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Free transfer of company shares to ensure company succession not necessarily subject to wage tax

According to a recent judgment of the Supreme Tax Court, the gratuitous transfer of shares to senior employees to secure continuity in succession is not taxable as income from employment. The court further noted that there was no automatic presumption that a share transfer to an employee was made in consideration for employee services rendered.

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Background

The plaintiff had been working in the management of a smaller company for many years. As the son of the founding partners - who had originally been foreseen as successor - left the company, it was decided to place the management of the company in the hands of the plaintiff and the other members of the management board to ensure the continuation of the company. For this purpose, the founding partners each transferred 5.08% of the shares to the plaintiff and to four other persons as a gift.

The tax office considered the benefit resulting from the gratuitous transfer to be subject to wage tax under the general rules for benefits in kind. In contrast, the tax court of first instance held that, when viewed objectively, the benefit granted was not derived or the result from the plaintiff's employment.

Decision

The Supreme Tax Court confirmed this latter view.

If an employee shareholding is not transferred at prevailing market price the relevant benefit is determined as the difference between the reduced price compared to the market price. However, the assumption of taxable wages on such benefit also requires that it is granted to the employee “for” his job performance as such.

The Supreme Tax Court went on to say that even if it the transfer of shares was connected to the plaintiff's employment, it nevertheless did not (in a significant enough way) originate from it. There is no automatic presumption that a free share transfer was made in consideration for employee services rendered. Specifically, it may not be assumed from the outset a salary payment (a remuneration for work) if a separately concluded agreement does have an economic content different to that of the employment contract.

The main reason for the transfer in the case of dispute was the arrangement for a smooth future company succession which was obvious for everybody involved. In this situation, the advantage inherent in the transfer for reasons of company law did not constitute remuneration of the executive employees for services provided in the past or to be provided in future.

The transfer of shares was not contingent on the continuation of the employment relationship which the Supreme Tax Court saw as an indication against the assumption of taxable wage. The benefit claimed by the tax office was also markedly disproportionate compared to the gross wages of the recipients.

Source:

Supreme Tax Court, judgment of 20 November 2024 (VI R 21/22) – published on 16 January 2025.

Keywords

employee benefit, employee shares