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Finance ministry refuses foreign parent of Organschaft

The finance ministry has decreed that a Supreme Tax Court judgment accepting a British company as the parent of a trade tax Organschaft is not to be followed as a precedent.

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In February 2011, the Supreme Tax Court held that a British parent company could lead a trade tax *Organschaft*, provided that it fulfilled the then qualifying conditions of financial control, common management and integrated business objectives. The requirement in the Corporation Tax Act that an *Organschaft* parent be a domestic entity was a discrimination prohibited by the UK/German double tax treaty. The German subsidiary's trading income was thus to be added to that of the UK, with the total being split over the local elements of the combined entity. The court accepted that this result could well lead to the loss of trading income to German taxation – the foreign parent would have to file a German trade tax return in its own name – but felt that it could not override the discrimination prohibition of the treaty.

The finance ministry has now issued a decree instructing tax offices not to follow this judgment except in the three cases decided. They should therefore continue to apply the old view of the law in all cases still open to the effect that a trade tax *Organschaft* should always be centred on a domestic parent. It argues that the court's interpretation of the treaty discrimination prohibition is contradicted by the official commentary of 2010 on the OECD Model Treaty, but does not, perhaps wisely, attempt to explain the relevance of a 2010 commentary to a 1964 treaty.

This case could be seen as a fundamental blow to the trade tax system. However, its long-term effects are likely to be minimal. On the one hand the trade tax Organschaft has been equated with that for corporation tax since 2002 – including the requirement for a formal five-year profit pooling agreement – and on the other, a new, modern treaty took effect for 2011. The case can thus be seen as obsolete as a guide to the future, though undoubtedly provides ammunition for those still in dispute with the tax authorities over the past.

The Supreme Tax Court's case reference is I R 55/10, judgment of February 9, 2011 and the ministry's decree is dated December 27, 2011.

Keywords

Organschaft, foreign parent, trade tax