



KMLZ VAT NEWSLETTER

Allocation of purchased goods and services to the business

On 2 January 2014 the Federal Ministry of Finance issued a 62 page long notification in which it specified the principles for the allocation of goods and services to the business and thereby amending sec. 15.2 para 1 of the German Administrative Circular.

1. Allocation rules

Taxable persons can purchase goods and services (i) solely for business purposes or (ii) for non-business purposes or (iii) partly for business purposes and partly for non-business purposes. With regard to non-business activities, a distinction has to be made between non-economic activities (e.g. sole administration of holdings) and private activities (e.g. use for private purposes). A taxable person is only entitled to an input VAT deduction if the purchased goods or services are used for business purposes. According to the intended use, the following allocation rules are applicable:

- If the goods or services are used solely for business activities, these have to be allocated solely to the business.
- If the goods or services are used solely for non-business activities, allocation to the business is not permitted.

Allocation principles for input VAT deduction

A taxable person is only entitled to an input VAT deduction with regard to goods and services purchased for business purposes. In its notification dated 2 January 2014, the Federal Ministry of Finance stipulates the general allocation principles to the business. In particular, with regard to construction work, the allocation to the business has to be executed by 31 May of the following year. Otherwise, there is a risk that the input VAT cannot be deducted.

- If goods or services are purchased partly for business purposes and partly for non-business purposes, the taxable person has to allocate the said goods or services according to their intended use. If a taxable person intends to use an object partly for business purposes and partly for non-economic purposes, it also has to allocate the said object according to its intended use.
- If a taxable person intends to use an object partly for business purposes and partly for private activities, it has the following options:
 - Allocate the object solely to its business
 - Allocate the object solely to its private sphere
 - Allocate the object according to its use for business purposes to the business.

The use for business purposes must amount to a minimum of 10%. If it does not, allocation to the business is not permitted.

2. Allocation key

If goods or services are purchased partly for business purposes and partly for non-business purposes, the allocation key stipulated in sec. 15 para 4 of the German VAT Act can



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be used. Here, the taxable person has to estimate the appropriate portion of the use for business purposes. With regard to buildings, the calculation based on the ratio between the area of the premises allowing for VAT deduction and that of the premises not allowing for VAT deduction is regarded as appropriate. The allocation according to economic criteria is only applicable if the areas of the premises are not comparable. This is e.g. the case with regard to photovoltaic facilities. In this case, the proportion between the (fictitious) rent fees for the roof area and the area of the rest of the building can be applied as the allocation key.

3. Allocation object

The taxable person has to make an allocation decision with regard to each supply purchased. An allocation decision has to be made when an object is acquired or constructed as well as with regard to expenditures necessary for the maintenance of the object. Construction costs which occur after the object is established are regarded as a separate allocation object. The construction costs which occur if an established building is extended have to be allocated according to the intended use of the new part of the building. If the construction period takes more than a year, the intended use for the later established object at the point in time when the first supply is purchased, is decisive for the allocation. Objects such as e.g. photovoltaic facilities, block heating works and operating facilities, are considered to be separate allocation objects, even if they are primarily regarded as essential parts of the respective building.

4. Documentation of the application decision

In the case where the taxable person can choose either to allocate the object solely to his business or solely to his

private sphere or according to its use for business purposes, the allocation decision has to be made at the point in time when the first supply is purchased.

4.1 Input VAT deduction by 31 May

To claim the input VAT deduction is a substantial indication for the allocation to the business. In order to prove the allocation to the business, it is necessary to deduct the input VAT via the annual VAT return by 31 May of the following year, at the latest. It is possible to correct any allocation decision made up until 31 May of the following year. Any extension of the deadline to file the annual VAT return does not extend the deadline for the allocation decision.

4.2 Other evidence

Only in cases where an input VAT deduction is not possible, other evidence can be used to prove the allocation decision. An acquisition or sale using the company name, the company insurance of an object or the accounting treatment can all be regarded as indications for the allocation to the business. If an input VAT deduction is not possible when acquiring or constructing a building, the taxable person can file a written statement with the tax authorities in which it is documented, to what extent, the building is allocated to the business. This written statement also has to be received by the tax authorities by 31 May of the following year, at the latest.

In particular, if the construction work takes a few years, the deadline regarding the documentation of the allocation decision as per 31 May of the following year has to be considered. Otherwise, it is assumed that the object is not allocated to the business with the consequence that the input VAT deduction for all purchased goods and services is denied until a new allocation decision can be made.