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Federal Fiscal Court: Input VAT allocation for mixed-use buildings

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1   Background

In the case of mixed-use buildings, the input VAT deduction is only permissible to the extent that the goods and services purchased can be allocated to taxable supplies performed. In the case of the construction of buildings - in contrast to mere maintenance expenses - a direct allocation of the costs to the square footage used for taxable or VAT-exempt supplies is often not feasible. In the case of a mixed-use building's acquisition or construction costs, the deductible input VAT is therefore determined on the basis of the percentage of use of the building as a whole. The choice of the appropriate proportion standard has repeatedly been the subject of case law. Now, the discussion seems to have calmed down: In the present decision, the Federal Fiscal Court confirms its previous case law.

2   Facts

In 2009 and 2010, the claimant constructed a mixed-use building complex. In addition to a supermarket, which was leased out subject to VAT, the complex also contained a residential complex, which was leased out VAT-exempt. The claimant calculated its share of deductible input VAT according to the square footage used. Later, in the course of a tax audit, the tax office reduced this share.

The claimant objected to the tax office's decision and subsequently filed a lawsuit. It claimed that the object-related proportion according to the turnover was applicable due to the different equipment of the different parts of the building. This would lead to a higher input VAT deduction (48,27%). However, the tax court, considered the claimant to be bound by its original choice of the proportion according to the square footage.
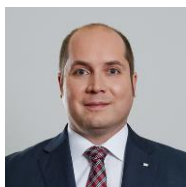
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3   Opinion of the Federal Fiscal Court

The Federal Fiscal Court now counters this finding of the tax court with its decision of 11.11.2020 (XI R 7/20). The choice of the proportion is generally incumbent on the taxpayer. However, the chosen proportion must correspond to an appropriate estimate within the meaning of sec. 15 para. 4 sentence 2 of the German VAT Act. In the case of an inappropriate proportion, the choice made is not binding. At a later stage - for example on the occasion of a tax audit - the taxpayer can change to a different proportion. In the opinion of the Federal Fiscal Court, the proportion according to the square footage was not appropriate in the present case, but rather, the object-related proportion according to the turnover. The Federal Fiscal Court considers the fact that the VAT return for the years in dispute, i.e. 2009 and 2010, were already formally final to be irrelevant.

The Federal Fiscal Court arrived at this result by interpreting sec. 15 para. 4 of the German VAT Act in conformity with the EU VAT Directive: In the case of the construction and acquisition of mixed-use buildings, according to case law and the tax authorities, the proportion according to the square footage is generally applied (Federal Fiscal Court decision of 16.11.2016 - XI R 31/09). Under national law (sec. 15 para. 4 sentence 3 of the German VAT Act) the proportion according to the turnover can only be applied if no other economic allocation is possible. EU law (Art. 173 para. 1 subpara. 1 and para. 2 letter c of the EU VAT Directive) provides for the global object-related proportion according to the turnover as a regular principle. In its landmark decision in the *BLC Baumarkt* case (C-511/10), the ECJ resolved this tension as follows. The application of the proportion according to the square footage is permissible if it allows for a more precise determination than the object-related proportion according to the turnover. In its case law, however, the Federal Fiscal Court is now in fact largely pushing back the proportion according to the square footage. According to the case law of the Federal Fiscal Court, this is at least not the more accurate method of apportionment if there are considerable differences in the equipment of the rooms used for different purposes (see also sec. 15.17 para. 7 sentence 6 of the Administrative VAT Circular). In this case, the goods and services purchased are not distributed evenly over the different parts of the building. Therefore, the object-related proportion according to the turnover is to be used to allocate the input VAT.

Incidentally, the Federal Fiscal Court confirms the "one-pot" theory in its decision. There is still a two-tier division. While goods and services purchased for use, maintenance and upkeep are, in principle, to be directly and immediately allocated to the various supplies performed, the goods and services purchased for construction and acquisition are to be collected in a single pot and allocated on a percentage basis in accordance with sec. 15 para. 4 of German VAT Act.

4   Consequences for the practice

In many cases, rooms used for different purposes will have different equipment characteristics - such as varying ceiling heights, wall and ceiling thickness and with regard to interior fittings. The present decision therefore opens up a de facto right of choice to the taxpayer in the instance where the proportion according to the square footage proves in retrospect to be inappropriate. It is not the taxpayer who has to prove that the object-related proportion according to the turnover is more precise than the proportion according to the square footage in an individual case. Rather, the tax authorities are only allowed to apply the proportion according to the square footage if it allows a more precise allocation.

Insofar as there are indications of different equipment, taxpayers can now check whether a change in the proportion is worthwhile. If the VAT assessment has not yet become substantively effective the original choice of the proportion according to the square footage can also be revised retroactively where the originally chosen proportion was not appropriate. As regards when the differences in the equipment are so significant that they conflict with the proportion according to the square