

# Transaction Costs

Dutch CIT, VAT and tax accounting

# Introduction

- Watched live, this webinar qualifies for 1 PE point
- The button '**[Ask a question]**' allows you to ask a live question via chat
- Any other questions via your PwC advisor or fill in the form on [\*\*pwc.nl\*\*](https://pwc.nl)
- View this webcast or presentation at a later stage
- Slides will become available afterwards
- Evaluation form afterwards



# Agenda

1. Introduction
2. CIT
3. VAT
4. Tax accounting
5. Wrap-up



# 1

## Introduction

# Why? Limitation of deductibility

TenneT supports steps towards possible German State participation in TenneT

**JDE Peet's Announces Its Intention to Launch an Offering and List on Euronext Amsterdam**

KKR to invest \$750m in cosmetics maker Coty

PE firm takes step towards buying majority stake in group's beauty and haircare unit

Johnson & Johnson to buy biotech Momenta in \$6.5bn deal

Relx continues deal spree

Just Eat Takeaway combines with Grubhub in \$7.3bn deal

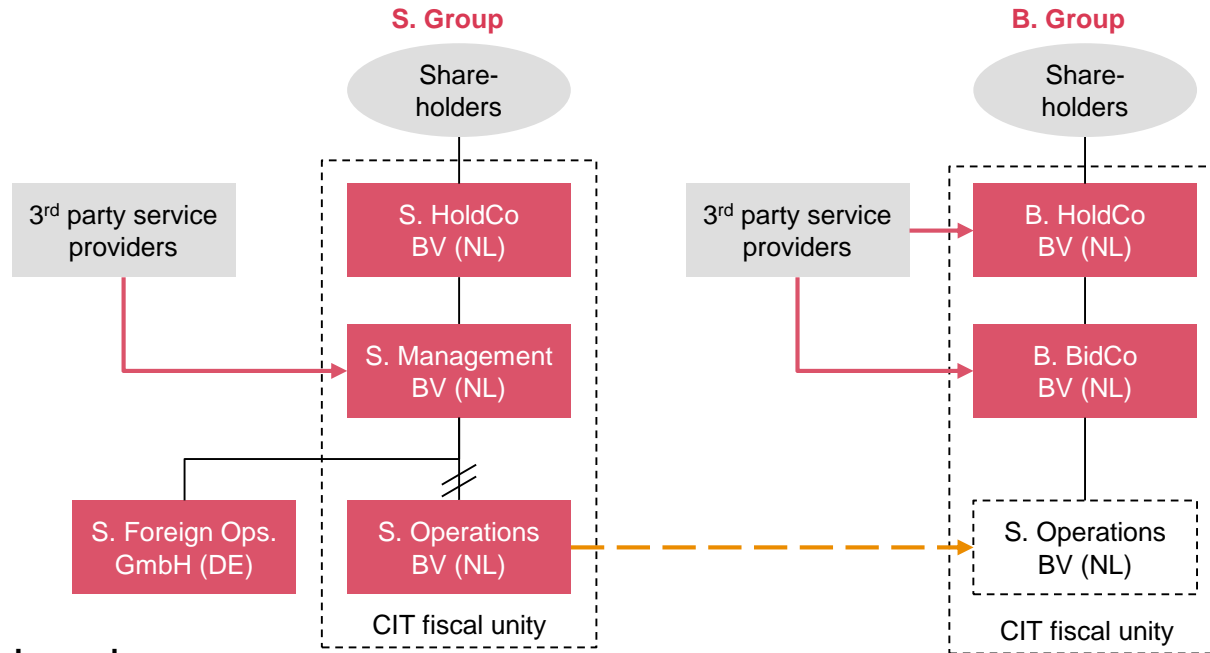
“

Would it be better to just wait one year after every transaction? Yes, sure. We'd get more sleep. But that's just not how the world turns

