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By PwC Deutschland | 14 March 2011

No input tax deduction on sale of less than full share capital

The Supreme Tax Court has held that the sale of less than 100% of the share capital of a subsidiary cannot rank as the sale of a business. The transaction is a VAT-free sale of shares and the input tax on the associated costs is not deductible.

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A company wished to divest itself of a subsidiary in order to gain cash for reinvestment in its core business. To this end, it sold its holding to a US company under an agreement allowing that company to determine later the exact (related-party) buyer. In the event, the buyer named its German subsidiary as the immediate contract partner, apparently to enable an *Organschaft* with a view to pooling German profits and losses. However, the company could sell only 99% of the shares as the other 1% were held by a third party with no direct involvement in the transaction. In the course of the sale, the company took structuring advice from a lawyer and financial advice from a banker. Both consultants charged VAT on their bills and the tax office refused an input tax deduction in both cases.

The company appealed successfully to the lower tax court, but has now lost its case before the Supreme Tax Court. The legal and financial consultancy charges were incurred in connection with a tax-free sale of shares. The related input tax was therefore not deductible. The sale of a 99% holding could not be equated with the non-taxable sale of a business (assets sale) as the sale of a business implied the full transfer of ownership rights. Thus, only a full transfer of all the shares could achieve equal status. In theory, it would be possible to treat the transfer of the shares held in an *Organschaft* subsidiary as the sale of a business, but only if the purchaser entered the transaction with the firm intention of forming its own *Organschaft*. This, however, was not the case here, given that the ultimate purchaser had deliberately left open the exact identity of the acquisition vehicle. As a last resort, the company tried to argue that its reason for the sale was to gain cash to finance further investment in its core business. The purpose of the transaction was thus to fund the expansion of taxable activities. To this, the court replied that the purpose as stated only led to an indirect connection with the expenses at issue. The direct connection was to the tax-free share transfer. This remained the determining factor for the denial of input tax deduction.

Supreme Tax Court judgment V R 38/09 of January 1, 2011 published on March 9

Keywords

Sale of shares, sale of assets, sale of business