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By PwC Deutschland | 15 March 2025

Restriction to offset losses from tax deferral models not unconstitutional

Section 15b Income Tax Act dealing with the restriction of loss utilization for tax deferral models does not presuppose that an investment is not economically sensible or has not proved particularly successful. The restriction for an offset and deduction of losses from tax deferral models is also constitutional in the case of a so-called definitive loss. This was currently decided by the Supreme Tax Court who hereby confirmed its previous case law on this matter.

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Background

A tax deferral model within the meaning of Section 15b (1) Income Tax Act (ITA) exists if it is intended to achieve tax advantages in the form of negative income based on a model structure (Section 15b paragraph 2 sentence 1 ITA). This is the case if the taxpayer is offered the opportunity to offset losses against other income at least in the initial phase of the investment and based on a pre-defined concept. Such losses may neither be offset against income from business operations nor against other types of income. A loss carry-back or carry-forward is also not possible. The losses only reduce the income of the taxpayer from the same source of income in subsequent financial years.

In the case of dispute, the plaintiff participated as a limited partner in a GmbH & Co. KG which set up and operated a plant to produce biodiesel from rapeseed. In the prospectus of the closed-end fund, cumulative tax losses of € 3.973 million for the initial years 2005 through 2007 were projected for potential investors. Profits were to accrue from 2008 onwards. Investors were expected to generate a total surplus of around 155% by 2020. However, insolvency proceedings were opened over the company's assets in 2009 and its operations discontinued.

The tax office considered the company to be a tax deferral model and allowed the losses of the limited partners to be offset only against future profits (no immediate offset and deduction). The appeal of the plaintiff against the assessment notice for 2009 was rejected.

Decision

In the opinion of the Supreme Tax Court, the plaintiff participated in a tax deferral model as defined in Section 15b ITA. The assumption of such a model does not presuppose that a specific individual investment is not economically viable or makes little sense. The application of Section 15b ITA is also not precluded by the fact that the losses that could not be offset in 2009 can no longer be offset against later profits from the same source of income due to the insolvency of the company and the discontinuation of the business.

The restriction of the loss offset, and the deduction of losses is found by theSupreme Tax Court to be constitutional also in the event of definitive losses as in the case of dispute. A sufficient material reason and justification for the unequal treatment is due to the legislator’s objective of policy control as pursued by Section 15b ITA and the aspect of avoiding abuse.

Section 15b ITA is meant to limit the attractiveness of tax deferral models which are often based on investments that make little business sense. The explanatory memorandum to the draft bill states that an increasing number of taxpayers are attempting to reduce their tax burden by subscribing to tax deferral models (in particular media funds, new energy funds, ship investments and securities trading funds). According to the explanation of the legislator, the restriction on offsetting losses would create an incentive for greater profitability and put an end to the promotion of economically questionable tax-saving models.

Finally, the Supreme Tax Court notes that the restrictions of loss compensation and loss deduction for tax deferral models in case of partnerships also covers (individual) special operating expenses of the

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shareholder, such as losses from the granting of subordinated shareholder loans.

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Keywords

loss offset, tax deferral scheme, tax loss carry-back