

Local court rules on five-year minimum term of PLTA in retroactive spinoff

The local tax court of Düsseldorf has ruled that the five-year minimum term of a PLTA is not met if the subsidiary was not in existence for the entire period. The retroactive effect of reorganization is disregarded in determining the term of a PLTA.

The local tax court of Düsseldorf issued a decision dated 3 March 2015 (6 K 4332/12 K F), in which the court disregarded the retroactive effect of a reorganization when determining the minimum term of a profit and loss transfer agreement (PLTA).

One of the requirements to implement an income tax consolidated group (Organschaft) between two German companies is that the parent company and the subsidiary (in which the parent company holds a majority of the voting rights) enter into a valid and binding PLTA for at least five years (i.e. 60 months). The five-year minimum term requirement will not be met if the PLTA has been concluded for a period of 5 business years and where the five business years do not cover a full period of 60 months, for example, because one of the business years covers less than 12 months.

Under a PLTA, the subsidiary must transfer all of its annual net income under German GAAP to the parent company. If the subsidiary incurs an annual net loss under German GAAP, the parent company must compensate the loss.

The case before the local tax court of Düsseldorf involved a German corporation (A-GmbH) that concluded a PLTA with its subsidiary (B-GmbH), following a corporate restructuring. The sequence of events is as follows:

- February 2005: B-GmbH established
- August 2005: A-GmbH acquires all shares in B-GmbH
- August 2005: Certain assets of A-GmbH are spun off into B-GmbH, with economic and tax effect as from 1 January 2005
- November 2005: PLTA concluded between A-GmbH and B-GmbH for the period 1 January 2005 through 31 December 2009.

The German tax authorities disallowed the Organschaft between A-GmbH and B-GmbH because the PLTA actually only covered a term of four years and 11 months since B-GmbH was not established until February 2005. According to the authorities, the minimum term requirement can be met only if B-GmbH was in existence for the entire 60-month period.

The taxpayer argued that the retroactive effect of the spinoff for economic and tax purposes as from 1 January 2005 had to be taken into account in determining the term of the PLTA, so that the 60-month term was in fact fulfilled.

The local tax court of Düsseldorf agreed with the tax authorities, concluding that the 60-month minimum term was not fulfilled because B-GmbH was not established until February 2005. As a result, the retroactive effect of the reorganization could not be taken into account when determining the minimum term of the PLTA; the 60-month period is a factual requirement and any deemed/notional retroactive effects are disregarded.

The case illustrates that it may be difficult to determine whether the minimum term requirement for a PLTA is met, and if there are any doubts, a six-year PLTA should be concluded.

The taxpayer is expected to appeal the case to the Federal Tax Court, which will issue a final decision on the issue.

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