

By PwC Deutschland | 04. Dezember 2023

# Excessive payments not tax-free as tips

**In two decisions, the Tax Court of Cologne decided that payments of EUR 50,000 and some EUR 1.3 million respectively made to authorized representatives of a GmbH do not generally qualify as tax-free tips but are rather part of the employment and subject to the personal income tax of the recipients.**

## Background

According to Section 3 No. 51 Income Tax Act (ITA), tipping is tax-free if the tip is paid by third parties to the employee in the course of his work (customer gives employee money directly), if the payment is made voluntarily (otherwise the tip is subject to income tax and social security contributions), a legal claim is waived, and if the amount is handed over as a supplement to work performance (as additional remuneration).

A company with a shareholding in a GmbH paid the two authorized representatives (employees) of the GmbH amounts of EUR 50,000 and around EUR 1.3 million respectively for work performed in connection with the sale of shares and restructuring measures accompanied by a letter expressing „a big thank you for their involvement and the inspiring time together“. In their income tax returns the employees claimed the tax exemption of the payments according to Section 3 No. 51 ITA. The tax office treated the amounts as taxable wages.

## Decision

The tax court of Cologne confirmed the view held by the tax office.

The payments received are taxable as remuneration from employment (wages). According to Section 19 ITA, income from employment includes all salary, bonuses, allowances, benefits in kind from third parties, and all other forms of remuneration given to, or provided for, an employee (in connection with individual services of the employee for the employer). According to the “thank you letter” submitted by the shareholding company and also from their point of view, the plaintiffs received the payments precisely for their successful activity as acting representatives of the GmbH.

Further, the payments are not tax-free solely because of the amount as such but also in view of the overall circumstances. The fact that the legislator has abolished the tax-exempt threshold of EUR 1,224 was not meant to assume the tax limit was to be abandoned altogether in the future and once and for all. Both payments in the case of dispute clearly are beyond the conventional understanding of a tip and not in accordance with the prevailing view of the market.

## Source:

Cologne Tax Court, decisions of 14 December 2022 (cases: 9 K 2507/20 and 9 K 2814/20).

## Schlagwörter

employment income, tax-free