

## **Federal Tax Court confirms treatment of acquired accruals**

The Federal Tax Court has refined its jurisprudence relating to “acquired” provisions for jubilee benefits and provisions for payments to pension insurance associations in a transfer of a business.

Under German income tax law, certain provisions for liabilities may not be recognized in the tax balance sheet or may not be recorded in the same amount as for German GAAP purposes. In its decision of 14 December 2011 (case reference: [I R 72/10](#)), the Federal Tax Court (BFH) held that the acquirer of a business may recognize these provisions in its tax balance sheet and may continue to record the items at subsequent balance sheet dates if the provisions are “acquired” (e.g. in the case of an asset deal).

In the case, a German parent company acquired the entire business of its subsidiary in an asset deal. As a part of the transaction, the parent took over certain provisions for jubilee benefits and for payments to pension insurance associations that could not be recorded at the level of the transferor for tax purposes. The parent company, as the acquiring entity, recognized the provisions in its tax balance sheet following the transfer of the business. The tax authorities rejected the recognition.

The BFH, however, ruled in favor of the taxpayer, reiterating its position in a previous case on “acquired” provisions for contingent losses in the case of a business transfer (case reference: [I R 102/08](#), see [GTLN](#)). According to the BFH, liabilities that generally are prohibited from being recognized in the tax balance sheet are part of the acquisition price, so they must be recognized in the first balance sheet reflecting the acquisition. The BFH also rejected the view of the tax authorities that the provisions would need to be eliminated on the following balance sheet date as stated in 2011 guidance issued by the Ministry of Finance; the court confirmed that the liabilities would still need to be reflected also on subsequent balance sheet dates.

The underlying rationale of the BFH should be relevant in reorganizations, such as mergers under the Reorganization Act which are carried out at a value exceeding book value. In a circular dated 11 November 2011, the Ministry of Finance ([BMF](#)) took the view that even if recognized in the course of a reorganization, the receiving entity must eliminate such provisions in the first tax balance sheet following the merger balance sheet. As a result of the Ministry’s position, a gain is regularly created. It appears likely that the BFH also would overrule this interpretation of the BMF.

It remains to be seen whether the legislator will react to the decision by codifying the position of the BMF.

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