Jitse Groen, Just Eat Takeaway chief executive



# Sample case



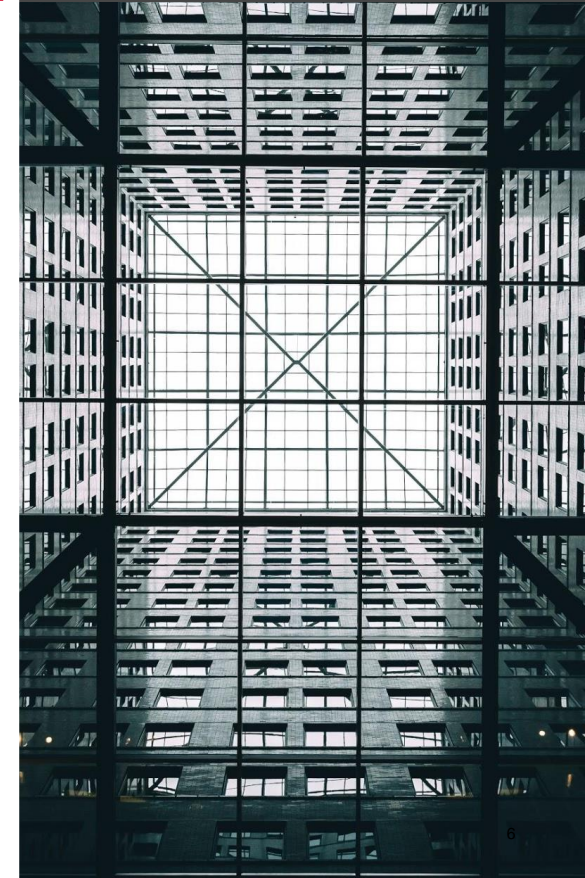
## Legend



Provision of transaction services (e.g. advisory, legal and financing costs)



Sale of S. Operations BV's shares (by S. Management BV to B. BidCo BV)



# Transaction costs

## Seller

- Restructuring / Carve-out costs
- Corporate Finance advisor (e.g. for identifying buyers)
- Setting up + hosting a virtual data room
- Vendor Assistance / Vendor Due Diligence report, e.g.:
  - Commercial
  - Financial
  - Legal
  - Tax
- Share Purchase Agreement services

## Buyer

- Due diligence investigation, e.g.:
  - Financial
  - Tax
- Structuring fees
- Share Purchase Agreement services
- Costs for attracting financing
- Warranty and indemnity (W&I) insurance
- Developing Management Incentive Plan
- Post-deal integration services
- Purchase price allocation





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Corporate Income Tax

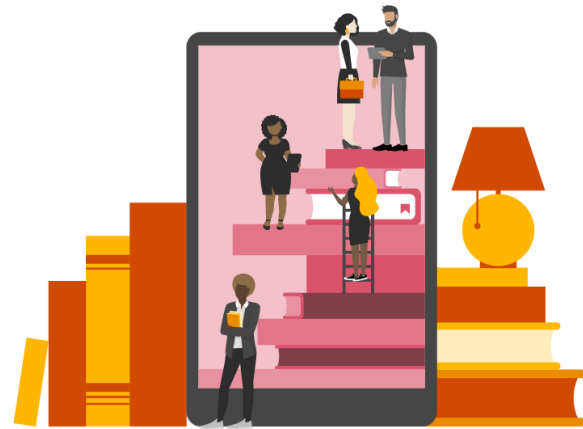
# Corporate income tax

## Legal framework

- Article 13 sub 1 Dutch CIT Act:

*In determining the profit, the benefits from a participation as well as **the costs related to the acquisition or disposal of that participation, are not taken into account** (participation exemption).*

- Step 1 - Allocation to **the relevant taxpayer** (transfer pricing rules)
- Step 2 - Type of transaction costs:
  1. Acquisition costs / selling costs
  2. Financing costs
  3. Mixed costs
  4. Other costs
- In practice, grey area and no clear view of the Dutch tax authorities



# Corporate income tax



## Selling and acquisition costs

- Directly related to the sale of shares (i.e. there is direct causality between the sale/acquisition of shares and the costs incurred)
- Not deductible
- Acquisition costs are capitalised as part of the cost price of the acquired shares
- Decision Dutch Supreme Court 7 December 2018
  - Only costs related to the actual acquisition or disposal of a specific participation.
  - Both internal and external costs
  - Transaction not yet taken place: accrual at year-end
- Decision Dutch Referral Court Den Bosch 17 October 2019

# Corporate income tax



## Financing costs

- Directly related to obtaining debt financing
- Deductible at the moment the financing is attracted or capitalised and amortised over the term of the loan
- Decision Court Noord-Holland 10 February 2020



## Mixed costs

- Costs related to both the acquisition of shares and the financing
- Partly deductible, practical approach
- Decision Court Noord-Holland 10 February 2020



