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VAT NEWSLETTER

VAT treatment of community of part owners

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1 Background

To date, the following situation has applied: Communities of part owners can also constitute taxable persons, in terms of the VAT Act (see Art. 2.1 para 2 sentence 2 of the German VAT Circular). One of the Federal Fiscal Court decisions, which characterises the way in which communities of part owners are dealt with, is a decision from 2001 (V R 42/89). A married couple purchased salesrooms together and subsequently rented the premises out. In the absence of a specific agreement, the letting of co-ownership by a community of part owners is deemed to be an administrative measure in accordance with secs. 744 & 745 of the German Civil Code. The Federal Fiscal Court decided that such a marital community can be a treated as a single taxable person, despite having no legal capacity. In subsequent decisions, the Court added, that a community of part owners will only be considered to be a taxable person, if it carries out transactions on its own behalf. However, if the community of part owners constitutes a mere purchasing community and makes the object of purchase available to its members free of charge, it is not a taxable person for VAT purposes.

2 New Federal Fiscal Court case law

With its decision of 22.11.2018 (V R 65/17), the Federal Fiscal Court threw everything overboard with the stroke of a pen. The Federal Fiscal Court decided that a community of part owners cannot be classified as a taxable person for VAT. The decision was based on the following facts: Together with other persons, the Plaintiff invented methods for the early detection of two types of tumours. The A-GmbH & Co. KG was granted contractual licenses to exploit the inventions and paid licence fees directly to the Plaintiff and the other inventors. In addition, A-GmbH & Co. KG issued self-billing invoices, which were addressed to the individual inventors. The Plaintiff reported its share of royalties as a sole proprietor and

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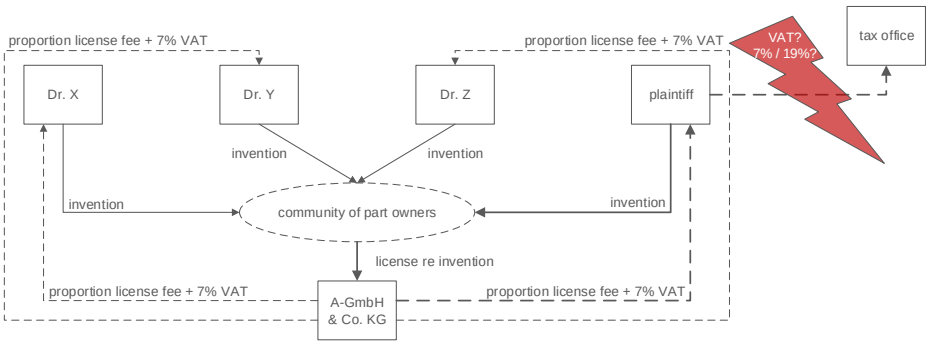
applied the reduced tax rate. The tax office subsequently questioned whether the revenue was, from a VAT perspective, to be allocated to the Plaintiff or to the community of part owners consisting of all of the inventors. There was also a dispute about the applicability of the reduced VAT rate.



In order to justify its decision, the Federal Fiscal Court stated that a community of part owners could not be involved in a legal relationship due to its lack of legal capacity. However, suppliers and recipients are determined on the basis of the underlying legal relationship. Thus, under civil law, neither a purchase of services nor a supply of services can be allocated to a community of part owners. The VAT Act follows this classification.

3 Consequences for the practice

The decision, the justification for which sounds simple and "somehow plausible", marks a real turnaround in case law with disastrous consequences for existing communities of part owners. While these communities of part owners were previously assumed to be economically active, the Federal Fiscal Court now tells us that this is not the case. As a result, all invoices issued to a community of part owners are incorrectly issued. This applies to both output transactions and input supplies. The relevant taxable person is not the community of part owners, but rather its individual members. They are entitled to input VAT deduction - provided that they have a proper invoice - and they must pay tax on the transactions, which are allocated to them. In addition, the community of part owners is liable for the payment of the relevant VAT in accordance with sec 14c of the German VAT Act. It is not entitled to any input VAT deduction.

For the tax authorities, it has now been proven that attempts to repair old "mistakes" may end up doing more harm than good. In 2008 (with a delay of 10 years!), the tax authorities reacted to two 1998 decisions of the V. Senate on the inability of a community of part owners to be the recipient of a supply by issuing a non-application decree (see Federal Ministry of Finance letter, Federal Tax Gazette. I 2008, 675). Whether this reaction is classified as a mistake or not: The tax authority will not be able to preserve its attitude and dealing with this change in case law will not become easier as time goes by. However, it is already clear that the tax authorities will have to grant protection of legitimate expectations. The decision of the Federal Fiscal Court openly conflicts with the current version of the German VAT Circular, which comments on communities of part owners in numerous places (see e.g. sec 1.5 para 2a sentence 2; sec 2.1 para 2 sentence 6; sec 2.1 para 2 sentence 2 and 3). Thus, it is likely that the tax authorities will offer communities of part owners a temporary non-objection period in which they can continue to be treated as taxable persons for VAT purposes. It is therefore recommended for those affected to follow this development very closely and to react in due time to changes in the VAT treatment.

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