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By PwC Deutschland | 03. November 2021

Retention period infringement under Section 6 (5) Sentence 6 Income Tax Act due to change of legal form of a parent company at book value

According to a decision of the Supreme Tax Court, where, within the framework of a multi-level partnership, an upper partnership, which indirectly participated in an asset transferred at book value under Section 6 (5) Sentence 3 Income Tax Act ("ITA"), changes its legal form into a corporation at book value, this will be considered an infringement of the retention period under Section 6 (5) Sentence 6 ITA

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Background

The dispute related to whether there was an infringement of the retention period under Section 6 (5) Sentence 6 ITA in a situation where, within the framework of a multi-level partnership, an upper partnership indirectly participating in a previously transferred asset changed its legal form into a corporation at book value.

The plaintiff is a GmbH (limited liability company), which was created by way of change of legal form from B GmbH & Co. KG (B KG). The sole limited partner of B KG was A KG. For its part, B KG was the sole limited partner of Z KG. In the year in dispute (2010), B KG contributed a plot of land to Z KG at book value pursuant to Section 6 (5) ITA. In 2012, both A KG and B KG were transformed into limited liability companies.

The tax office considered the change of the partnership's legal form into a GmbH to be an infringement of the retention period, because the change of legal form within the seven-year retention period under Section 6 (5) Sentence 6 ITA indirectly created a corporation's 100% share in the transferred asset (the business real estate) via its 100% share in the subsidiary partnership.

The Lower Tax Court shared the view of the tax authorities.

Decision

Referring the case back to the Lower Tax Court, the Supreme Tax Court ruled as follows:

- The reference "the share" in Section 6 (5) Sentences 5 and 6 ITA is to be understood as the (direct or indirect) pecuniary interest of a corporate taxpayer in an asset previously transferred under Section 6 (5) Sentence 3 ITA and thus in the underlying hidden reserves.
- The phrase "for another reason" in Section 6 (5) Sentence 6 ITA covers any transaction which – following a transfer under Section 6 (5) Sentence 3 ITA in a chronological sense - leads to the (direct or indirect) creation or increase of the share of a corporate taxpayer in the transferred asset.
- Where, in the case of a multi-level partnership, an upper partnership changes its form to a corporation at book value within the retention period thereby creating an indirect share of this corporation in an asset previously transferred under Section 6 (5) Sentence 3 ITA , an infringement of the retention period under with Section 6 (5) Sentence 6 ITA will be deemed to have occurred.
- A teleological constriction of Sentence 6 cannot be contemplated where, at the time of the change of legal form, natural persons (also) held an interest in the assets of the parent partnership as co-entrepreneurs and thus as co-entrepreneurs already held a (indirect) share in the assets of the business real estate transferred pursuant to Sentence 3.
- If the indirect share - of a corporation participating as a co-entrepreneur in the upper partnership which has changed its legal form - is reduced in the asset transferred under Section 6 (5) Sentence 3 ITA before the change of legal form (retention period infringement), the extent of the partial valuation in accordance with Sentence 6 shall be determined in accordance with the shareholding

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relationships in terms of the assets held at the time of the transfer in accordance with Sentence 3.

Source:

Supreme Tax Court decision of July 15, 2021 (IV R 36/18), published on October 28, 2021.

Schlagwörter

change of legal form, multi-tier partnerships, transfer at book value