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No return of capital contribution in the same year

The Supreme Tax Court has held that distributions to shareholders may only rank as a (tax free) return of a capital contribution if they do not exceed the balance brought forward at the beginning of the year.

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A corporate shareholder gave an investment to its wholly-owned subsidiary as a capital contribution in kind at market value. The subsidiary sold this investment to a third-party on the same day for the same amount. Later, it declared a dividend to its parent which it treated as a partial return of the capital contribution previously received. The tax office refused to accept this treatment, as a capital contribution could not be returned with tax effect in the same year.

The Supreme Tax Court sided with the tax office. It agreed that the statute was not explicit on the point, but held, nonetheless, that restricting returns of capital contributions to the amount brought forward at the beginning of the year was the interpretation of the law that led to systematic consistency. Primarily, all distributions were deemed to come from opening retained earnings regardless of the wording of the shareholder's resolution. Only once that and other sources had been exhausted, were they a return of a shareholder's capital contribution. However, the Corporation Tax Act specifically ruled that a distribution to shareholders could not lead to a negative balance on the capital contributions account. The two provisions together presupposed a common definition, that is, that the opening balance link for the retained earnings also be applied to shareholders' capital contributions. In consequence, contributions made during the year were not available to fund a distribution to shareholders until the following year. The one exception was the special case of a company in its first year of German residence.

Supreme Tax Court judgment I R 35/11 of January 30, 2013 , published on May 29

Schlagwörter

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