Capital gains from the sale of shares by a foreign corporate shareholder fully tax exempt

November 2017

In brief

The disposal of shares in a German corporation by a foreign corporate shareholder is generally a taxable event triggering in the German tax authorities' view an effective taxation of ca. 0.8%. In current private equity structures this *tax charge is usually not due because of still favorable tax treaties. However, this landscape may change* in the near future given the OECD's BEPS initiative. A recently published decision of the BFH *may help to keep capital gains free of German capital gains taxes even in the changing tax environment.*

General background

Capital gains from the disposal of shares in a German corporation by a corporate shareholder are generally tax exempt. However, 5% of such capital gains are deemed to be non-deductible business expenses and are therefore subject to German taxation.

In the German tax authorities' view this fiction does not only apply to German corporate shareholders but also to foreign corporate shareholders selling shares in a German corporation. The difference is the tax rate effectively 1.5% in case of a German tax resident shareholder and effectively 0.8% in case of a foreign corporate shareholder without German permanent establishment.

In case the foreign corporate shareholder is tax resident in a country with which Germany has a tax treaty and the foreign corporate shareholder can actually benefit from this treaty (e.g. fulfills the substance test and / or the limitation-of-benefit test of the tax treaty) Germany usually restrains from applying the above.

Land-mark decision

In its recently published decision, the BFH decided that in case of a foreign corporate shareholder (a Bermuda Ltd. in the case at hand) the deemed non-deductible business expenses of 5% are contrary to the German tax authorities' view not to be applied.

Impact of the decision

The impact of this decision is two-fold.

In scenarios where the German tax authorities challenge the applicability of a tax treaty and / or where no tax treaty is available at all and the German tax authorities want to effectively tax capital gains with 0.8% the decision of the BFH may help to defend against the German tax authorities' view.

Further, it needs to be considered that within the ongoing Base Erosion and Profit Shifting (BEPS) initiative of the OECD and the G20, the substance requirements of the tax treaties are likely to be tightened by the implementation of a principle purpose test (or by limitation-of-benefit clauses). Depending on the details of these tests, private equity structures may not met these tests and it may be questionable whether private equity structures can meet these tests in the future. The decision of the BFH may help to keep capital gains of a LuxCo and / or a DutchCo free of German capital gains taxes.

However, as always, when the BFH decides in favor of the tax payers the reaction of the German tax authorities and the German tax law giver needs to be awaited.

We will keep you posted.

Contact

Dr. Ralf U. Braunagel
Frankfurt
Tel.: +49 69 9585-6376
ralf.ulrich.braunagel@de.pwc.com

Nicole Dehnhard
Frankfurt
Tel.: +49 69 9585-2513
nicole.dehnhard@de.pwc.com

Alke Fiebig
Hamburg
Tel.: +49 40 6378-1318
alke.fiebig@de.pwc.com

Hansjoachim Köhler
Frankfurt
Tel.: +49 69 9585-5039
hansjoachim.koehler@de.pwc.com

Dr. Lars Lawall
Frankfurt
Tel.: +49 69 9585-6622
lars.lawall@de.pwc.com

Dr. Axel P. Mielke
Frankfurt
Tel.: +49 69 9585-6926
axel.mielke@de.pwc.com

Jürgen Scheidsteger
Frankfurt
Tel.: +49 69 9585-5150
juergen.scheidsteger@de.pwc.com

Christian Tempich
München
Tel.: +49 89 5790-6321
christian.tempich@de.pwc.com

Subscribe / Unsubscribe

If you would like to subscribe to our English PDF M&A Tax Newsletter, please send an e-mail with “Subscribe” in the subject line to the following address: ADValue@de.pwc.com.

If you would like to cancel your subscription, please send an e-mail with the word “Cancel” in the subject line to the following address: ADValue@de.pwc.com.