## Other costs

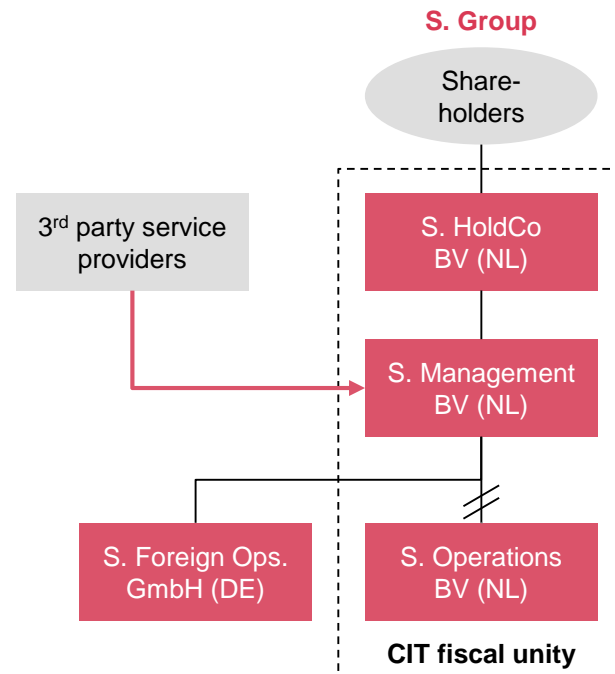
- Other costs frequently made in a transaction process: corporate body costs, implementation of a management incentive plan, a restructuring post acquisition

# Poll 1 - Seller transaction costs

## Questions

Costs • Strategic orientation

Which entity should bear these costs and what is the qualification of the costs?



### Legend

→ Provision of transaction services (e.g. advisory, legal and financing costs)

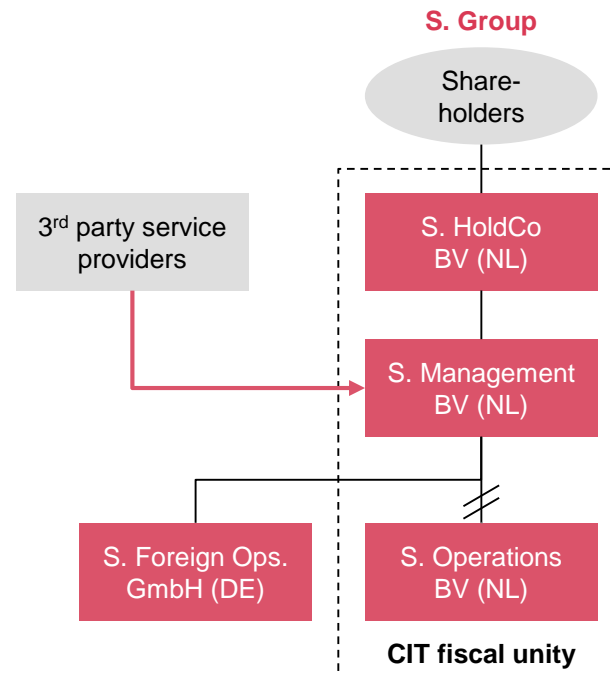
# Poll 2 - Seller transaction costs

## Questions

### Costs

- Bonus to S. Operations BV (Target)'s employees for specific activities in relation to the acquisition

What is the qualification of the costs?



### Legend

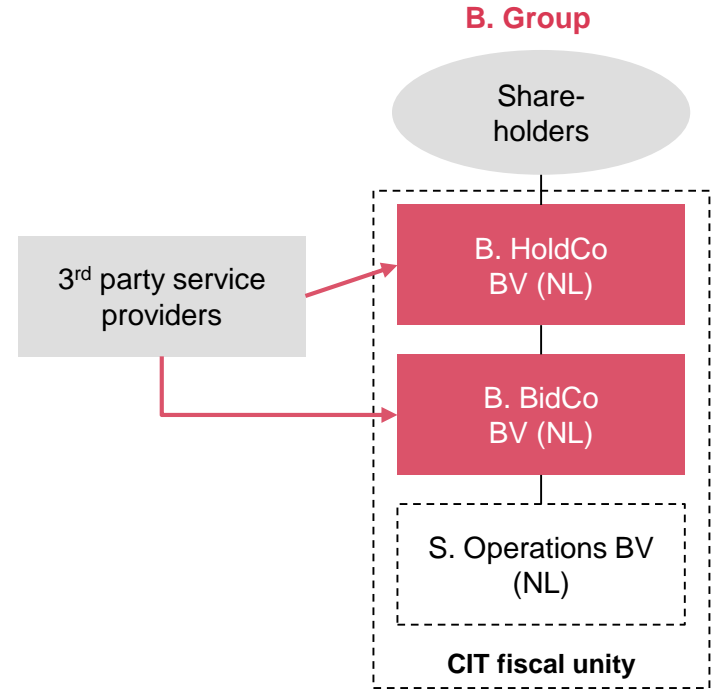
→ Provision of transaction services (e.g. advisory, legal and financing costs)

# Poll 3 - Buyer transaction costs

## Questions

Costs • Internal M&A department buyer

Which entity should bear these costs and what is the qualification of the costs?

