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Constitutional Court refuses case on non-deductibility of trade tax for companies

The Constitutional Court has rejected a claim that the trade tax charge on companies is unconstitutional in that companies are treated differently from natural persons.

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A company operating a chain of filling stations on leased property objected to its disproportionate trade tax burden in comparison to that borne by sole traders or natural person partners. Its objections were based on the unequal treatment arising from the non-deductibility of the trade tax from the profit chargeable to corporation tax in the face of the (usually) significant relief from a trade tax credit against the income tax due. This lack of deductibility was exacerbated for corporations with significant rental costs due to the disallowance of one-quarter of the assumed implicit interest. The taxpayer also made the point that the lack of a trade tax deduction was inconsistent with the nature of the tax as a business expense. However, the Supreme Tax Court in its judgment of I R 21/12 of January 16, 2014 did not agree that any of these points offended against the constitution, in particular against the equal treatment provision or the ownership guarantee from excessive taxation.

The case was brought to the Constitutional Court who did not accept the constitutional complaint for lack of prospects for success and therefore refrained from making a definite decision on the matter itself. Thus the earlier judgment of the Supreme Tax Court is still valid in its substance.

The Supreme Tax Court had based its judgment (i. e. in the case I R 21/12) on the circumstances of the tax reform of 2007 taking effect for 2008. This reform abolished the deduction for trade tax as a business expense whilst introducing a significant relief from its burden in the form of a credit for natural persons. However, the same reform also cut the corporation tax rate from 25% to 15%. The object of the reform was to improve the apparent German tax climate in comparison to neighboring countries by reducing the nominal rates of taxation whilst broadening the basis of assessment. This objective was constitutionally legitimate, particularly as there was no constitutional requirement for any aspect of the previous trade tax system. The corporation tax rate reduction reduced the effective tax burden on corporations and it was legitimate to partly compensate this with a trade tax increase in the interests of improving the transparency of the tax system. The reformed tax burden on corporations was thus not generally excessive and - in the view of the Supreme Tax Court at the time - there was no constitutional requirement to tax corporations and sole traders in an identical fashion.

Constitutional Court resolution *2 BvR 1559/14* of July 12, 2016; Supreme Tax Court judgment of *I R 21/12* of January 16, 2014

Keywords

non-deductibility, trade tax burden, trade tax charge