

Tax authorities of federal states issue guidance on application of trade tax provisions following CJEU decision

Guidance is an interim solution pending the revision of provisions the CJEU found to violate EU law.

The tax authorities of the federal states of Germany issued guidance on the application of the trade tax provisions on 25 January 2019, following a 20 September 2018 decision (C-685/16, EV) of the Court of Justice of the European Union (CJEU) that the provisions violate EU law.

The CJEU concluded that the trade tax provisions that result in the different tax treatment of dividends received from subsidiaries resident in non-EU countries, compared to subsidiaries resident in EU member states, are in breach of the free movement of capital principle in the Treaty on the Functioning of the European Union (TFEU).

German legislation provides that dividends from domestic shareholdings are exempt from trade tax, provided the parent company holds at least 15% of the subsidiary's share capital. However, the requirements for an exemption in respect of third-country (non-EU) shareholdings are more restrictive. In addition to the minimum holding requirement, the distribution also must satisfy other conditions. The CJEU found those conditions to be in violation of article 63 of the TFEU on the free movement of capital. Until the legislation is revised, its provisions still must be applied, but may be applied only to the extent that they do not infringe principles of EU law.

After a discussion among the representatives of the tax authorities of the federal states, they concluded that the current version of the relevant trade tax provisions should be applied with certain modifications following the CJEU decision and issued guidance on those modifications.

To benefit from the trade tax exemption, the minimum shareholding now must be held only at the start of the relevant fiscal year, instead of throughout the entire fiscal year. Further requirements that non-EU subsidiaries previously had to fulfill, for example to prove that their income is derived from an active business, no longer will be applied.

This effectively means that distributions received from third-country subsidiaries now will be exempt from trade tax under the same conditions as distributions received from domestic subsidiaries. The main condition, thus, will be the minimum ownership of 15% at the beginning of the fiscal year. The abolition of the requirement to prove the active business that is the source of the profits should be a substantial relief for many multinational groups, especially those with multi-tiered structures.

The German tax authorities will act in accordance with these principles for all open cases until the legislation is amended and the revised version of the relevant trade tax provisions enters into effect. Taxpayers that have been subject to these trade tax provisions should ensure that they understand what the guidelines mean with respect to their situation, and act accordingly.

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