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VAT NEWSLETTER

ECJ partially questions the German practice of company car taxation

03 I 2021

1 Background

For many years, the German tax authorities have deemed the provision of a company car to an employee, which is also available for private use, as a taxable long-term rental of a means of transport, which is to be taxed at the place where the end user resides, in accordance with sec. 3a para. 3 no. 2 sentence 3 of the German VAT Act (Art. 56 para. 2 of the VAT Directive). As a result, there is no taxation in Germany in cases where an employee, who resides in a foreign country close to the German border, is given a company car, which is also for his private use, within the scope of his employment relationship. The Saarland Fiscal Court assumes that the car concerned is not provided for consideration in circumstances where the employee does not pay consideration and nor does the employer retain an amount of money from the employee's salary with regard to the car. The Saarland Fiscal Court referred the question to the ECJ as to whether the provision of a vehicle to a member of staff, which vehicle is allocated to the business, in this case constitutes a long-term rental of a means of transport to an end consumer within the meaning of Art. 56 para. 2 of the VAT Directive.

2 ECJ decision

In its judgment of 20 January 2021 (C-288/19), the ECJ denied the existence of the consideration required for the taxable hiring of a means of transport, in circumstances where the employee neither makes a payment nor uses part of his cash remuneration with respect to his use of the business allocated vehicle, and also does not waive other benefits. The ECJ is of the opinion that, in this case, only a taxation of a supply carried out free of charge, in accordance with sec. 3 para. 9a no. 1 of the German VAT Act (Art. 26 para. 1 letter a of the VAT Directive), is possible. This requires that the input VAT on such a vehicle was fully or partly deductible. In this case, there is no taxation at the employee's place of residence in accordance with sec. 3a para. 3 no. 2 sentence 3 of the German VAT Act (Art. 56 para. 2 of the VAT Directive).

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3 Consequences for the practice

The ECJ's decision is based on a particular individual case. The question referred concerns the situation where the employer does not retain a sum of money and nor does the employee pay remuneration or have the option to choose whether he takes the company car with waiver of other benefits on the basis of an agreement. In practice, this sort of case is likely to be very rare. This is because usually, in the case where an employee is offered a company car, the employer enters into an agreement with the employee on a conversion of remuneration, i.e. company car transfer with salary waiver. Even in the absence of such an agreement, the question arises as to whether the work performance in the specific individual case is to be regarded as consideration for the company car (barter-like transaction).

Since the ECJ only decides specific individual cases and the findings can only be transferred to comparable cases, it is not possible to draw a compelling conclusion on the basis of the ECJ ruling that the provision of a company car is free of charge in all cases. Nevertheless, taxable persons should carefully review their contracts for the provision of company cars with regard to the agreed remuneration. If there are arguments in favour of non-remuneration in a specific case, the companies concerned can refer directly to the ECJ ruling and may possibly benefit in cross-border situations as follows:

3.1 Implications for domestic taxable persons in the case of non-remuneration

In the case of full allocation to the company and a full input VAT deduction, a supply carried out free of charge is given in the amount of the non-business use, in accordance with sec. 3 para. 9a no. 1 of the German VAT Act. Taxation does not apply in the instance of an input VAT deduction which is only claimed in the amount of the actual business use and in the case of a lack of input VAT deduction entitlement (e.g. banks and insurance companies).

The supply carried out free of charge has to be taxed at the place from which the employer operates its business in accordance with sec. 3a para. 1 of the German VAT Act. This means that – contrary to the view of the German tax authorities – taxation also takes place in Germany if an employee is resident in a foreign country close to the German border. In this case, any existing obligation to register for VAT purposes in a foreign country does not apply. Thus, domestic taxable persons can benefit from the ECJ ruling if the VAT rate in Germany is lower compared to that of the employee's country of residence. Moreover, a possibly existing obligation to register abroad for VAT purposes does not apply.

3.2 Implications for foreign taxable persons in the case of non-remuneration

A company car provided free of charge by foreign taxable persons to employees resident in Germany is - contrary to the view of the German tax authorities - not subject to taxation in Germany. Foreign taxable persons can apply for VAT refunds if they have declared German VAT on the provision of company cars to employees resident in Germany in reporting periods that have not yet become final.

3.3 Implications for rental and leasing of cars in the case of non-remuneration

The ECJ was not required to rule on the far more practically relevant case, where an employer merely rents a vehicle (or leases it without an agreed transfer of ownership). In this situation, a supply carried out free of charge in accordance with sec. 3 para. 9a no. 2 of the German VAT Act could be considered, provided that an input VAT deduction is claimed not only in the amount of the actual business use. In this case too, the place of supply is determined by sec. 3a para. 1 of the German VAT Act, so that the implications mentioned above in 3.1 and 3.2 could, in principle, also apply to rental and leasing cars.

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