



Further transitional regulation for legal entities under public law

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1 Extension of transitional regulation for sec. 2b of the German VAT Act by 31.12.2024

For the past seven years, legal entities under public law have been struggling with the transition to the new regulation of sec. 2b of the German VAT Act. A few have managed the changeover well. Most, however, failed to meet the (original) deadline. The changeover to the new VAT regime for the public sector was supposed to be completed by 31.12.2022. Now – at the last minute – the legislator has provided for a further transitional regulation of another two years by virtue of the Annual VAT Act. Legal entities under public law will now have had no less than 9 years to implement a single VAT provision. This is an unprecedented event in German VAT legislation.

Most representatives of the public sector are grateful for the two-year postponement. So are we as VAT consultants, since the need for advice is enormous. In most cases, it is more about the organisation of accounting and the implementation of tax compliance structures than about substantive questions regarding sec. 2b of the German VAT Act.

While the last extension was justified on the grounds of the COVID-19 pandemic, the legislator is now a little more earnest. According to the legislator, there are many open questions that lead to great uncertainty and overall fuel doubts that an accurate taxation of the public sector can be ensured nationwide by 01.01.2023. In addition, the legislator claims, inter alia, that based on the experience of the last two years, there is no reason to fear a significant impairment of competition as a result of the renewed extension of the transitional regulation. This is surprising. Was the implementation of the new regulation seven years ago not originally intended to protect competition? This raises the legitimate question whether sec. 2b of the German VAT Act is required at all. We may already be curious about the legislator's considerations in the future.



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2 Recommendations for the practice

In the vast majority of cases, legal entities under public law would do well not to prematurely apply sec. 2b of the German VAT Act. This might not be the case only if there is a considerable amount of input VAT that would otherwise be forfeited. In most cases, a board resolution will not be required to make use of extended transitional regulation, as the public entities will merely continue to use the originally declared option to the old regulation of sec. 2 para. 3 of the German VAT Act.

If extensive arrangements have already been made for the changeover on 01.01.2023, everything must now be put on hold and adjustments that have been carried out must be considered in the light of the old regulation of sec. 2 para. 3 of the German VAT Act:

- Contract adjustments may have to be made again (gross/net price agreement; risk regarding sec. 14c of the German VAT Act),
- Changes to the invoicing systems may lead to the need for further corrections, and
- Applied-for tax numbers (especially for organisational units of federal and state authorities) must be deleted again.

Nevertheless, it is recommended that work on the issue be continued at full speed. The time that has been bought must be used and the following work must be pushed ahead quickly, as a matter of priority:

- Finalisation of the so-called revenue analysis with proper documentation of all details and ongoing further development in the form of a "test phase" for the time when sec. 2b of the German VAT Act applies,
- Development of a functioning invoicing system with sufficient (secure) interfaces,
- Completion of the contract analysis and ongoing further development ("test phase") for the time when sec. 2b of the German VAT Act applies,
- Solving cases of cooperation with the means of the expense pool, the VAT group (see KMLZ VAT Newsletter 50 | 2022) or the arrangement as a cost sharing group according to sec. 4 no. 29 of the German VAT Act,
- Application for binding tax rulings (including an application to waive the fees!),
- Implementation of tax compliance structures and creation of a VAT law organisation,
- Determination of input VAT volumes and, if necessary, calculation of pro-rata shares (see also the draft of the Federal Ministry of Finance dated 25.10.2022).

Many transition projects have shown that errors might have occurred in the past or that a VAT assessment was made incorrectly. In these cases, the necessary corrections must be made in a timely manner, irrespective of sec. 2b of the German VAT Act, taking into account aspects of the German Fiscal Code.

3 Introduction of so-called cash accounting scheme

The Annual VAT Act 2022 enables legal entities under public law to apply for the calculation of VAT on the basis of the remuneration received – regardless of turnover limits. The prerequisite is that the legal entity under public law does not voluntarily keep records and does not regularly prepare financial statements based on annual inventories or is legally obliged to do so. According to reports, the term "insofar as" should not be interpreted too narrowly. The obligation to keep records for an individual operation of a commercial nature ("BgA") or an owner-operated municipal undertaking ("Eigenbetrieb") will probably not infect the entire municipality. The change was long overdue, as many legal entities under public law, such as churches, the federal and state governments use a specific ("cameralistic") accounting method.