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By PwC Deutschland | 31 March 2025

German-French double tax treaty: Taxation of severance payments and stock options

As the state of employment, Germany has the right to tax a severance payment to the extent that the employee has exercised the activity in Germany. According to a decision of the Supreme Tax Court in the case of cross-border situations, the exclusion to tax benefits in kind from the exercise of share options and comparable rights under tax treaty law is based pro rata temporis on the place of employment of the employee during the vesting period (defined as the period in which the employee is entitled to acquire the options).

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Background

Between 2010 and 2019, the spouses (“plaintiffs”) had a German residence, but their main place of residence and center of life was in France. The plaintiff had been with a domestic employer (a GmbH) since 2011 and worked both in Germany and in France as well as in third countries. In November 2014, the employer informed him of the intention to terminate the employment; the plaintiff immediately ceased his activities at the employer's request and from that point stayed in France. In January 2015, the plaintiff concluded a termination agreement with his employer which provided for a release from work with continued payment of wages until 31 March 2015 and a one-time severance payment. The GmbH had already previously granted the plaintiff stock options and Timely Restricted Stock Awards (rights to a future allocation of shares). The plaintiff was able to exercise the associated rights (options and share awards) in February and March of the year in dispute (2015).

The tax court of Berlin-Brandenburg had dismissed the claim and found that only half of the severance payment and the pecuniary benefits from the employee participation were excluded from German taxation but taken into account when calculating the overall tax rate of the couple’s income (progression proviso).

Decision

The Supreme Tax Court fully agreed with the view of the lower tax court.

Pursuant to Article 13 (1) sentence 1 of the double tax treaty between Germany and France 1959/2001 (DTT France), Germany as the state in which the work is carried out is only allowed to tax income from employment to the extent that the taxpayer actually carried out his or her work in Germany.

The right to tax severance payments as a result of the termination of the employment relationship is determined according to the related work performed and is therefore only available to the (respective) country as far as the employee has carried out his work there in the past. This corresponds to the wording of the relevant article in the DTT France that the income in question must „be derived from a personal activity“.

The benefits in kind from the employee participation are similar benefits within the meaning of Art. 13 (1) sentence 2 DTT France. The activity from which the income “derives”, in the case of both the benefits from the share options and the benefits from the share awards, comprises the work performed by the plaintiff for the GmbH in the past (after the share options or the future share awards were granted) until the time when the share options or share awards could be exercised for the first time (in this case February and March of the year in dispute).

The fact that half of the severance payment has already been subject to tax in France does not prevent it from being taxed in Germany. The plaintiffs can eliminate any potential double taxation by initiating a mutual agreement procedure as laid down in Article 25 DTT France. The respective application must be submitted to the competent authority in the country of residence (e.g. the tax office responsible for taxation of the party concerned).

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Notes:

With this decision, the Supreme Tax Court has confirmed its previous case law on severance payments (decision VI R 52/20,**blog post from 28 October 2024**) and on stock options (decision I R 11/20, **blog post from 8 March 2023**).

The current decision once again deals with the interpretation of Article 13 DTT France. This differs from Article 15 OECD-Model Treaty insofar as the DTT France provides for a strict “activity principle” for determining the right of taxation. As a result, the assessment made by the lower tax court and the Supreme Tax Court is consistent. However, it cannot necessarily be applied to other DTTs.

Source:

Supreme Tax Court judgment of 20 November 2024 (VI R 33/21) – published on 27 March 2025.

Keywords

income from employment, severance payment, stock options