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URL: http://mobile.deloitte-tax-news.de/german-tax-legal-news/bfh-asks-federal-ministry-of-finance-to-opine-on-whether-rett-intragroup-exemption-constitutes-state-aid.html

29.02.2016

German Tax and Legal News

BFH asks Federal Ministry of Finance to opine on whether RETT intragroup exemption constitutes state aid

RETT intragroup restructuring clause could constitute unlawful state aid under EU principles

On 25 November 2015, Germany's Federal Tax Court (BFH) asked the Ministry of Finance (MOF) to join a pending case on the intragroup restructuring exemption under the real estate transfer tax (RETT) rules (case ref. II R 62/14). One of the issues on which the BFH requested the MOF's input is whether the intragroup exemption was notified to the European Commission as potential state aid before the implementation of the relevant rule.

Under the RETT intragroup restructuring exemption, certain direct or indirect transfers of real estate/shares in real estate-owning entities are exempt from RETT. One condition for the exemption to apply is that the transaction must involve one controlling company and one or more controlled entities, and a direct or indirect shareholding of at least 95% must exist between the entities for five years before and after the transaction. If this criterion is interpreted based on the literal wording of the rule, the criterion cannot be met where the transaction involves a merger (where the controlled entity is eliminated) or a demerger (where the controlled entity is newly created) because the 95% shareholding either would not survive the transaction or would not exist prior to the transaction, respectively.

In the case, the German tax authorities denied the intragroup restructuring exemption and assessed RETT in a situation where the controlled entity owning real estate was eliminated through an upstream merger. The lower tax court rejected the position of the tax authorities and ruled that the RETT intragroup restructuring exemption generally covers cases where the real estate-owning entity is merged upstream into its parent entity, which consequently leads to a dissolution of the corporate group for RETT purposes since only one entity survives (see prior coverage in the GTLN dated March 25, 2015).

The tax authorities appealed the lower tax court's decision, and the case is now pending before the BFH. Due to the complexity of the rule and the inconsistency of the current administrative guidance, the BFH has asked the MOF to join the case and to provide its views on the rule.

In addition, the BFH has raised the issue of whether the intragroup restructuring exemption could constitute unlawful state aid under article 107 of the Treaty on the Functioning of the European Union. The BFH has asked the MOF to provide its view, and to explain whether the rule was notified as potential state aid to the European Commission before its implementation.

Based on the information contained in the state aid register of the European Commission, no official approval process was initiated before the implementation of the RETT rule. It, therefore, is possible that the BFH could request a preliminary ruling from the Court of Justice of the European Union after hearing the MOF's position. It also is possible that the European Commission could initiate a procedure to consider the issue, independently from the proceedings involving the BFH.

In cases where a measure is implemented without prior notification to the European Commission and it later is determined that the measure constitutes state aid incompatible with EU law, the member state that implemented the measure may be required to recover the aid on a retroactive basis from taxpayers that benefitted from the measure. Final tax assessment notices issued during the previous 10 years could be affected. A member state's domestic law (including binding rulings on the relevant issue) does not permit taxpayers to rely on measures that contravene controlling EU law.

The BFH's actions have created significant uncertainty about the future (and past) application of the intragroup restructuring clause for RETT purposes. Tax practitioners should carefully consider the risk associated with relying on the intragroup restructuring clause.

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