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Deduction of input VAT on abort costs

On 3 May 2018, Advocate General ("AG") Kokott delivered her opinion in the Ryanair case (C-249/17) concerning the deduction of input VAT on costs incurred in relation to an unsuccessful acquisition of a company's entire share capital.

Background

Ryanair, an airline company established in Ireland, intended to take over a competitor, the Irish airline Aer Lingus. The takeover failed due to competition law issues. However, Ryanair requested the deduction of the input VAT on costs related to this failed acquisition, based on the intended economic activity, i.e. the supply of management services to Aer Lingus. Such deduction was rejected by the Irish tax authorities (the Revenue Commissioners) and after initial court proceedings, the case was brought before the High Court which referred the question of the input VAT deduction right for abort costs in a share deal to the European Court of Justice ("ECJ") for a preliminary ruling.

AG's opinion

In order to determine the input VAT deduction right of Ryanair, the AG does not refer to the reasoning of ECJ precedents but adopts a "functional" analysis and looks to the economic context of the intended takeover.

On this basis, beyond the mere acquisition of shares and the intended management activity, Ryanair is undoubtedly engaged in an operational activity as an airline company and it is only in this context that the Irish company envisaged acquiring a competitor, contrary to the situation of a pure holding company.

Therefore, by adopting this functional approach, the AG comes to the conclusion that abort costs in the share deal have a direct and immediate link with the income generated by the operational activity and any related input VAT incurred can be fully deductible.

Beyond the AG's opinion: clarification on the input VAT deduction right of active holdings?

Beyond the approach taken by the AG in this case, its reasoning raises some interesting points concerning the determination of the input VAT deduction right for holding companies and concerning in particular the question of (dis) proportion between the costs incurred and the turnover generated by the supply of management services for a holding company.

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In this context, the AG recalls that the case law does not limit this input VAT deduction right despite the disproportion and rejects the proposal from the European Commission to limit this input VAT right in relation to the acquisition of shares in proportion to the income generated by the supply of management services. Indeed, according to her, the determination of this proportion raises many issues in practice and might affect the VAT neutrality principle.

This statement should however be mitigated in view of the context of this case while awaiting the final decision of the ECJ. Indeed, as underlined by the AG, Ryanair does not constitute a pure holding company but on the contrary carries out an operational activity which already entitles it to an input VAT recovery right.

At the level of Luxembourg, the conditions of the input VAT deduction right of holding companies are often questioned and the above-mentioned AG's analysis might constitute an additional element to consider when determining the extent of such right.

The release of the ECJ judgement in this context should therefore be closely followed.

Your Arendt VAT team is at your disposal should you wish any further information in this respect.

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