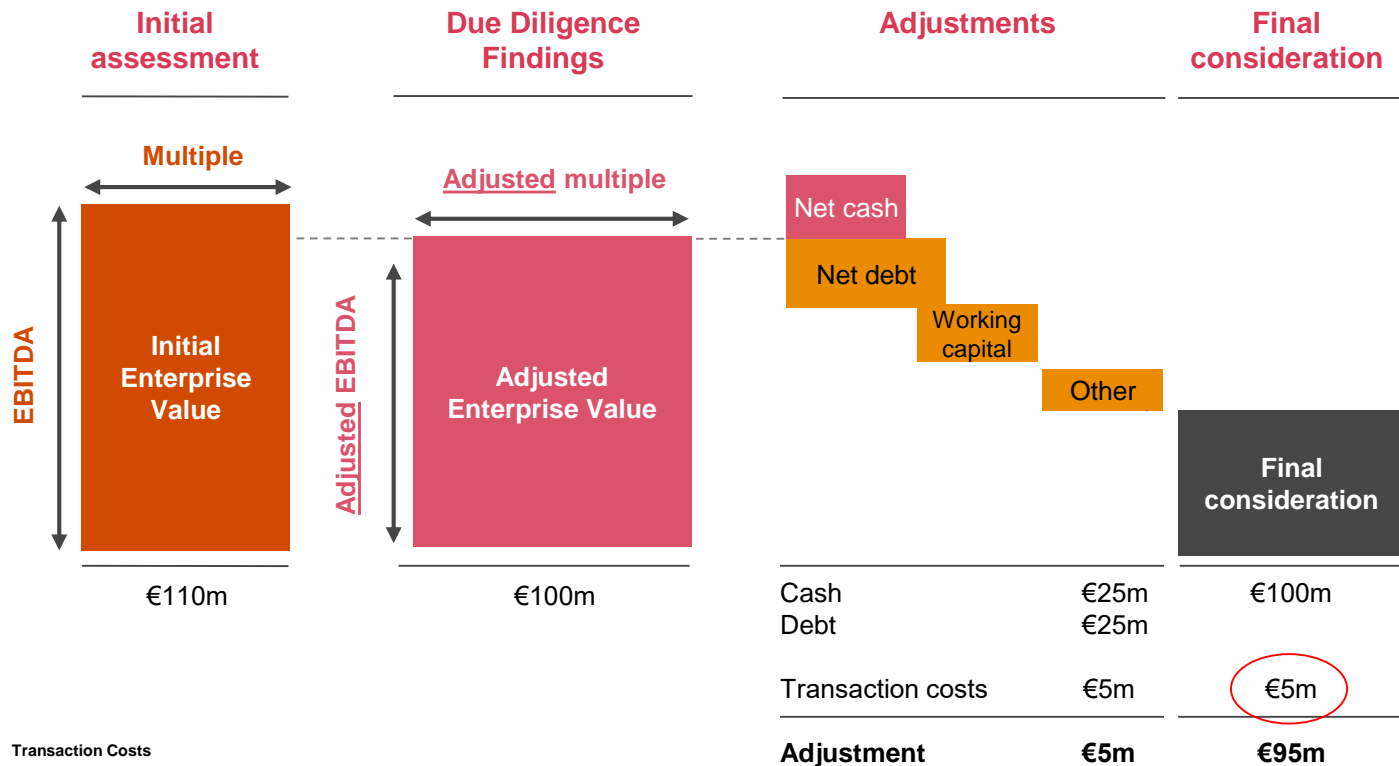


### Legend

→ Provision of transaction services (e.g. advisory, legal and financing costs)



# Practical impact on the deal



- Net or gross deduction of Transaction costs
- Conduct in SPA
- Agree on treatment between signing and closing.
- Gross up clause in W&I policy

=====  
Incorrect TP allocation?  
↓  
Risk of deemed dividend

# Poll 1 - Seller transaction costs

Answer - Strategic orientation

- A) S. Operations BV (Target) & Other costs
- B) S. Management BV (Seller) & Selling costs
- C) S. Operations BV (Target) & Selling costs
- D) S. Management BV (Seller) & Other costs

# Poll 2 - Seller transaction costs

Answer - Bonus to Target employees specific activities for the acquisition

- A) Acquisition costs
- B) Other costs

# Poll 3 - Buyer transaction costs

Answer - Internal M&A department buyer

- A) S. Operations BV (Target) & Other costs
- B) S. Operations BV (Target) & Mixed costs
- C) B. BidCo BV (Buyer) & Other costs
- D) B. BidCo BV (Buyer) & Mixed costs

# Important takeaways for CIT



## Pre deal

- **Discuss** the disposal / acquisition **steps** to be taken and the expected **costs** to be made



## Deal process

- **Document** which entity has what **benefit for each cost**
- E.g. document whether DD reports were condition for Buyer to obtain financing



## Information availability

- **Availability** of **engagement letters** and **invoices** at the company benefiting from the costs



