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KMLZ VAT NEWSLETTER

Input VAT deduction for the absorption of relocation expenses

Relocation expenses in the business interest

The Fiscal Court in Hesse dealt with the issue of absorption of employee relocation expenses by employers in a judgement published in July 2018 (6 K 2033/15 of 22.02.2018). In the particular case, the Court held that the employer's business interest in the move took priority. Thus, there is no free of charge supply here. Consequently, the absorption of relocation expenses by an employer can justify a claim for the company's input VAT deduction. The Court considered the assumption of an exchange-like transaction as unrealistic.

1. Introduction

Discussions concerning the controversy of the VAT treatment of the absorption of relocation expenses by an employer for his or her employees have been ongoing for some time. The input VAT deduction claimed by the employer is the controversial issue. Until the end of 2006, sec 15 para 1a no 3 German VAT Act stipulated an explicit prohibition of input VAT deduction for relocation expenses. According to the Fiscal Court in Hamburg (judgement of 04.04.2006, reference number III 105/05), this regulation is contrary to the law of the European Union. The provision was ultimately repealed at the end of 2006. Since then, the tax authorities have been examining the right to input VAT deduction following the general conditions of sec 15 para 1 no 1 German VAT Act. Input VAT deduction is usually denied because a work-related move is always also considered to be a private matter. The tax authorities consider that this fact outweighs the business interest. To date, the German Federal Fiscal Court has not commented on this issue.

2. Facts

The Plaintiff is an affiliate, which renders central consulting services to other companies in the group. For this purpose, certain responsibilities and functions were shifted, from the headquarters and other locations, to the Plaintiff. Experienced employees were required to be transferred to the Plaintiff's location so that she could commence work. Employees, who up to this point been working abroad, were promised that their various relocation expenses would be absorbed by the Plaintiff. This agreement was stipulated in their employment contracts. In 2013, the Plaintiff received invoices covering the supplies of real estate agents for the location of accommodation for the employees. The Plaintiff subsequently claimed input VAT deduction.

Following a VAT audit, the tax office treated the absorption of relocation expenses as a taxable exchange-like transaction. The cost absorption was stipulated in the employment contract. The basis of assessment was the fair market value of the return service as part of the employee's work perfor-

Contact: Dr. Christian Salder
Lawyer, Certified Tax Consultant
Phone: +49 89 217501285
christian.salder@kmlz.de

mance. Moreover, the tax office denied the Plaintiff's claim for input VAT deduction from the relocation expenses.

3. The Fiscal Court's decision

According to the Fiscal Court in Hesse, the absorption of relocation expenses by the Plaintiff was not made within an exchange-like transaction. Thus, it is not subject to VAT. The absorption of relocation expenses was not directly associated with the employees' work performance. The absorption is intended to motivate the affected employees to fulfill the tasks assigned to them, even if that means that they have to accept considerable personal changes, such as moving to a foreign country. However, this means that the cost absorption of the work to be performed by the employee is covered in advance. The absorption of costs is intended to create conditions, which enable the employees to be able to perform their work in the first place. It does not constitute remuneration for the work performance. It is only a one-time benefit, which would, at best, be paid in addition to the cash wage at short notice. In terms of a realistic interpretation, it must be ruled out that an employee would partly provide his or her labour free of charge.

The absorption of relocation expenses is also not a free of charge supply equivalent to another supply against payment (sec 3 para 9a no 2 German VAT Act). The employees choose their residence in order to arrive at work on time. This private need is overshadowed by business requirements. The Fiscal Court took into account that the Plaintiff had a considerable business interest in commencing her work as soon as possible. In order to do so, experienced employees were required. They were explicitly demanded by the Plaintiff and were required to move from abroad.

Consequently, the Fiscal Court granted the Plaintiff the input VAT deduction from the relocation expenses. In this particular case, the moving supplies were rendered for the company. In other cases, the absorption of relocation expenses – as well as other comparable expenses of the taxable person, e.g. food and transport of his staff – can be caused by primarily business interests. An existing personal benefit, which withdraws behind the needs of the company, does not exclude input VAT deduction. The Fiscal Court in Hesse explicitly agrees with the Fiscal Court in Hamburg and disagrees with a general prohibition of input VAT deduction.

4. Practical information

This judgement presents valuable arguments for discussion with the tax authorities. However, it has to be considered in light of the concrete facts. It is questionable if the Court would make the same decision in the event of absorption of relocation expenses for new employees or for relocations within Germany. In all cases, it is recommended that the benefit received by the company be sufficiently documented. This means that the employer needs to conclude the relevant contracts with the suppliers and incur the resulting expenses in his or her own name (meaning that he or she is the recipient of the invoice). The tax office has filed an appeal against this judgement (German Federal Fiscal Court V R 18/18). Thus, the German Federal Fiscal Court's judgement will hopefully clarify the legal situation. Affected companies should therefore apply for the suspension of appeals and legal proceedings in outstanding cases and await the decision of the German Federal Fiscal Court.