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Reduced VAT rate for hotel breakfasts and input tax deduction for tenant electricity PV systems

ECJ submissions on the apportionment requirement and consolidation of the BFH case law

The BFH (Federal Fiscal Court) has now referred three cases to the ECJ (European Court of Justice) to examine the 19 % VAT rate on ancillary services for hotel accommodation, while at the same time it has decided regarding photovoltaic (PV) systems that input VAT deduction should generally be possible because the tenant's electricity is not supplied VAT-free.

Initial situation: Apportionment requirement despite uniformity of supply

German VAT law differentiates between accommodation services (7 %) and „services that do not directly serve the accommodation" (19 %) for the purposes of applying the reduced VAT rate in Section 12 (2) no. 11 sentence 2 of the German VAT Act [UStG]. The latter typically refers to catering services, but also includes use of communication networks (e.g. hotel Wi-Fi), the use of the minibar in the hotel room and the use of the hotel parking lot.

This „apportionment requirement" applies exclusively to those services that are to be regarded as ancillary services to accommodation services. If this rule did not exist, breakfast or the use of parking spaces, for example, would share the same fate as accommodation services, with the result that the reduced VAT rate would also apply to them (Section 3.10 (5) sentence 1 of the German VAT Application Decree [UStAE]). Conversely, a special regulation becomes irrelevant if it is established that breakfast etc. are independent services.

Dispute over the unlawfulness of the apportionment requirement for accommodation services under EU law

The apportionment requirement therefore represents a national exception to the VAT principle of uniformity of supply. Whether this is permissible under European law requirements has been a matter of debate particularly since the ECJ ruling in the „Stadion Amsterdam" case from 18.1.2018 (C-463/16).

Regarding the rental of operating facilities, which – in contrast to property rentals – is expressly to be treated as taxable in accordance with Section 4 (12) sentence 2 UStG, the ECJ has spoken out against dividing such services into tax-exempt rental of properties and taxable rental of operating facilities if the rental of operating facilities can be regarded as an ancillary service (see ECJ of 4.5.2023, C-516/21, FA X). The BFH agreed with this in its subsequent decision (BFH of 17.8.2023, V R 7/23). Nevertheless, the tax authorities have not yet implemented this in practice, which gives companies the opportunity to invoke the case law in individual circumstances.

Although it is clear from this mixed situation that uniform services must not be treated differently by national regulations, there is the question of what leeway the (national) legislator has, at least regarding tax rates.

BFH upholds the apportionment requirement for accommodation services

The BFH must currently decide in three proceedings (all dated 10.1.2024) whether certain additional services to accommodation services are subject to the reduced tax rate. Specifically, the proceedings concern breakfast services (XI R 13/23) as well as parking spaces, fitness and wellness facilities and hotel Wi-Fi (XI R 13/23 and 14/23). Due to recent developments at EU level, the BFH has referred all three proceedings to the ECJ.

In the orders for reference, the BFH upholds the principle of apportionment regarding the reduced tax rate. This is because, in contrast to the tax exemption regulations, the national legislator has been granted leeway by the Union legislator about the tax rates, allowing the reduced tax rate to be applied just to certain parts of a uniform supply to which a reduced tax rate may be applied. The only condition is that the Member States observe the principle of fiscal neutrality.

In its orders for reference, the BFH also clarifies the cases in which the apportionment requirement does not apply, namely when the additional services can be independently deselected by the hotel guest. In these cases, it is clear that the additional services have an independent character and are therefore to be regarded as independent services. These are subject to the standard VAT rate, meaning that Section 12 (2) no. 11 sentence 2 UStG becomes irrelevant. As the BFH deemed this indisputable, it saw no reason to refer the issue to the ECJ for clarification.

Input tax deduction for PV systems

A few months later, the BFH confirmed this legal opinion in a case concerning the supply of electricity by a landlord to a tenant. The background was a dispute about input tax deduction for PV systems that had been purchased for tenant electricity supplies. The BFH ruled that the supply of electricity was not an ancillary service to the (tax-free) rental service because, by law, the tenant is free to choose their electricity provider and the supply of electricity is billed separately and according to individual consumption (see BFH of 17.7.2024, XI R 8/21). In the specific case, the fact that the tenant had to bear conversion costs when switching to other electricity providers was irrelevant.

Implications for practice

Should the ECJ declare the German apportionment requirement for accommodation services to be contrary to EU law, this would particularly benefit hotel operators. Although the tax authorities are not expected to implement the new principles directly, hotel operators should have a good chance of successfully invoking the reduced tax rate, and this would lead to a genuine VAT advantage.

Regarding electricity supplies with PV systems for tax-free long-term rentals, current case law strongly supports the landlord's right to deduct input tax for the PV systems. Landlords should refer to this if there are any objections from the tax office; moreover, future investments can now be calculated with greater legal certainty.

Conclusion / key facts:

The apportionment requirement for accommodation services is entering the next round with the latest ECJ referrals from the Federal Fiscal Court, and the ECJ's decisions in this matter are eagerly awaited. The hotel industry in particular may benefit from VAT advantages in the future. In the case of investments in systems that are used for electricity supplies for tax-free rented properties, the possibility of claiming input tax deduction is at risk and a case-by-case assessment is urgently recommended.

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