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Federal Ministry of Finance locks third-country taxable persons out of applying the TOMS regime (special regulation for travel agents, in acc. with Art. 306 EU VAT-Directive)

Germany's Federal Ministry of Finance has been examining the taxation of travel services performed by companies based in third countries. In a letter issued on January 29, 2021 (bundesfinanzministerium.de), the ministry states that the special scheme for travel agents (Sec. 25 of the German VAT Act – UStG) will no longer be applicable if the performer of these services is based outside the EU and does not have a fixed establishment in Community territory.
The amended administrative opinion (Sec. 25.1(1) p.12 of the German VAT administrative guidelines [UStAE], new version) will apply in all current cases, with a non-objection rule in place for services provided before January 1, 2021.
Both notably and regrettably, the substance of the letter consists of a single sentence. As no mention is made of any background or consequences, the new administrative opinion raises numerous questions. It is also surprising that the ministry is speaking on this topic now. Margin taxation has already been extended to the B2B sector, entering German VAT law with effect from December 18, 2019. However, both taxable persons and advisors are still waiting for clarification from the tax authorities about this and, in particular, on the question of showing taxes on invoices for services.

Taxation of travel services
The special regulation for the taxation of travel services – TOMS regime (Sec. 25 UStG, Art. 306 et seq. VAT Directive) is intended to simplify matters. Individual service components (such as flight and accommodation) which are owed to the service recipient – usually the traveler – are bundled into a single service taxable at the service provider's place of business under Sec. 3a (1) UStG. This simplification rule aims primarily to prevent the taxpayer from having to register in multiple EU states for VAT purposes if individual components would be taxable when viewed individually (such as short-term vacation home rental).
Excluding the input tax deduction on inbound advance travel services (Sec. 25(4) UStG), the service provider pays tax only on the margin, i.e. the difference between the travel package price and the sum of third-party advance travel services.

Background
An exemption of third-country travel agents from the regulation was discussed at EU level several years ago (cf. European Commission draft of February 8, 2002 for an amending directive to Art. 26 of the 6th EC Directive, OJ C 126 E/390). This stemmed from the Commission having identified considerable room for maneuver, leading to non-taxation in Community territory. As a result, travel agents from third countries could receive individual advance services, in some cases without being taxed. If the state of residence in question has no VAT, or at least no comparable regulations for travel

services, travel agents could supply services to customers without VAT. This would result in a considerable competitive disadvantage for travel agents based in Germany or in the rest of the EU.
No such limitation as the one made by the Federal Ministry of Finance is found in the UStG, although one could perhaps be derived from the VAT Directive. Article 307 states that the "service shall be taxable in the Member State in which the travel agent has established his business or has a fixed establishment".

Potential impact and unresolved questions
With this in mind, it is not clear how to treat services performed by travel agents with their registered office in third countries.

Outbound services
If the special regulation under Sec. 25 UStG for travel services no longer applied in this context, the place of performance would no longer have to be defined as the registered office of the supplier (in this case in a third country). Accordingly, places of performance could also be domestic, provided that the individual service components (such as the transport of passengers or accommodation) are separated and assessed in isolation for VAT purposes.
A 'travel service' typically comprises multiple services, including advance services, that the customer wants to receive in a single package. A single overnight stay, a transfer or one leg of a return flight is of no interest to customers. Instead, they want a flight plus transfer to their hotel and, at the end of the vacation, a transfer back to the airport and the return flight home. As a result, in the future, these services should not be split into individual components without applying Sec. 25 UStG. What's more, no places of performance should be determined for these services that might assign Germany the right to tax them.
Even without Sec. 25 UStG, a complex, one-of-a-kind service must often be assumed, for which no separate rule about the place of performance applies. In the B2C sector, the place of performance would then still be the registered office of the third-country travel agent performing the service, unless the service were attributable to a domestic permanent establishment.
The question thus arises as to whether Germany can derive the right to tax even if Sec. 25 UStG is not applied.

Inbound services
Taking into account the non-application of Sec. 25 UStG, this must then also apply to the input transactions. If Sec. 25 UStG does not apply, it would be permissible to deduct input tax from these input transactions if German VAT is owed in the first place.
Certainly, the tax authorities will not want it to be understood this way. However, the regular application of VAT principles provides sound reasons for allowing an input tax deduction in this case.

Outlook
It remains to be seen whether the tax authorities will regularly assume that travel services (performed by travel agencies in third countries) must be broken down into individual components – and whether

and to what extent this is compatible with CJEU principles under which service packages may not be 'artificially' split.
From a German perspective, double taxation can become a risk if a travel service is split into components that are each assessed in isolation. This applies, for example, to the following services performed in Germany:

- Transportation services (Sec. 3b UStG)
- Accommodation services (Sec. 3a(3) no. 1 sentence 2(a) UStG, Art. 31a(2)(i) VAT Implementing Regulation)
- Catering services (Sec. 3a(3) no. 3(b) UStG or, if applicable, Sec. 3e UStG)

The tax rate is another issue, as accommodation services and (at least until December 31, 2022) the provision of meals are subject to the reduced tax rate.
Double taxation is likely to be a particular threat for travel agents in the UK. Although the UK is now a third country, travel agents there have historically taxed travel services (largely) in accordance with the principles of EU law.
Depending on how a service is defined (for example, as a single service with place of performance in accordance with Sec. 3a(1) UStG), non-taxation may continue.

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