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Parallel imports of (original) medicinal products may be hidden profit distribution

The Supreme Tax Court decided that so-called parallel imports of (original) pharmaceuticals may constitute a hidden profit distribution on the part of the group's (domestic) sales company and in favor of the (foreign) parent company.

Background

The plaintiff, a GmbH, is part of an international pharmaceutical group with a foreign parent company. A domestic (group) distribution company (subsidiary of the plaintiff) was responsible for the sale of the group's original products in Germany. Due to legal requirements, domestic pharmacies are obliged to purchase part of the goods from parallel importers abroad at significantly lower prices. In economic terms, parallel imports of pharmaceuticals are a consequence of the differing price levels for pharmaceuticals within the EU or EEA.

In the case of dispute, the sales success of the parent company associated with the parallel imports were not remunerated separately even though they were indirectly attributable to the sales activities of the domestic distribution company. As a result, the tax office assumed a hidden distribution (cost savings of the parent company) and increased the taxable income of the plaintiff.

The tax court of first instance was of the opinion that the requirements for a hidden distribution were not met; the tax office had not proven that a third party, which would exclusively distribute original products of the group in Germany, would have been granted a higher net margin than the net margin to which the group-affiliated sales company was actually entitled with regard to the parallel imports.

Decision

The Supreme Tax Court overturned the previous court decision. A hidden distribution due to a transfer of assets as a result of expenses saved at the foreign parent company cannot be excluded. The lower tax court did not consider the fact that the domestic sales company inevitably carried out its marketing activities in the interests of the group as a whole and thus with an (albeit unintended) effect on the parallel imports. This should also have been remunerated since, according to the assessment of the tax court of first instance, the “arm's length remuneration” of the field staff of the domestic sales company based on the total domestic turnover, including the turnover from parallel imports in the assessment basis of the remuneration, suggests that it would be arm's length to recharge these costs.

However, the Supreme Tax Court has not yet been able to reach a final decision on the precise amount of expenses saved by the parent. The tax court must therefore elaborate further in a second hearing.

Source:

Supreme Tax Court decision of 11 December 2024 I R 41/21 - published on 2 May 2025.

Keywords

hidden distributions, third country imports