



COVID-19: Reduced VAT Rate for the Restaurant Industry / Extension of the Transitional Period for sec 2b for the Public Sector

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1 Problem

The restaurant industry has, in particular, been affected by the Corona pandemic. The issue of when the restaurant industry will be able to return to normal operations remains unclear. Politicians want to take this into account by reducing the VAT rate for the supply of restaurant and catering services.

The public sector has also not escaped the effects of the Corona pandemic. Necessary measures taken in order to cope with the COVID-19 crisis have now resulted in the legislator taking steps to extend the transitional period for sec. 2b of the German VAT Act, a move which was previously anticipated. This signal is important because under the new provisions legal entities under public law are much more subject to VAT than before.

2 VAT reductions and extension of the transitional period for sec 2b of the German VAT Act

A draft law (Corona Tax Subsidy Act) has been published which provides for a reduced VAT rate of 7 % for the supply of restaurant and catering services rendered after 30 June 2020 and before 1 July 2021 (sec. 12 para. 2 no. 15 of the German VAT Act new version). It should be noted, that the application of the reduced VAT rate is not limited to restaurants. Rather, all industries providing such services can apply the reduced VAT rate of 7 % (e.g: caterers, food retailers, bakeries, butchers). Therefore, the scheme also applies to supplies provided by, for example, canteens and by refectories run by the public sector or by non-profit organisations. The sale of beverages, however, is explicitly excluded from the draft legislation.



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The existing transitional provision concerning the taxation of the public sector according to sec. 2b of the German VAT Act in sec. 27 para. 22 of the German VAT Act will be extended until 31 December 2022 by virtue of the newly introduced sec. 27 para. 22a of the German VAT Act new version. The legislator has, in particular, justified this postponement pursuant to the consideration that the retention of the current transitional period would have long lasting consequences for intermunicipal cooperation, the supply of services of general interest and the performance of legal entities under public law, especially the municipalities. This situation has been significantly exacerbated by the corona pandemic.

3 Consequences for the practice

In principle, the VAT support measures for the benefit of the restaurant industry, through the application of a reduced VAT rate, are to be welcomed. Unlike many other sectors, the restaurant industry cannot recoup its loss of sales. Nevertheless, the burden on the overall budget is immense: this support will cost the taxpayer EUR 2.7 billion. Selective subsidies granted to specific sectors might cause problems, from a VAT policy perspective. Nevertheless, there are many arguments in favour of this temporary exception. However, we must be aware, that the extension of the reduced VAT rate will lead to numerous problems in the day-to-day application of the law. It also remains to be seen whether politicians will be able to withstand the associated social pressure shortly before the next parliamentary election (*Bundestagswahl*) and whether they will ultimately choose not to cancel the deadline. This is especially true against the background that there are already considerable distortions of competition in border areas. Austria, for example, is one of the various neighbouring countries, where the reduced VAT rate has always been granted. Companies concerned are recommended to adapt their cash register systems and invoicing processes at an early stage.

The extension of the transitional period for the reorganisation of the taxation of the public sector, in accordance with sec. 2b of the German VAT Act, had already become apparent prior to the outbreak of the corona pandemic. The EU Commission had already expressed its approval in advance of Corona. The justification of the law is in this regard interesting as it states, in terms of the extension of the deadline: *“During the transitional period which has already been running since 2016, no significant distortion of competition has been identified so far and it is not expected that such a distortion will arise if the deadline is extended by two years.”* This statement is somewhat irritating, on the one hand in view of the legislative motive of sec. 2b of the German VAT Act - namely the prevention of distortion of competition - and on the other hand in view of the fact that the Federal Ministry of Finance declared provision sec. 2b para. 3 no. 2 of the German VAT Act to be factually inapplicable (see Federal Ministry of Finance letter of 14 November 2019 and our KMLZ Newsletter 45/2019). In conclusion, the extension of the transitional period is to be welcomed. This gives legal entities under public law considerably more time to complete their conversion towards sec. 2b of the German VAT Act. In practice, however, it is becoming increasingly apparent that the problem does not lie in the substantive legal issues of sec. 2b of the German VAT Act, but rather in the organisation of tax processes within the authorities, which results from the decentralised structures. For this reason, the extension of the transitional period is extremely important for the implementation of tax compliance structures.