



VAT NEWSLETTER

German Federal Ministry of Finance on warranty commitments: subject to VAT or insurance tax?

18 | 2021

1 Background

Warranty commitments are generally characterized by the fact that the seller issues a warranty declaration that goes beyond statutory warranty rights and for which the seller charges a separate fee. The concrete form of such warranty rights can vary greatly. The guarantee may, for example, pertain to rectification (repair), supplementary performance (replacement/substitution) or reimbursement of the purchase price/current value and may also include compensation for consequential damage such as loss of income. In some cases, the warrantor secures itself through an insurance company, e.g. through reinsurance or insurance for the benefit of the customer.

In addition to the question of whether warranty commitments represent a dependent ancillary service to the supply of goods or a separate service, uncertainty also existed as to whether the warranty commitments were subject to VAT or insurance tax. The German Federal Ministry of Finance (BMF) has now taken up the issue in a letter dated 11 May 2021, categorizing the warranty commitments and commenting on both types of tax for the individual categories. Although the BMF letter was expressly issued only with respect to the warranty commitments of a car dealer, it should also be applicable to similar cases in other business sectors.

2 Warranty commitments as separate services

The BMF adopts the established case law of the Federal Fiscal Court (BFH), according to which the warranty commitment of a car dealer for a consideration is not a dependent ancillary service to the supply of the vehicle, but rather a separate service.



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3 Warranty commitments as insurance agreements

The BMF also confirms that the warranty commitment of a car dealer for consideration is a transaction based on an insurance agreement (and therefore subject to insurance tax, but exempt from VAT under sec. 4 no. 10 letter a of the German VAT Act). Whether the warrantor guarantees a monetary payment or a repair service in the event of a warranty claim is considered to be irrelevant. The warrantor thus becomes responsible for declaring and paying the insurance tax included in the consideration. If the warrantor insures himself with (another) insurer against the occurrence of the warranty claims, this constitutes a tax-exempt reinsurance within the meaning of sec. 4 no. 1 of the German Insurance Tax Act.

4 Exception: full maintenance contracts

According to the BMF, an exception only applies to warranty commitments within the scope of full maintenance contracts. These are not categorized as insurance services, but rather specific services that are subject to VAT. In these cases, the warrantor does not insure a (third-party) risk of the customer, but bears his own entrepreneurial risk resulting from the obligation to perform the maintenance. Therefore, in these cases, the coverage by an insurer is not a tax-free reinsurance but rather a primary insurance subject to insurance tax.

5 Special case: providing insurance coverage

A seller who issues a warranty commitment may allow the customer to decide whether to (i) make a repair claim against the seller or (ii) make a repair cost compensation claim against (another) insurer. In the case of (i), an insurance agreement is established between the seller and the customer. In the case of (ii), insurance cover is provided, whereby the seller is the policyholder and the customer is the insured person. Both services are VAT-exempt according to sec. 4 no. 10 letter a or b of the German VAT Act. For insurance tax purposes, however, the seller must differentiate between the remuneration components. For the portion of the warranty charge to be paid by the customer, which the seller retains, the seller is liable for the payment of insurance tax. For the share that the seller passes on to the (other) insurer, the insurer is the tax debtor.

6 Mark-ups on the sale of insurance

Should the seller charge the premium for the insurance concluded with (another) insurer in favour of the customer, as the insured person to the customer, the premium is also subject to insurance tax. However, the (other) insurer is the tax debtor in this respect. Pursuant to sec. 4 no. 2 of the German Insurance Tax Implementing Regulation, the seller is then obliged to notify the (other) insurer of the amount of the sales premium subject to insurance tax, unless the seller, as policyholder, declares and pays the tax himself.

7 Practical issues

The principles of the new BMF letter are applicable to warranty commitments made after 30 June 2021. Affected businesses will therefore need to check, in a timely manner, what the consequences for new warranty commitments will be. For warranty commitments made prior to 1 July 2021, an option exists whether to continue to apply the principles of the BMF letter of 15 December 2010, which has now been repealed, or to apply the principles of the new BMF letter. In the case of cross-border warranty commitments, it will also have to be examined whether and in which country the warranty commitment is subject to insurance tax. Although there are common regulations on the risk allocation of insurance companies via EU Directive 2009/138, no full harmonization for insurance tax exists within the EU. Deviations in VAT due to different interpretations within the Member States may also come into play.