



KMLZ VAT NEWSLETTER

Calculation of deductible proportion of VAT

1. Background

The applicant set up a residential and commercial complex in 2003 and 2004. After its completion, this said complex was rented, partly subject to VAT and partly VAT exempt. The applicant claimed deduction of approximately 54% of VAT which accrued in the relevant year and which was not directly attributed to particular parts of the building. He determined this percentage on the basis of the calculated turnover from the rental of apartments for residential use and the rental of business premises. The tax office viewed the situation differently and only intended to allow a VAT deduction amounting to 34% for 2004 according to the ratio between the area of the premises allowing for VAT deduction and that of the premises not allowing for VAT deduction due to the fact that the German legislator had ordered the priority of this ratio by its revision of sec. 15 para 4 sentence 3 of the German VAT Act in 2004.

Goodbye to simple calculation of deductible proportion of input VAT

Calculating the deductible proportion of VAT for mixed-use buildings based on the ratio between the area of the premises allowing for VAT deduction and that of the premises not allowing for VAT deduction is compatible with EU law. This is the main thrust of a decision by the German Federal Tax Court. What is more interesting, however, are the further comments regarding input VAT deduction. The Federal Tax Court interprets the rule regarding the determination of the proportion of input VAT deduction in such a way that the allocation of input VAT according to economic criteria will only apply to those VAT amounts that are subject to adjustment of input VAT deduction as referred to in Art. 184 – 192 Directive 2006/112/EC.

After submission to the European Court of Justice, the ECJ ruled, in its judgment of 8 November 2012, C-511/10, *BLC Baumarkt*, that EU law allows for a further and different calculation of the proportion of the VAT deduction for mixed-use buildings, other than that based on turnover. The prerequisite, however, is that this different calculation „ensures a precise determination of the deductible proportion“. With this decision, the Federal Tax Court created more problems than it solved as the Federal Tax Court was now to decide in which cases the ratio between the area of the premises allowing for VAT deduction and that of the premises not allowing for VAT deduction presented the more precise key.



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2. The Federal Tax Court's judgment of 22 August 2013 (V R 19/09)

Ultimately, the Federal Tax Court has retained the standardized priority of the ratio between the area of the premises allowing for VAT deduction and that of the premises not allowing for VAT deduction as laid out in sec. 15 para 4 sentence 3 of the German VAT Act for mixed-use buildings in line with EU law. However, the rule would have to be laid out in accordance with the VAT Directive.

3. Effects on the practice

It is now certain that entrepreneurs are tied to this ratio concerning the acquisition or construction of buildings. The tax authorities will have to completely revise the German Administrative VAT Circular in terms of sec. 15.17 as, to date, there are three categories for calculating the deductible proportion of VAT, in terms of economic attribution:

- VAT, which can be deducted in full, as it can be ascribed exclusively to turnover which allows for VAT deduction.
- VAT amounts which are excluded from VAT deduction in the full amount as they can be ascribed exclusively to turnover which does not allow for VAT deduction.
- Other VAT amounts, namely VAT amounts that are economically connected to turnover which, on the one hand, allow for VAT deduction and, on the other hand, are excluded from VAT deduction.

This approach, in terms of economic attribution, is only permissible for VAT amounts that are subject to adjustment of VAT deduction according to the Art. 184 – 192 Directive 2006/112/EC. In other words, for purchases that do not relate to capital goods, only the calculation of the proportion based on the total turnover of the taxable person might come into question.

This might be of particular importance for banks, for example, as they have optimized their proportion of deductible VAT separately for each sector and will now have to calculate these amounts with respect to the total turnover of the bank.