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5-year tax deferral on transfer of roll-over relief provision also applied retroactively

The Supreme Tax Court has upheld the German rule providing for immediate taxation (but with a deferral option) of the transfer of a roll-over provision to be held as a fixed asset of a permanent establishment in another member state.

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Tax situation: Under a provision in the Income Tax Act, businesses may defer the tax charge on the capital gain from the sale of certain business assets (mostly land and buildings) by deducting the gain from the cost of a replacement asset. This reduces the basis for amortisation of the replacement asset and also its base acquisition cost for computing any gain on a future sale. The replacement must be acquired within a set time limit (basically four years for the purchase or commencement of construction) and must be held as a fixed asset of a domestic permanent establishment. In the meantime the ECJ has confirmed that charging a gain to tax before it is realised is a hindrance on the taxpayer's freedom of establishment, but has also held that that hindrance is justified by the need to preserve the balance of taxing rights between Member States. A ten-year deferral of the burden is sufficient to alleviate undue hardship, particularly in view of the increasing risk of taxpayer default with the passage of time (ECJ case reference C-657/13, *Verder Lab Tec* Judgment of May 21, 2015).

The German tax administration implemented the ECJ guidelines in the course of the Tax Amendment Act 2015: As an alternative, taxation on the gain reinvested in another member state may be deferred and spread over 5 years. This new option was applicable retroactively in all open cases.

The case at hand: The appellant owned an agriculture and forestry business which he took over from his parents in 2006. The business assets included a roll-over relief provision stemming from a sale of real estate in 2005/2006. In 2010 the provision was partially released and transferred to real estate located in Hungary as part of the business of a local partnership half-owned by the appellant himself. The Hungarian property thus no longer belonged to a domestic permanent establishment of the appellant and, as a consequence, the tax office treated the release amount as taxable income.

The decision: The Supreme Tax Court confirmed this approach in principle and held the German right to taxation to be undisputed. Following recent ECJ case law the court went on to say that the German business reinvesting the gain on the sale of a German asset in a replacement asset in another Member State at least be allowed the option of deferring payment of the tax liability over a period of five years. Although the application for deferral must be made in the year of sale, the Supreme Tax Court held that a subsequent application is sufficient. Since the sale of real estate took place prior to the enactment of the new rules and the respective tax return was also filed before the enactment date (6 November 2015) the taxpayer must be treated as if he had submitted the application in time.

Supreme Tax Court judgment VI R 84/14 of June 22, 2017 published on August 23, 2017

Schlagwörter

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