## Tax authorities

- **Mapping** of costs less obvious to allocate
- Discussions with **Dutch tax authorities**

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VAT



# VAT 101 - quick refresher

## Recovery of VAT - basic principles

- EU VAT is an indirect tax on consumption (not on production, revenue, profit, etc.)
- Entrepreneurs serve as tax collectors between consumers and the tax authorities
- Entrepreneurs can therefore recover **input** VAT, but only to the extent it's linked to VAT taxed **output**
  1. Input directly attributable to VAT taxed output = recovery
  2. Input directly attributable to VAT exempt output = no recovery
  3. Input attributable to both VAT taxed and VAT exempt output = pro rata recovery

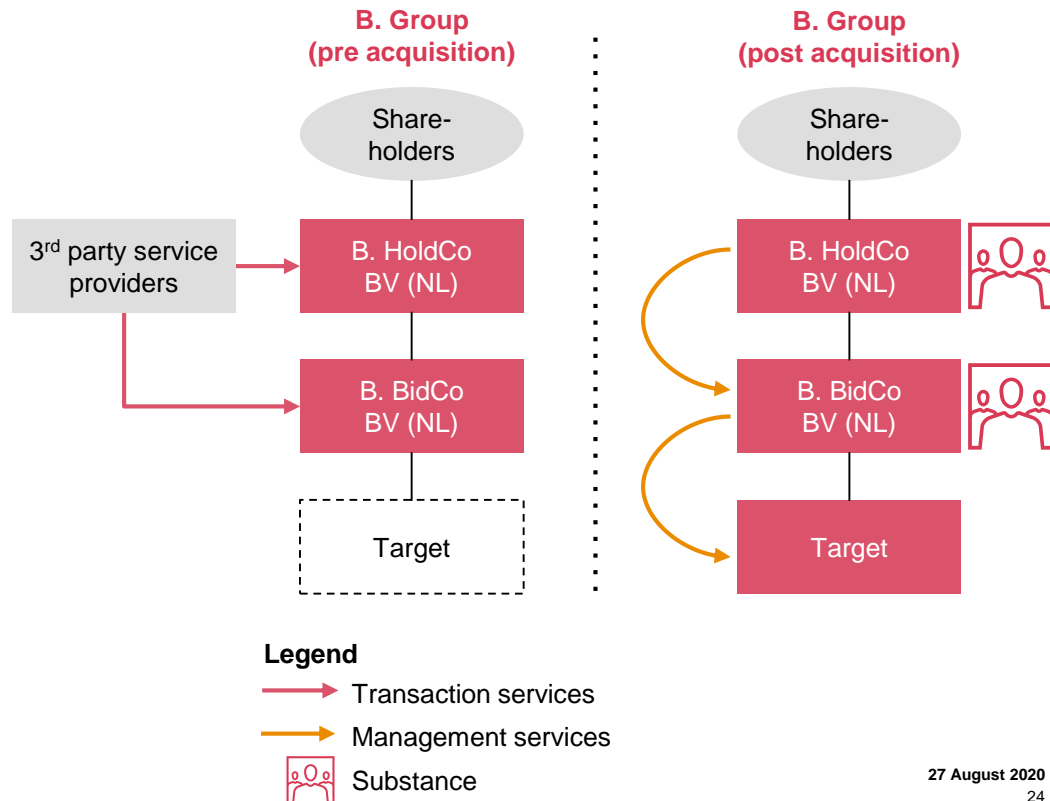


# Acquisition costs

## VAT consequences for buyer

### Steps plan for buyer

1. Determine which entity engages 3rd party service providers
2. Determine if that entity is a VAT taxable person and if not, determine what is needed to become a VAT taxable person
3. Further substantiate this position with substance and documentation
4. Determine the VAT recovery
5. Consider if on-charging costs is required and if so, determine the best method



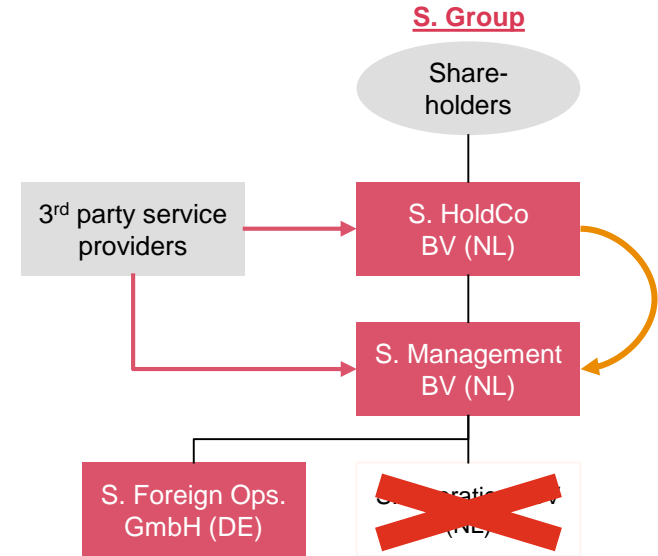
# Acquisition costs

## VAT consequences for seller


### Steps plan for seller

In principle, no VAT recovery!

