



# KMLZ VAT NEWSLETTER

## Circular of the Federal Ministry of Finance on reform of VAT taxation of public bodies now available

### 1. Facts

By means of sec 2b of the VAT Act, the legislator has restructured the VAT taxation of public bodies (see Newsletter 02/2016). In doing so, the German VAT Act has been moved very much closer to the VAT Directive and the case law of the Federal Fiscal Court. Legal entities under public law ("public bodies") are deemed to act as taxable persons in accordance with sec 2b of the VAT Act as soon as they render supplies on the basis of private law or compete with private third parties. Public bodies will now more often fall within the scope of VAT due to this provision. In particular, the hitherto fiscal authority exemptions in the fields of asset management and assistance operations will no longer exist in this way in the future. With sec 27 para 22 of the VAT Act, the legislator has created a generous transitional regulation to assist public bodies to adjust to these fundamental changes. Sec 2b of the VAT Act is to be applied to all supplies as of 01.01.2017. By filing a declaration, the still applicable sec 2 para 3 of the VAT Act can be claimed for all supplies until 31.12.2020. Public bodies must file their declarations at the competent tax office by 31.12.2016.

### Notwithstanding the transitional regulation for sec 2b of the VAT Act, time is of the essence

By means of sec 2b of the German VAT Act, the legislator has reformed the VAT taxation of public bodies. The amendment is accompanied by a transitional regulation in sec 27 para 22 of the German VAT Act. Sec 2b of the German VAT Act is applicable to supplies as of 01.01.2017. By making a declaration to the tax office, the application of the new regulation can be waived in favor of continuing with the existing legal situation. The Federal Ministry of Finance has now issued an opinion on sec 27 para 22 of the German VAT Act. Public bodies need to check, in due time, whether the new implementation arrangements application rule would be advantageous.

### 2. Content of the Circular

According to the Federal Ministry of Finance Circular, the declaration has to be filed by the public body itself through a legal representative or by an authorized person. The declaration cannot be filed by an individual organizational unit of the public body, such as an authority or a commercial business. Thus, "cherry-picking" of selected fields of activities is not possible. The Minister-President of a federal state or his authorized representative is required to uniformly declare the option for all regional authorities, commercial businesses and other corporate entities.

The declaration has to be filed with the tax office of the district in which the public body is entirely or mainly operating its business (sec 21 of the German Fiscal Code). Problems of competences may arise where a public body has been operating its respective commercial business in the districts of different tax offices. It is not mandatory to file the



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declaration in writing, as proposed by the tax office, but from the public body's view it is highly recommended for the purposes of evidence. The declaration has to be sufficiently specific. The Federal Ministry of Finance Circular does not mention any other formal requirements.

To date, public bodies have been referring to the Federal Fiscal Court's case law as regards the VAT taxation of public bodies. Sec 2b of the VAT Act is, to the greatest extent possible, in line with this case law. Where a public body invoked the case law, it had to apply this case law to all its activities. In the fiscal authority's opinion, the public body could not return to applying sec 2 para 3 of the VAT Act. According to the Federal Ministry of Finance Circular, this administrative opinion is now revoked by the new legal provision. Thus, a public body, which has already invoked the case law of the Federal Fiscal Court, may now return to applying sec 2 para 3 of the VAT Act for supplies as of 01.01.2017, by filing a declaration with the tax office.

If the public body declares its intention to continue applying sec 2 para 3 of the VAT Act, it will automatically remain in force until 31.12.2020. Public bodies may revoke this declaration. Any withdrawal must be filed by 31.12. of a particular calendar year, so as to enable the public body to apply sec 2b of the VAT Act as of the following year. A repeated return to applying sec 2 para 3 of the VAT Act is no longer possible. Sec 2 para 3 of the VAT Act cannot be applied to public bodies founded after 31.12.2016. Where individual public bodies have opted for a merger, the newly founded public body may choose to apply sec 2b or sec 2 para 3 of the VAT Act. A previously declared option is also binding for legal successors.

### 3. Tips for the practice

In the course of 2016, all public bodies need to check whether applying sec 2 para 3 of the VAT Act continues to be useful to them. As a golden rule, we can say: Where there is no high input tax volume, sec 2 para 3 of the VAT Act is the better alternative. This golden rule should, however, be respectively reviewed in the individual case, to economize budgetary resources. As public bodies already applying the new case law of the Federal Fiscal Court may opt to return to the old regulation, this option also should be taken into consideration.

Therefore, a project plan has to be developed under which not only possible input tax volumes have to be reviewed but also all revenue titles should be examined to determine whether these revenues will be subject to future taxation. Apart from many other questions, such as establishing a tax department, consideration of pre-existing accounting departments' IT ability to meet the new requirements must ensue. Should this evaluation demonstrate that the application of sec 2 para 3 of the VAT Act is more favorable, the public body should, in due time, file a respective written declaration – after having obtained the appropriate board resolution. A confirmation of receipt should be retained.

Even if a public body intends to apply sec 2 para 3 of the VAT Act until 31.12.2020, it is recommended that consideration of future alternative arrangements take place now. This often requires negotiating with existing contracting partners, coordinating internal and external committees and even amending statutes, regulations or the law. To allow for time to negotiate, making an early start is absolutely essential.