. If your business is involved in the sale of participations and if costs are incurred in connection with the preparation thereof, then in view of this Opinion, it would be advisable to have your VAT position reviewed. Our VAT specialists in the Indirect Tax Group will be happy to be of assistance in this respect. This Opinion is particularly important for M&A practices, whether or not within groups, private equity enterprises, but also for operating businesses holding participations.

If the CJEU were to adopt this Opinion, it might also have an impact on the right to recover VAT in the case of proposed (VAT-exempt or VAT-taxed) services in other sectors, such as the healthcare sector, education and real estate.

Meijburg & Co  
September 2018

*The information contained in this memorandum is of a general nature and does not address the specific circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.*