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German Federal Fiscal Court's (*Bundesfinanzhof*) Decision Regarding the Tax Liability of a Service Recipient in the Case of a VAT Consolidated Tax Group

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In a fiscal court procedure, the Federal Fiscal Court made a very positive decision for property developers regarding the tax liability of a service recipient in the case of a VAT consolidated tax group (tax group) and clarified an important legal matter for so-called property developer cases that had been controversial until then.

According to the Federal Fiscal Court, in the case of a tax group, the parent company receives incoming turnovers; therefore, the external turnovers of the tax group are relevant for § 13b Section 5 Sentence 2 in connection with Section 2 No. 4 of the German VAT Act.

Therefore, the parent company was not a tax debtor, because traditional property companies incorporated in the tax group sold apartments built on their own land to various purchasers.

This was decided by the 5th Senate of the Federal Fiscal Court in its decision dated 23 July 2020 (V R 32/19).

Facts

The plaintiff, a sole entrepreneur represented by our firm, was a majority shareholder in several corporations, including the X-GmbH (GmbH).

The GmbH provided construction services to affiliated companies for tax-exempt turnovers within the scope of property development activities in accordance with § 4 No. 9 letter a) of the German VAT Act.

The GmbH engaged other entrepreneurs (third parties) for construction services, which did not belong to the plaintiff's company group.

The third parties and the GmbH assumed that the GmbH was the tax debtor according to § 13b Section 2 Sentence 2 in connection with Section 1 No. 4 of the German VAT Act (since 1 July 2010: § 13b Section 5 Sentence 2 in connection with Section 2 No. 4 of the German VAT Act).

Following several external audits, the tax office assumed that there was a tax group between the plaintiff as the parent company and the GmbH and its sister companies as subsidiaries according to § 2 Section 2 No. 2 of the German VAT Act.

Later change notices were issued, in which the tax authority recognised the tax group for all years in dispute and included the tax debts for the construction works provided to the GmbH at the plaintiff.

In the opposition proceedings, we argued on behalf of the plaintiff that the conditions for the tax liability of the recipient of the service were not met.

It is true that the GmbH used the construction services obtained from the third-party contractors to provide construction services to its sister companies (property companies). However, due to the tax group, this is irrelevant because of intra-group sales.

The crucial point is, therefore, that the construction services obtained by the GmbH as a subsidiary were used by the tax group for tax-free property deliveries to the various purchasers of the apartments in accordance with § 4 No. 9 letter a) of the German VAT Act.

The lawsuit filed by our firm before the Berlin-Brandenburg Finance Court was successful.

Decision of the Federal Fiscal Court

The Federal Fiscal Court followed the decision of the lower instance and rejected the appeal of the tax office as unfounded.

According to the Federal Fiscal Court, the Berlin-Brandenburg Fiscal Court correctly decided that the plaintiff is not a tax debtor for the construction services received from the GmbH as a subsidiary.

In the case of a tax group, the parent company, but not the subsidiary, receives the incoming turnovers, so that in the case of § 13b Section 5 Sentence 2 in connection with Section 2 No. 4 of the German VAT Act refers to the external turnover to be allocated to the parent company and not to non-taxable internal turnover of the companies in the tax group.

For the tax liability of the recipient, it is necessary that the recipient uses the work supplied or other service provided to them, i.e. construction, repair, maintenance, modification or removal of buildings, to provide such a service (Federal Fiscal Court decision dated 22 August 2013, V R 37/10).

The Federal Fiscal Court continues to adhere to this case law, which was issued for the old law.

If a subsidiary receives construction services and uses them for construction services to another group company, the use of the services as defined by the Federal Fiscal Court decision dated 22 August 2013, V R 37/10, does not depend on this internal turnover, but on the external turnover – attributable to the parent company – for which the received construction services are used.

Since this external turnover related to the sale of apartments (land deliveries) and, thus, to classic property development services, the controlling company was not classified as a tax debtor.

The question regarding the compatibility of the tax group with EU law (cf. Federal Fiscal Court, decision dated 11 December 2019, XI R 16/18, and decision dated 7 May 2020, V R 40/19) is not relevant in a dispute in which the tax claim asserted by the tax office does not exist even on the basis of a tax group.

Conclusion

This decision is of considerable importance for property developers, as the constellation of a tax group is frequently encountered in practice.

In these cases, construction services are provided by third-party subcontractors to a general contractor who is part of the tax group.

This general contractor provides its services as so-called internal turnover to companies holding real estate, who are part of a tax group.

The construction work is, thus, used "outwardly" towards the buyers of the apartments as a classic developer service (delivery of land), so the developer is not a tax debtor.

From now on, developers can refer to this fundamental decision of the Federal Fiscal Court in comparable constellations.

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