

By PwC Deutschland | 28. März 2013

Taxable income must take all subsequent events into account

The Supreme Tax Court has held that the tax office must adjust taxable income in the light of objective evidence not available when the balance sheet was drawn up.

A mobile telephone company distributed mobile phones below cost as an inducement to the recipient to sign a two-year service contract. It took the apparent loss on sale to immediate expense. At the time, this could be considered an acceptable accounting treatment, though largely because of the lack of relevant case law guidance. In the meantime, the legal position has been clarified and it is now generally accepted that the company should have deferred the expense over the fixed term of the contracts. The tax office assessed the company to corporation tax on the basis of income increased by the expense deferral, but the company objected on the basis that the financial statements were tenable from the point of view of commercial prudence at the time they were drawn up. At that time they reflected the current state of the law as well as all known facts and were therefore “subjectively correct”. The tax office could not insist on an adjustment in the light of later court rulings or other revelations. This view had some support in earlier case law of the Supreme Tax Court, although the “senate” (chamber) trying the case did not wish to accept it without reservation. Accordingly, it laid the matter before the Grand Senate, a panel of one judge from each chamber charged with ensuring ruling consistency between the 11 chambers of the court.

The Grand Senate has now held that tax offices are bound to assess on the basis of all facts and circumstances known when the assessment is raised. This follows from the legal requirement that an assessment be “objectively correct”. Taxable income as originally computed must thus be amended in the light of all matters coming to light afterwards, including changes in legal precedents or the tax authorities’ view of the law. Thus it is not open to taxpayers to argue that the financial statements were drawn up to the best of their knowledge and belief at the time, in the face of events occurring later.

It is worth noting that although this decision contradicts the position taken by the taxpayer in the given instance, it does not necessarily go to the disadvantage of taxpayers generally. This is shown by the unsuccessful plea by the finance ministry for a generous transition period, should the Grand Senate hold in favour of the tax office and thus open the way to taxpayers to claim upward adjustment of their accruals on tax audit in the light of the firmer evidence now available on the true extent of the cost. On the other hand, the court explicitly reserved its judgment on provisions based on forecast or estimate.

Supreme Tax Court – Grand Senate – judgment GrS 1/10 of January 31, 2013 published on March 27

Schlagwörter

accrual, expense deferral, subsequent event