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60% of liquidation loss deductible by natural person significant investor

The Supreme Tax Court has held that that the partial charge business income determination of natural person shareholders with a holding of at least 1% also applies to liquidation losses if a liquidation dividend is paid.

Natural persons with a share in a company of at least 1% at any time during the previous five years earn business income on their investment. Under the partial charge system of taxing business investment income, 60% of the dividends received or capital gains realised is charged to income tax as business income. Correspondingly, 60% of related expenditure and capital losses are deductible. A natural person shareholder disputed the application of the latter provision to liquidation losses on the grounds that the liquidation ended the company and thus ended all possibility of future earnings. He held one-third of the share capital in a GmbH and had received a first and final liquidation dividend of 37%. This was his only receipt from the GmbH throughout its existence.

The Supreme Tax Court has accepted the taxpayer's argument in principle, but rejected its application to the present case. A liquidation loss corresponds to a loss on sale of the investment and is therefore normally only deductible by a natural person shareholder with a qualifying holding as to 60%. If, however, there is no prospect of earning income in the future, and none was earned in the past, the loss is not incurred in connection with earning income. Thus, the 60% limitation must be disapplied and the loss becomes fully deductible as a business loss. However, the term "income" is to be seen in cash terms; thus a liquidation dividend is "income" in this context. Hence, the shareholder had received "income" from his investment and thus fell under the partial charge system in respect of costs or losses.

Supreme Tax Court judgment IX R 19/13 of May 6, 2014 published on July 16

Keywords

business income, liquidation dividend, liquidation loss, partial charge