

By PwC Deutschland | 10. Februar 2025

Disallowance of flat rate holding discount when determining the market value of shares in a corporation from sales

When valuing an unlisted share in a corporation for gift tax purposes a constant flat-rate holding markdown is not acceptable. The market value of an unlisted share in a corporation can only be derived from sales between third parties if the sales take place in the normal course of business and in accordance with ongoing market principles, the Supreme Tax Court said in a most recent judgment.

Background

In the case of dispute, the father transferred shares in the plaintiff, a family holding company, to his children as a gift. The plaintiff determined the value of the shares for gift tax purposes by taking as a reference basis some sixty sales of other comparable shares during a period of 12 months prior to the gift. The sales had primarily taken place between (distantly related) family members. The purchase prices were based on the net asset value of the company together with a flat-rate deduction of 20% as determined by the plaintiff's tax department. The so called 20%-holding markdown is meant to account for impairments resulting from holding costs, financial obligations not included in net financial indebtedness, reduced tradability of the shares in the holding company and limited flexibility of the shareholders due to the specified investment portfolio, among other things. Although the tax office accepted the valuation according to the net asset value method, it did not allow the so-called holding discount (of 20 %). The tax court of first instance took a different view and granted the appeal.

Decision

The Supreme Tax Court reversed the former court's decision and upheld the claim brought by the tax office.

The fair market value of an unlisted share in a corporation can only be derived in accordance with Section 11 (2) sentence 2 Valuation Act from sales between third parties that took place less than one year ago if the sale takes place in the ordinary course of business, and which follows the market economy principles of supply and demand. Whether this is the case always depends on the circumstances of the individual case.

Contrary to the opinion of the tax court of first instance, the value of the transferred shares could not be derived from sales between third parties because the determination of the price had not taken place during ordinary business transactions ("free market").

Accordingly, the net asset value determined by the plaintiff's tax department was acceptable in principle. However, and contrary to the opinion of the former tax court, the holding discount could not be applied. In the case of dispute, the discount was determined by the plaintiff purely on an empirical basis and therefore too generalized to be acceptable for tax purposes.

A constant (unchanged) flat-rate holding discount applied for all years is not to be taken into account when deriving the market value of a share in a corporation if it is not based on the specific nature of the asset and if it cannot be ruled out that it is also intended to compensate for the shareholder's personal restraints on disposal.

According to the established case law of the Supreme Tax Court, discounts used to determine the market value must be applied in an objective and specific manner to the respective asset being valued. In the case of dispute, the discount did not relate to the individual shares sold but rather remained unchanged at a flat rate of 20% over a lengthy period of time.

In addition, according to the plaintiff, it was intended to reflect the fact that holding shares are more difficult

to sell than other company shares due to their internal restrictions. But these are “personal circumstances” that may not be taken into account in the valuation for gift tax purposes in accordance with Section 9 (2) sentence 3, (3) of the Valuation Act.

Source:

Supreme Tax Court judgment of 25 September 2024 (II R 49/22) – published on 6 February 2025.

Schlagwörter

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