1. Determine if the Target is an actively held subsidiary
2. Determine the aim of the share disposal
3. Determine the VAT recovery ratio
4. Consider if on-charging costs is required and if so, determine the appropriate method



#### Legend

- Transaction services
- Management services
-  Substance

# Important takeaways for VAT



## VAT taxable person

- Substantiate the VAT position, especially for holding entities!



## VAT taxed output = Input VAT recovery

- Not every type of output leads to VAT recovery



## Legal relationship vs. Economic reality

- In principle: engagement letters + invoices are leading,
- but 'substance over form' when conduct is not in line with economic reality.
- Case law is interpretable, so expect discussions!



## Timing

- Start with the steps before the transaction takes place

# Agenda

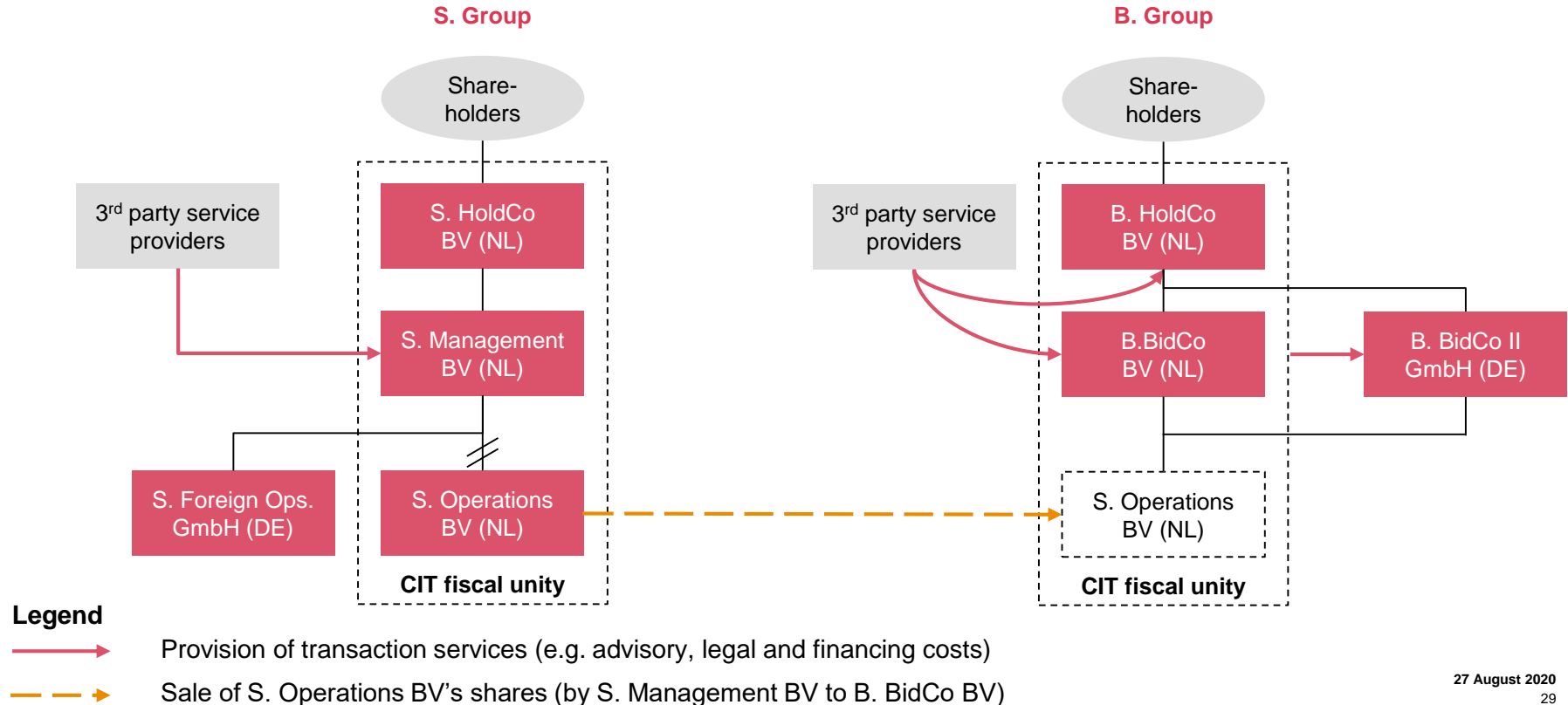
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# 4

