

By PwC Deutschland | 27. Dezember 2024

Merger with retroactive tax effect: No offset of profits from retroactive period with loss carry- back

According to a recent judgment of the Supreme Tax Court, Section 2 (4) sentence 3 of the Reorganization Tax Act also prevents offsetting positive income generated during the retroactive period by the transferring legal entity with a loss carry-back of the acquiring legal entity from the following (post-merger) year.

Background

According to **Section 2 (4) sentence 3 of the Reorganization Tax Act (RTA)**, offsetting or charging positive income of the transferring entity during the period of retrospective application with losses, remaining losses brought forward, unrecovered negative earnings and an interest brought forward under Section 4h (1) sentence 5 Income Tax Act of the acquiring legal entity is not permitted.

The interpretation of this provision was the subject matter of the appeal before the tax courts. **O-GmbH was merged into the GmbH (“the plaintiff”) with retrospective tax effect from 1 January 2013 in accordance with the merger agreement dated 28 August 2013. As of 31 December 2012, the plaintiff had a loss carryforward of around € 1.5 million. As per 31 December 2013, the plaintiff had generated taxable income of around € 600,000 and remained with a loss carryforward of around € 600,000. The following year 2014 finished with a loss of almost € 3 million.**

The tax office rejected the loss carry-back of around € 600,000 from 2014 to 2013 requested by the plaintiff. The Hamburg Tax Court granted the action brought by the plaintiff: Section 2 (4) sentence 3 RTA only prohibits the compensation and offsetting against negative income of the acquiring legal entity that arises or has already arisen in the retroactive period.

Decision

The Supreme Tax Court held the appeal to be substantiated and justified. Contrary to the opinion of the Hamburg Tax Court, Section 2 (4) sentence 3 RTA 2006 (new version) includes the loss carry-back. The case was nevertheless referred back to the lower tax court as it yet has to be examined whether Section 2 (4) sentence 6 RTA prevents the applicability of Section 2 (4) sentence 3 RTA: This is the case if the transferring entity and the acquiring entity are affiliated companies within the meaning of Section 271 (2) of the German Commercial Code prior to the expiry of the tax date of transfer.

The statutory definition “ **unrecovered negative earnings** ” of the acquiring entity also includes the loss carry-back from an assessment period following the assessment period in which the merger takes place. To the Supreme Tax Court, this follows from the parallel language to the provision of Section 10d (1) sentence 1 Income Tax Act which defines the loss carry-back as “negative income that is not offset when determining the total amount of income”.

In the opinion of the Supreme Tax Court, this broad interpretation of Section 2 (4) sentence 3 RTA is in line with the intention and purpose of the provision. The legislator seeks to prevent arrangements which avoid the taxation of profits of companies with significant hidden reserves by offset against tax losses of another company in the retroactive period. This objective includes not only the losses generated by the acquiring entity in the tax year of the merger, but also losses incurred in the post-merger tax year that would then be carried back to the tax year of the merger.

Source:

Supreme Tax Court, decision of 13 March 2024 (X R 32/21) – published on 19 December 2024.

Schlagwörter

loss carry-back, retroactive merger