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By PwC Deutschland | 19 August 2025

Partial write- down of partner loan receivable upon termination of business by trading partnership

The fact that a commercial limited partnership (KG) receives income ranking as business income because of the so called „tainting effect“ does not preclude the partial write-off of a worthless loan owed to its partner if the principles of corresponding accounting between partnership and the partners no longer apply because of the discontinuation (cessation) of the business of the KG. Unlike the tax court of first instance, the Supreme Tax Court allowed the loss from the partial write-down to be recognized already at the time of the cessation of the business activities.

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Cessation of business refers to the discontinuation of business activities and the abandonment of essential business resources. **Complete termination**, on the other hand, is the final dissolution of a company, often following liquidation.

Corresponding accounting results in simultaneous recognition in the special balance sheet of the partner and in the balance sheet of the partnership. This ensures that the individual contributions of each partner to the overall result of the company as a whole are appropriately taken into account.

Background:

The case concered the tax consequences of the discontinuation of advertising activities by a trading partnership (L-KG) whose income ranked as income per se due to the so-called tainting effect. L-KG was dissolved under company law on 31 December 2014, and itsbusiness assets were transferred to the plaintiff (a GmbH & Co. KG) as per that date by way of accrual. L-KG operated a restaurant which closed in August 2012; subsequently, no further revenue was recorded. It also no longer employed any staff. The plaintiff had granted a loan to L KG. Even after re-registering the business in 2014, no staff was employed; likewise, no revenue was recorded. The plaintiff's intention was either to be able to continue its negative capital account following the closure of the restaurant or, at least, be allowed to make a partial write-down on its loan receivable from L-KG which was part of the special business assets of the partnership (Sonderbetriebsvermögen), if it were to be assumed that the business had been liquidated and the negative capital account had therefore ceased to exist.

The lower tax court of Muenster had dismissed the appeal. A partial write-off of the loan in the case of L-KG is not already possible upon cessation of operations of L-KG but rather (later) at the time of its complete termination.

Decision:

Unlike the lower court, the Supreme Tax Court held that a loss realization as a result of a partial write-down of a worthless loan from the partner which was part of the special business assets of the partnership was possible already at the time of discontinuation (cessation) of the business (here: of L-KG). Neither did the principles of corresponding accounting nor the fact that the partnership was to be treated as a trading partnership preclude this conclusion. The date on which the partnership was finally wound up (complete termination of business) was not relevant.

TheSupreme Tax Court went on to explain that the reclassification as trading income (fiction) is meant to treat the partnership established by the general partner GmbH in the same way as a corporation for trade tax purposes and to avoid double determination of profits. However, it does not presuppose that a co-entrepreneurial activity that has been terminated because of the closure of the business continues to exist. The mere shell of a commercial partnership does not constitute or imply any commercial activity to be carried out by its partners.

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Conclusion: When determining the gain or loss on disposal, all expenses incurred by the shareholder in connection with the disposal are deductible. The Supreme Tax Court could not finally determine whether, when and to what extent the expenses claimed as special operating losses should be taken into account, and for this reason referred the case back to the lower tax court.

Source:

Supreme Tax Court decision of 12 June 2025 IV R 28/22 - published on 14 August 2025.

Keywords

tainted income, write-down