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Tax treatment of shareholder loan granted to asset-managing partnership

A shareholder loan granted to an asset-managing partnership is not recognized from a tax point of view insofar as the company's loan liability is attributable to its shareholder for tax purposes (Section 39 (2) no. 2 of the German Fiscal Code). According to a recent decision of the Supreme Tax Court, the loan agreement neither leads to deductible income-related expenses for the borrower nor to income from capital assets for the lender but is rather considered a tax-neutral contribution. This would be different only in the case of commercially active partnerships.

Legal background

According to Section 39 (2) No. 2 **Fiscal Code** and notwithstanding the general rule contained in Section 39 (1) that assets shall be attributable to their owner, the following provisions shall apply (…):

No. 2. *Assets to which several persons are jointly entitled shall be attributable proportionally to the participants insofar as taxation requires separate attribution*.

Section 15 (1) sentence 1 number 2 **Income Tax Act** (ITA) provides that the taxable income of a business is defined (i. a.) as „the profit shares of the partners of a general partnership, a limited partnership and another company in which the partner is to be regarded as the entrepreneur (co-entrepreneur) of the business, and the remuneration that the partner has received from the company for his work in the service of the company or for the granting of loans or for the transfer of assets“.

Case of dispute

The plaintiff is an asset-managing partnership (GmbH & Co. KG). The shareholders of the plaintiff are K GmbH as general partner with no participation in the company‘s assets and the limited partner F living in Russia. The plaintiff acquired a (developed) property located in Germany and received rental income. To finance the purchase price, the limited partner granted the plaintiff an interest-bearing loan with a term of 15 years and an interest rate of 6% per year. Following an external tax audit, the tax office classified the income which the plaintiff declared as commercial profits as rental income. The tax office did not consider the loan interest as income-related expenses because the loan as such was not acceptable for tax purposes in accordance with the case law of the Supreme Tax Court as regards the rental agreements between an asset-managing partnership and its partner. The Munich Tax Court rejected the appeal brought by the plaintiff.

Decision

The Supreme Tax Court confirmed the decision of the court of first instance and dismissed the plaintiff’s appeal as unfounded.

The plaintiff, as an asset-managing partnership, received rental income from the letting of a developed property in accordance with Section 21 (1) sentence 1 no. 1 ITA. Classification as commercial income within the meaning of § 15 para. 3 no. 2 ITA is not possible because not only K GmbH but also the limited partner F was authorized to manage the business.

The interest expense from the loan which the plaintiff took to finance the purchase price of the rental property are not considered as deductible income-related expenses.

The Supreme Tax Court went on to explain that - when recognizing contractual relationships between the partnership and its partners - tax law distinguishes between

(commercial) partnerships and purely asset-managing partnerships. In the case of commercially active partnerships, contracts and sales transactions concluded with their partners and which establish an external obligation within the meaning of Section 249 Commercial Code are accepted from a tax point of view based on Section 15 (1) sentence 1 no. 2 ITA if they are at arm's length. In contrast, Section 39 (2) no. 2 Fiscal Code must be observed for partnerships that exclusively manage assets because of Section 15 (1) sentence 1 no. 2 ITA which is not applicable there.

In summary, the Supreme Tax Court states that the tax treatment would be different only in case of commercially active partnerships. However, in the case of dispute, Section 39 (2) no. 2 Fiscal Code is applicable to the loan liability because the plaintiff, as a joint and several entity, fulfilled the taxable event under Section 21 Income Tax Act (rental income) since the KG itself was party to the rental agreements. As the loan liability of the plaintiff is fully attributable to F there is no typical debtor-creditor relationship (no difference between creditor and debtor).

Source:

Supreme Tax Court decision of 27 November 2024 I R 19/21– published on 24 April 2025.

Keywords

IFRS (Asset Management), shareholder loan