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Inputs for dual-use buildings generally in output ratio

The Supreme Tax Court has held that the input tax of a landlord is generally to be deducted in relation to the split of the outputs between taxable and tax-free turnover.

Living accommodation let to private individuals is VAT-free. Space let to business tenants is taxable turnover if the landlord has exercised the relevant option. The tax on inputs associated with taxable outputs is deductible as input tax; that on those connected with the exempt turnover is not. The VAT directive generally sees the desired split of the dual-use inputs for dual-use buildings to be in the ratio of taxable to exempt outputs. The German VAT Act allows this split only if no other split is economically justified. This latter provision has been generally held by the courts to imply that any other split taken must lead to a “more precise” result. Unfortunately, the courts have, up to now, refrained from defining “more precise”.

A taxpayer let the ground floor of her building to retail shops and the first floor to natural person tenants. She charged VAT on the shop rentals, but not on the amounts billed to the private tenants. The tax office pressed for a split based on floor space as being more precise, whilst the taxpayer continued to request a for her preferable split based on turnover. The Supreme Tax Court has now held that a turnover-based split is, in principle, to be favoured as being the primary focus of community law. It then added that the substantially different appointments of the floor let for business use from that let for private accommodation meant that a split based on floor space was not, as such, more precise. Whether that split could, though, be more precise for other reasons was a matter requiring further review by the lower court.

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