By PwC Deutschland | 31. März 2011

Memorandum of understanding does not protect a position

The Supreme Tax Court has held that a memorandum of understanding prior to a legal change does not bind a taxpayer sufficiently to allow him to claim protection from retroactive legislation.

Capital gains of up to DM 50m by natural persons on the sale of significant shareholdings up to August 1, 1997 were taxed at only half the scale rate of income tax otherwise due. The upper limit for the privilege then fell to DM 15 m. The change was enacted in a bill introduced to Parliament at first reading on August 5. By that date, a seller had already agreed the main points of a deal with the buyer as documented in a memorandum of understanding signed on June 4. Formally, though, the sale was not concluded until the contract signature before the notary public on August 28. The seller's gain fell between the old and the new limits; thus he was personally affected by the change in the law. The tax office held to the statute as enacted and allowed only the lower privilege. He claimed entitlement to the higher on the grounds that he was already committed to the deal by the time the change became apparent. Reducing the limit in his case was thus equivalent to retroactive application of burdensome legislation.

The Supreme Tax Court has now upheld the position of the tax office. Had the seller's commitment been formalised in a valid contract at the time of the first Parliamentary reading of the amendment bill, he would have indeed had a valid constitutional complaint of retrospective taxation. As it was, there was no absolute protection of a taxpayer's interests against unfavourable changes in the law, and at the time he was not yet fully committed to go through with the deal as negotiated. Indeed, up to contract signature, it was open to him to ask for renegotiation of terms as he felt appropriate. The memorandum of understanding was explicitly declared as not binding and carried a specific mutual waiver of all claims to compensation for damages or costs arising from it. Thus, it could not be interpreted as a preliminary, or prior, agreement to conclude a contract on set lines.

The tax privilege behind this dispute has long since been withdrawn altogether. As it stands, the ruling is thus irrelevant to M&A deals now being negotiated. However, it is of importance as a further step on the path to a clear distinction between the prohibited taxation in retrospect of transactions that have already taken place and the allowed disappointment of hopes for the future.

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Schlagwörter

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