Tax accounting

# Sample case with a twist





# Impact on financial statements (1) - Acquisition expenses

## Impact non-deductible expenses year 1:

Profit before tax	1,000
Expected tax charge	250
Tax effect non-deductible expenses	50
Total tax expense	300
Effective tax rate	30%



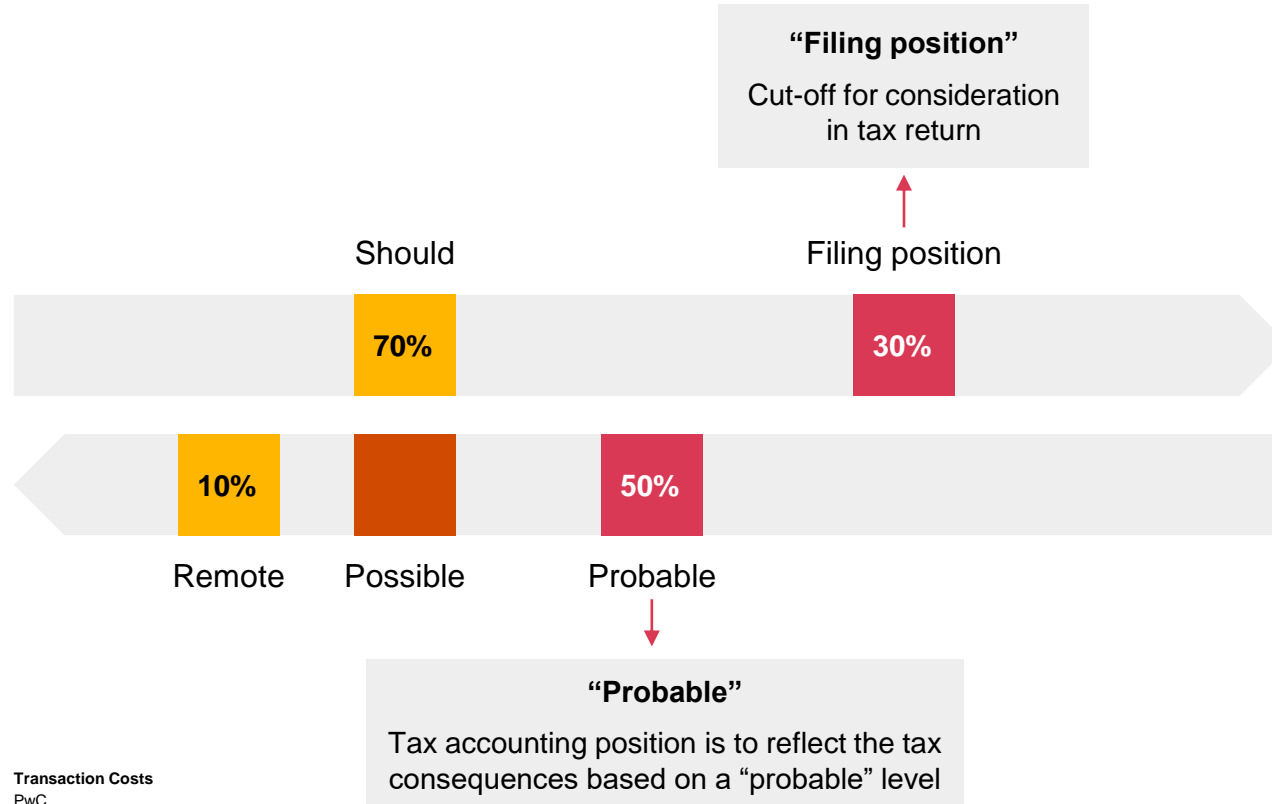
# Impact on financial statements (2) - Acquisition expenses

