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By PwC Deutschland | 31 May 2022

Update: Cum-ex trading is tax evasion

In its decision of 28 July 2021, the Federal Court of Justice held that claiming a refund or credit of withholding tax in the wake of cum-ex schemes is a criminal act of tax evasion. The proceeds obtained in these illegal transactions and the benefits derived therefrom may be collected.

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The accused, two British bankers, were found guilty of tax evasion and handed suspended prison sentences and one of the men was fined €14 million for his role in the scheme and one other bank must repay an amount of approximately €176 million.

Background

Cum-Ex ("Cum Ex") or also known as so called dividend stripping refers to a huge volume of transactions prior to 2012 that involved exploiting an ostensible loophole on dividend payments that enabled a number of parties to claim the same tax refund. “Cum-Ex” trades involved the acquisition of shares with (cum) dividends due on or just before the dividend record date and delivery of these shares after the dividend record date without (ex) dividends, which made it possible to obtain multiple refunds of withholding tax that had only been paid to the German tax authorities once.

The Regional Court, as the court of first resort, sentenced one of the defendants to a suspended sentence of one year and ten months for several counts of tax evasion in the years 2007 to 2011; against the co-defendant a suspended sentence of one year and ten months for several counts of aiding and abetting tax evasion was imposed.

Federal Court of Justice upholds lower court ruling in cum-ex case

With this final decision, the Federal Court of Justice confirmed the opinion of the lower court that the claim for dividend withholding tax based on cum-ex transactions constitutes a criminal offense of tax evasion.

There was no doubt in the court's view that this was an intentional criminal act as the parties involved had deliberately worked towards the payment of unpaid withholding tax due on or just before the dividend record date. At the time the criminal acts were committed, the relevant provisions in the German law already contained clear and unambiguous rules, which the parties involved had violated. This is made abundantly clear through the fact that only tax withheld at source may be claimed by way of a tax credit and a tax refund. Moreover, the case law of the Supreme Tax Court regarding beneficial ownership as referred to by the appellants does not cover such constellations, because the mere conclusion of this type of short sale agreement does not - at any time - give rise to beneficial ownership.

The decision of the Federal Court of Justice has a landmark effect far beyond the individual case. It is the first ruling by the highest court as numerous other criminal proceedings on cases of dividend laundering are still pending.

Update (31 May 2022)

Federal Court of Justice upholds lower court ruling in another cum-ex case

The Regional Court (Landgericht), as the court of first resort, had before sentenced the defendant to a total term of imprisonment of five years and six months on five counts of tax evasion. In its most recent decision of 6 April 2022 the Federal Court of Justice confirmed the Cum-Ex criminal case. According to the findings of the Regional Court, the defendant, Head of Accounting and Controlling Department (until mid-2010) and

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authorized signatory of a bank, was responsible for the cum-ex short sale transactions carried out by the bank in the years 2007 to 2011. The defendant either signed the corporate income tax returns containing false information on - in fact non-existent - refund claims of the bank or checked the prepared drafts and willingly authorized them for signature despite of the false declarations. - -**Source:** Federal Court of Justice, resolution of 6 April 2022 - case 1 StR 466/21.

Source:

Federal Court of Justice decision of 28 July 2021 (case ref. 1 StR 519/20), press release No. 146/2021 of 28 July 2021

Keywords

Tax evasion, cum-ex