Input tax: Holding companies

The deductibility of input tax incurred by group holding companies is often contentious. This article provides a brief overview of a recent case where the tax court in Cape Town considered a holding company's entitlement to deduct input tax in respect of services. The dispute centred around the nature of the holding company's enterprise and the connection between the services acquired to this enterprise.

Vendors may deduct input tax on goods or services acquired for purposes of making taxable supplies in the course of furtherance of their enterprise. This article considers a recent tax court judgment (case 1922) that dealt with input tax deducted by a group holding company.

Facts

The taxpayer is ZAW, a VAT vendor and listed company. It held shares in various operating subsidiaries, locally and abroad.

ZAW raised capital through a rights offer to residents and non-residents to repay a bridge facility that it used to fund the acquisition of the shares of an Australian department store. ZAW procured services from local and foreign providers to arrange and execute the facility and rights offer. It claimed input tax on the raising fees incurred in respect of the shares issued to non-residents, a zero-rated taxable supply.

Dispute and arguments

SARS disallowed this input tax deduction because the services were not acquired to make taxable supplies in the course of furtherance of ZAW's enterprise. ZAW's trading activities were not to issue shares. It also seems as if SARS contended that the services relating to capital raising were not sufficiently closely related to the management services (taxable supplies) that ZAW rendered to subsidiaries.

ZAW described its enterprise as a listed, active investment holding company as acquiring and holding investments, capital management of those investments, and providing financial and management services to its investment subsidiaries. Raising capital, as an aspect of capital management, is an integral element.

The dispute essentially centred around ZAW's enterprise as a group holding company and the connection between this enterprise and the capital-raising services.

Holding company's enterprise

SARS relied on the De Beers case, where the SCA concluded that services in connection with a takeover transaction were unrelated to and did not contribute to the taxpayer's enterprise of mining, marketing and selling diamonds. The tax court concluded that ZAW's case is distinguishable. It considered the provision of financial and management services to its subsidiaries for remuneration as an integral part of ZAW's business. Relying on *Consol Glass (Pty) Ltd v CSARS,* the tax court concluded:

> 'Taxpayer ZAW's actions in expanding its business and incurring costs, both local and foreign, in the course thereof has a functional link to the making of its VAT taxable supply of management services to its subsidiaries and that the expenses incurred in this regard were incurred wholly for the purpose of consumption, use or supply in the course of supplying goods and services (taxable supplies) and in the course or furtherance of its enterprise'

The judgment provides support for holding companies deducting input tax in connection with management services they render. It further recognises that the enterprise in question may consist of an integrated set of activities involving shareholding and related group financing.

Although not considered in this case, the judgment could also be relevant to questions about the deductibility of input tax in respect of raising costs more broadly. This topic in itself is contentious.

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