## Impact non-deductible expenses year 2:

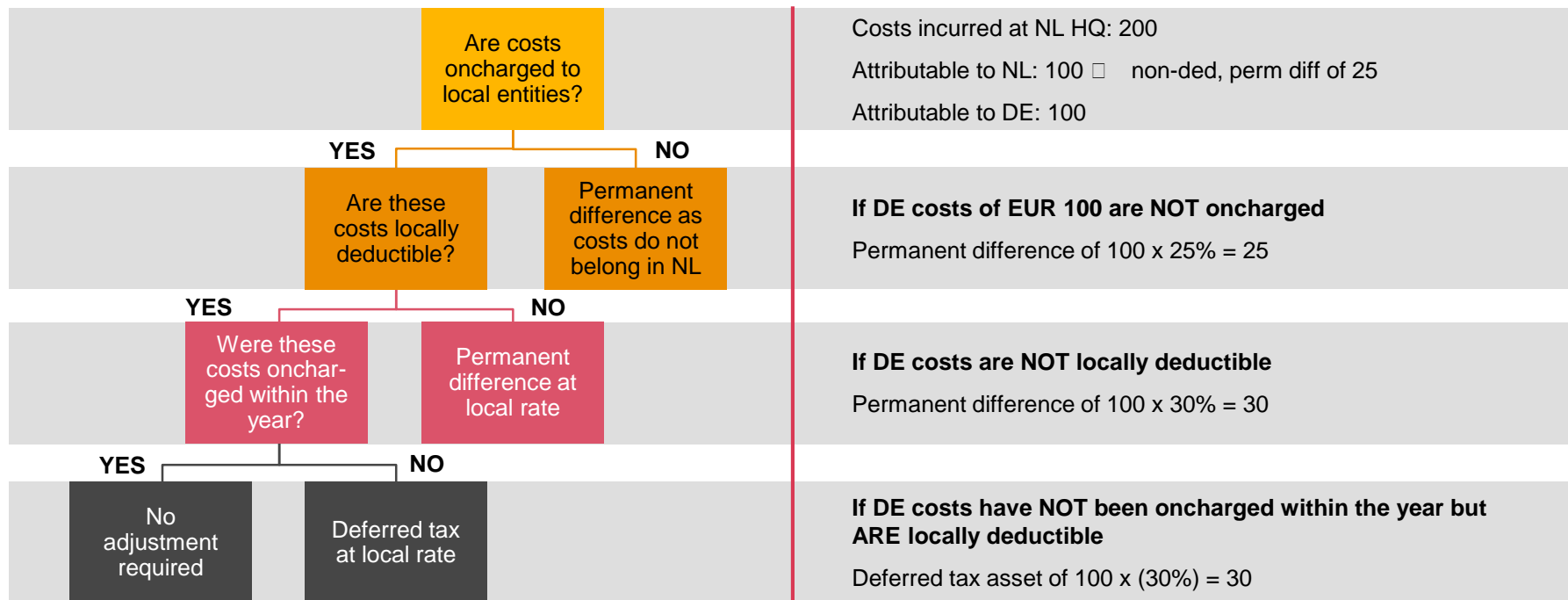
Profit before tax	1,000
Expected tax charge	250
Tax effect non-deductible expenses	(25)
Total tax expense	225
Effective tax rate	22.5%



# Uncertainty on deductibility



# Oncharge of acquisition costs



# Allocation between buckets: Accounting versus tax (1 of 2)

## Example 1

**Costs: EUR 1,000**

**Accounting:** Finance costs, activated in balance sheet, depreciated in 4 years

**Tax:** Acquisition costs, activated in balance sheet

### Year 1

PBT	EUR 3,750
<u>Adjustment depreciation</u>	<u>EUR 250</u>
Taxable amount	EUR 4,000
Current tax charge (25%)	EUR 1,000
Deferred tax charge	EUR 0
Total tax charge	EUR 1,000
ETR	26,7%

- Accounting **qualification** of costs as acquisition, financing costs or mixed/other is not always equal to qualification for tax purposes;
- Accounting **treatment** of acquisition and financing costs is not always equal to treatment for tax purposes.



# Allocation between buckets: Accounting versus tax (2 of 2)

- Accounting **qualification** of costs as acquisition, financing costs or mixed/other is not always equal to qualification for tax purposes;
- Accounting **treatment** of acquisition and financing costs is not always equal to treatment for tax purposes.

## Example 2

**Costs: EUR 1,000**

**Accounting:** Finance costs, considered through P&L in Y1

**Tax:** Finance costs, activated in balance sheet, depreciated in 4 years

### Year 1

PBT	EUR 3,000
<u>Adjustment finance costs</u>	<u>EUR 750</u>
Taxable amount	EUR 3,750
Current tax charge (25%)	EUR 937
Deferred tax charge/(benefit)	EUR (187)
Total tax charge	EUR 750
ETR	25%



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# Questions & Answers



# Wrap-up

ALLOCATION - important (but slightly different) for all perspectives

- **CIT:** Treatment of transaction costs is not straightforward and still crystallising.
- **VAT:** Form over substance, as long as it is aligned with economic reality
- **Tax accounting:** Uncertainties and differences in accounting qualification and treatment versus tax, can make the correct impact on the financial statements a tricky business.

TIMING - Involve all disciplines from the start



# Closing

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# Evaluation

- How would you rate this webinar on a scale from 1 to 10?
- The content was relevant. (Totally agree/Agree/Neutral/Disagree/Totally disagree)
- Do you have any suggestions and/or comments?
- Do you have specific questions and would you like us to contact you?



# Thank you

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