

Lower tax court rules change-in-ownership rules partially unconstitutional

Federal Constitutional Court now must rule on the issue

The lower court of Hamburg issued a decision on 29 August 2017, concluding that Germany's change-in-ownership rules, which result in a full forfeiture of tax losses (both carryforwards and current year losses) following a transfer of more than 50% of the shares in a German loss-making entity are incompatible with the constitution. The lower court then referred the case to the Federal Constitutional Court (BVerfG) to rule on the issue.

Under the change-in-ownership rules, net operating loss carryforwards, interest carryforwards and current year losses are forfeited where there is a "harmful change in ownership." A harmful change will exist where there is a direct or an indirect transfer of more than 25% (and up to 50%) of the shares in a company that has loss carryforwards results, leading to a pro rata forfeiture of the carryforwards; and a transfer of more than 50% of the shares results in a complete forfeiture of all available tax loss carryforwards. There are three exceptions to the loss forfeiture rules: the intragroup restructuring exception and the built-in-gains exception (both of which have applied since 2010), and the business continuation clause, which has applied since 2016.

On 29 March 2017, the Federal Constitutional Court ruled that the pro rata forfeiture of tax loss rules infringe the constitution and asked the German legislature to amend the change-in-ownership rules to bring them in line with the constitution, and make the change effective retroactively for the period 1 January 2008 - 31 December 2015. The legislative change should be finalized by 31 December 2018 (for further details, see [GTLN dated 05/15/2017](#)).

The BVerfG now will have to rule on the constitutionality of the rule that results in a full forfeiture of tax loss, and if the court issues a taxpayer-favorable decision, the German legislature may need to overhaul the change-in-ownership rules.

Affected taxpayers should monitor developments and keep relevant periods open (e.g. by filing an objection and applying for a suspension of proceedings by referring to the case before the BVerfG).

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