



VAT NEWSLETTER

## Annual Tax Act 2020 (Part 7): Implementation of a decentralised taxation procedure for federal and state governments 38 | 2020

### 1 Background

Until now, the German VAT Act has not provided for a decentralised taxation procedure for the public sector. Rather, the general rules of the taxation procedure applied to all legal entities governed by public law (*jPÖR*). Therefore, in accordance with sec. 2 para. 3 of the German VAT Act (old version), a legal entity governed by public law was required to report all supplies of its - possibly numerous - commercial businesses (*Betriebe gewerblicher Art*) in a single VAT return. This reporting obligation was to be fulfilled uniformly by the legal representative of the legal entity governed by public law. With regard to the federal and state authorities (*Bund und Länder*), however, the tax authorities have, so far, applied a decentralised taxation procedure despite the lack of a real legal basis for this (see, inter alia, sec. 1a.1 para. 3 of the German VAT Circular regarding intra-Community acquisitions). This approach was due to the fact that sec. 2 para. 3 of the German VAT Act (old version) built on the concept of commercial businesses according to the German Corporation Tax Act. However, this administrative practice was diametrically opposed to the case law of the ECJ. Since the judgment in the case *Gmina Wrocław* (C-276/14), it has been sufficiently clarified that a budgetary entity does not satisfy the criterion of independence. Thus, the legal entity governed by public law (not the budgetary entity) is the “taxable person”.

Under sec. 2b of the German VAT Act, this previous taxation practice can no longer be justified. For VAT purposes, commercial businesses no longer exist. Consequently, legal entities governed by public law must report all of their taxable supplies in a single VAT return. This is hardly manageable for federal and state authorities. The federal government, for example, comprises 156 lower federal authorities and numerous subordinate organisational units. It is difficult to determine the extent to which each of these is engaged in economic activities. Many representatives of the federal and



Prof. Dr. Thomas Küffner  
Lawyer, Certified Tax  
Consultant, Certified Public  
Accountant

+49 (0) 89 217 50 12-30  
thomas.kueffner@kmlz.de

state governments have come to the conclusion that they need to find a practical way of dealing with the consequences of the implementation of sec. 2b of the German VAT Act. So what can be done? Let's just change the law!

## 2 Legal regulation

With the implementation of sec. 18 para. 4f and sec. 18 para. 4g of the German VAT Act (draft), the legislator now intends to establish a legal basis for the decentralised taxation procedure and to disburden the federal and state authorities (see draft bill on the Annual Tax Act 2020 (as per: 17 July 2020)). According to the new regulation, the organisational units (hereinafter: OU) of the federal and state authorities are responsible for all rights and obligations under VAT law insofar as their respective actions give rise to a reporting obligation. The term OU is not defined in the new regulation. The legislator merely describes it in the official justification to the current draft bill of the Annual Tax Act 2020. It includes, for example, federal and state authorities, as well as federal/state representatives with their own legal personality. The OU must trigger an obligation to file VAT returns by its actions, which is also the case for taxable but VAT exempt supplies, as well as for intra-Community acquisitions. The respective OU is required to report its supplies in its own VAT returns. According to sec. 18 para. 4f sentence 2 of the German VAT Act (draft), in conjunction with sec. 30 para. 2 no. 1 lit. a and b of the German Fiscal Code, the OU takes the place of the corporation in the procedures mentioned therein, including the administrative, auditing and judicial procedures in tax matters and the criminal procedure for tax offences.

It is particularly "charming" that the authorities are granted a high degree of organisational freedom: By means of an organisational decision, the OUs can either form further subordinate OUs to fulfil their obligations or the superior OUs can exercise the subordinate's rights and duties. According to the new regulation, the various thresholds for the respective OUs, e.g. the threshold for the monthly VAT return period (EUR 7,500) and for the small business regulation (EUR 22,000 and EUR 50,000), should always be regarded as exceeded. This is consistent and correct and also simplifies matters. According to sec. 27 para. 22 sentence 7 of the German VAT Act (draft), sec. 18 para 4f of the German VAT Act (draft) is to be applied for the first time to VAT periods after the option period. However, the federal and state governments may waive the application of this provision (uniformly for all of their OUs) with effect for the future.

## 3 Consequences for the practice

The new statutory regulation provides for a considerable simplification of the taxation procedure for the federal and state governments. However, the regulation also extends the scope of duties of the responsible persons in the individual OUs. This is particularly true with regard to possible tax and administrative offences. A functioning tax compliance management system is therefore indispensable for the federal and state governments, at the latest by the end of the option period. From experience, the federal and state authorities will be faced with great challenges, as the tax law has, so far, been of minor importance. Due to sec. 2b of the German VAT Act, this will now completely change: Actions under private law are taxable from the first euro. The same applies to activities under public law insofar as they threaten to significantly distort competition. Many processes have to be redefined.

The regulation does not provide clarity with regard to the substantive legal problems resulting from decentralised taxation. The OU does not constitute the taxable person within the meaning of VAT law. Rather, the taxable person is broader than the OU and can comprise numerous OUs, so that non-taxable internal supplies between OUs are conceivable. It then becomes particularly interesting when one considers input VAT deduction: Who claims it? How do the OUs coordinate with each other? Who takes on the responsibility? There is a lot to do...