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By PwC Deutschland | 26 May 2025

Extended trade tax deduction where first property sales occur in sixth year

According to a decision of the Supreme Tax Court, commercial property trading - which is harmful for the extended trade tax deduction - may be precluded under specific circumstances of the individual case if neither property sales nor preparatory measures are carried out within the five-year period and several property sales occur only in the sixth year.

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Background

Extended trade tax deduction according to Section 9 no. 1 2nd Sentence of the Trade Tax Act (TTA): Enterprises, which exclusively manage and use their “own real estate”, may - upon application - make a deduction of that part of the trading income which relates to the management and use of their own real estate. This alternative (i. e. the extended deduction) takes the place of the deduction under Section 9 No. 1 1st Sentence TTA (lump sum deduction of 1.2% of the assessed value of the real estate).

Five-year period and three properties limit: Whether the activities had not gone beyond those of a pure (and thus harmless) asset management is generally determined during a five-year period and provided no more than three properties are sold. If more properties are purchased and sold the local tax office could potentially assume that commercial trading in property has taken place in which case the extended trade tax deduction would not be available.

The plaintiff (a GmbH) was part of a real estate group structure, its sole shareholder is a holding company. The plaintiff had two managing directors who were shareholders of the holding company. Following the acquisition of several rental properties in 2007, one of the managing directors died unexpectedly in 2012. The plaintiff then sold thirteen properties in 2013. The tax office thus assumed that the plaintiff had engaged in commercial property trading from the outset and was therefore not entitled to the extended trade tax deduction in the years of dispute (2011 and 2013). The lower tax court upheld the claim by stating that the high number of sales alone did not indicate the intention to sell already at the time of acquisition.

Decision

The Supreme Tax Court rejected the appeal of the tax office. The five-year timeline is not a fixed period. However, in the case of property sales after more than five years and especially in the case of first-time sales thereafter, further evidence must be provided to assume commercial property trading from the outset. The overall assessment of all circumstances by the lower tax court did not lead to further questions as it did not contradict the previous case law of the Supreme Tax Court in similar cases. A high number of sales

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occurring after the five-year period or a main professional activity in the construction sector does not necessarily lead to commercial property trading. Rather, the lower tax court was also at liberty to consider the unexpected death as a special circumstance in the case of dispute.

The lower tax court had done what it should have done, namely, to analyze and assess the development of the property market and the sales including the two years of dispute (2011 and 2013). The three-property limit within the five-year period was not exceeded - the plaintiff did not sell a single property during the first five years following its respective acquisition. Rather, it sold 13 properties only in the sixth year and two more in 2015. Therefore, and under the given situation, it is fair to conclude that there were no indications from the outset of GmbH's intention to sell.

Source:

Supreme Tax Court decision of 20 March 2025 III R 14/23- published on 22 May 2025.

Keywords

IFRS (Asset Management), extended trade tax deduction