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By PwC Deutschland | 14 May 2021

No taxation of bogus income from a Ponzi scheme in the case of tax withheld by fraudster

In a recent ruling, the Supreme Tax Court held that the deemed settlement of final withholding tax under Section 43 (5) Sentence 1, Half-Sentence 1 Income Tax Act (ITA) also applies if the tax has been withheld by the debtor (payer) of the investment income, but not declared and paid over to the tax office. As a result, investment income from a fraudulent pyramid scheme is in principle no longer to be included in the income tax base.

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Background

According to established case law of the Supreme Tax Court, investment income from fictitious profits in the context of a pyramid scheme is also subject to taxation where the investment income is at the disposal of the investor, e.g. by means of a reinvestment (novation), and the debtor of the investment income is willing and able to deliver the relevant performance at that time. This also applies if the Ponzi scheme collapses at a later date and the investor loses his money.

Decision

In the opinion of the Supreme Tax Court, however, the subjective view of the investor is not only to be taken into account in the taxation of the bogus income, but also on the question of whether the settlement of the final withholding tax has been deemed to occur in relation to the tax withheld by the operator of the Ponzi scheme (Section 43(5) Sentence 1 ITA). If the investor could assume that the bogus income had been subjected to a withholding tax deduction, the income tax is deemed settled. This also applies if the withholding tax was not declared and paid over by the fraudster to the tax office and if the fraudster did not have a permit pursuant to Section 32 of the German Banking Act. In this case, however, the bogus income accrues to the investor in full, i.e. also taking into account tax withheld, since the withholding was made for the account of the taxpayer as creditor of the investment income.

Source

Supreme Tax Court judgment of 29 September 2020 (VIII R 17/17), published on 14 May 2021, cf. Supreme Tax Court press release 017/21; see also the essentially identical judgment VIII R 3/20 and the partially identical judgment VIII R 42/18, both of 27 October 2020.

Keywords

Income Tax Act, Ponzi schemes, investment income, withholding tax