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By PwC Deutschland | 05 January 2011

Profit pooling agreement not properly implemented if prior losses ignored

The Supreme Tax Court has rejected an Organschaft as the profit pooling agreement was not properly implemented when the annual profit was surrendered without covering losses brought forward.

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The provisions of the Public Companies Act on profit pooling agreements require full surrender of the annual profit once the losses brought forward have been covered. Covered in this sense means that any loss brought forward must be deducted from the annual income, and only the remainder may be transferred to the parent. The GmbH Act is silent on this matter; however it is long since established case law that GmbHs must follow the provisions governing the profit pooling agreements of AGs. A small group of GmbHs established an Organschaft on this basis, that is, the profit pooling agreement called for offset of prior losses of the subsidiary before surrendering the current earnings. However, as events turned out, a loss brought forward from the year before the start of the agreement was ignored when the subsidiary returned to profitability. Rather, the subsidiary surrendered its full net earnings for the current year after it had received (correctly) a full subvention for its loss of the previous year, the first year of the Organschaft. The Supreme Tax Court did not accept the company's claim that the loss brought forward from the year before had merely been "forgotten" when drawing up the accounts. Neither could it accept that the failure to cover the deficit was of minor importance. On the contrary, first application of current earnings to prior loss offset was fundament to the Organschaft system and was important regardless of amount. Because the offset requirement had been ignored, the pooling agreement had not been properly implemented and the Organschaft was invalid.

The Supreme Tax Court also remarked as an aside that tax audit adjustments leading in retrospect to overs and unders were to be accepted as such. They did not invalidate the Organschaft. (AM)

Supreme Tax Court judgment IV R 21/07 of October 21, 2010 published on December 8

Keywords

Organschaft, loss coverage, offset, prior loss, profit pooling agreement