VAT on deal costs incurred by bid vehicle

BAA Ltd [2010] UKFTT 43 (TC)

HMRC continues to challenge VAT recovery in respect of costs incurred on corporate transactions and structuring activities. In this case, the First Tier Tribunal held that the representative member of the target VAT group was entitled to deduct the VAT incurred by a bid vehicle once it had joined the VAT group. The Tribunal considered that the bid vehicle was conducting an economic activity even though it had no intention to make taxable supplies and did not make any taxable supplies (although such supplies were made by the VAT group which it joined following completion of the deal).

Background

A bid vehicle incurred significant professional fees relating to the takeover of BAA Plc. After the takeover was completed, the bid vehicle joined the target company (BAA's) VAT group. The representative member of that VAT group (the Taxpayer) claimed the VAT incurred on the professional fees by the bid vehicle as attributable to the general overheads of the VAT group. HMRC raised an assessment disallowing the input VAT claimed and the Taxpayer appealed.

In March 2006 the bid vehicle was incorporated by the consortium established to make the takeover bid. The bid vehicle entered into engagements with professional advisors in relation to the bid. Towards the end of June 2006, the takeover bid was completed and in the following four months the fees were paid to the various professional advisors. In September 2006, the bid vehicle sought to join the target company's VAT group and although originally HMRC declined to group the bid vehicle, HMRC eventually admitted it to the VAT group with effect from 22 September 2006.

The Taxpayer produced evidence that, following the takeover, the bid vehicle provided management services (including directors' services) as the top holding company of the group. It provided strategic advice and direction to the group. After the takeover, the group undertook a refinancing exercise and one of the dividing issues between HMRC and the Taxpayer was whether this refinancing was a 'seamless' exercise or whether there were two separate stages, i.e. one prior to the acquisition and one post-acquisition.

The Taxpayer argued that the effect of HMRC's refusal to refund the input VAT claimed was to treat the bid vehicle as if it were a final consumer with the chain of supply ending at that point. The Taxpayer contended that was an impossible analysis since the costs incurred by the bid vehicle were used to make an acquisition and not a supply. The Taxpayer's argument was that

HMRC's refusal to repay was to leave the input VAT trapped in a chain of supply otherwise than as a result of a chain-breaking exempt transaction. HMRC replied that the key test was whether the bid vehicle was conducting an economic activity, and was acting as a final consumer. HMRC further contended that, since the bid vehicle had no intention to make any taxable supplies in its own right, no entitlement to input VAT deduction arose.

One of the key defining issues in the case was the implications of both VAT grouping, and the ECJ's judgment in Faxworld (Finanzamt Offenbach am Main-Land v Faxworld Vorgründungsgesellschaft Peter Hünninghausen und Wolfgang Klein GbR (C-137/02). In particular, the Taxpayer argued that the VAT grouping 'fiction' meant that the VAT incurred by the bid vehicle had the necessary 'direct and immediate link' with the supplies made by the representative member of the VAT group. In relation to Faxworld, the issue was whether it could be regarded as authority for the proposition that (in certain cases) VAT incurred by one entity could be recoverable by reference to the activities carried on by another entity, and whether an acquisition of shares by the bid vehicle in this case led to the same treatment as the TOGC situation in the Faxworld case.

Held

The Tribunal concluded that the bid vehicle did carry on an economic activity, as it was doing more than 'the mere acquisition and holding of shares' - it was not acting as a private investor. The Tribunal held that, as a fact, the bid vehicle was conceived and operated as the highest level of strategic and financial direction for the target business.

It held that there was no intention of the bid vehicle to make taxable supplies at the time that it incurred the VAT. Nonetheless, the Tribunal considered that the ECJ judgment in Faxworld required that the taxable supplies of the Taxpayer's VAT group should be imputed to the bid vehicle. Thus the necessary 'direct and immediate link' to taxable supplies was present.

The Tribunal therefore allowed the Taxpayer's appeal.

The decision is available on the BAILII website via this link.

Comment

This is the latest in the line of cases in which HMRC has attempted to restrict VAT recovery on deal costs. Businesses should be aware that this is an area where HMRC has a concerted approach to challenge deduction and, whilst in they have been unsuccessful both this case and in

the MyTravel case, it is understood that HMRC has appealed the My Travel decision and it would not be surprising if HMRC also sought to appeal this decision.

The VAT treatment of M&A transactions, whether share or asset acquisitions or disposals, remains a matter of some uncertainty and businesses may wish to take appropriate advice about how best to protect their position with respect to historic or planned transactions.

To discuss how this decision may impact your business, please contact 4 Eyes Ltd.

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