

Germany

Federal Finance Court Finds Bank Dividends Sale Not Subject To Tax

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In its recently published decision (IR VIII R 21/19) of 15 November 2022, the Federal Fiscal Court (*Bundesfinanzhof*) decided that no tax is due on a UK Bank dividends sale to a US bank.

(a) Facts. The plaintiff was a domestic credit institution (DB AG) that in 2013 managed several German securities on the respective dividend dates for UK-based credit institution AB Ltd., which sold discounted future dividend claims on those shares to the London branch (AC Inc.) of a US corporation 10 days before the distribution. AB Ltd. properly notified the plaintiff about all the sale and dividend claim assignments. In June 2013 DB AG paid the dividends to AC Inc.'s account without paying German withholding tax and declared these payouts accordingly.

After an audit, the tax authorities assessed DB AG for the withholding tax and a solidarity surcharge on the declared amount as it was the economic owner of the shares at the time of dividend distributions.

The tax administration further held that the only aim of the sale of the dividends was to avoid German tax and, therefore, should be disregarded.

The plaintiff challenged that decision arguing that from a comparison with subsequent tax amendments. In particular, the taxation of real estate investment trusts under the German Real Estate Investment Act follows that the legislature did not intend to tax non-residents' capital gains from the sale of future dividends.

(b) The issue was whether the taxpayer has received taxable dividends or tax-exempt capital gains.

(c) Decision. The Fiscal Court of Hesse followed the view of the tax administration and ruled that the plaintiff was obliged to pay withholding tax and a solidarity surcharge. That Court held that AB Ltd. derived dividends and not taxable gains.

The Federal Fiscal Court overturned that decision because AB Ltd. did not derive German dividends. That Court held that after the sale the taxable dividends were converted into capital gains. Upon the dividend distribution in June 2013, capital gains were not listed under the taxable sources of income for a non-resident as listed in articles 20(1) and 49(1)(5a) of the ITA 2013. Also, for resident taxpayers capital gains derived from the sale of future dividends were not taxable. This situation changed with the Income Tax Amendment Act of July 2014, but the modification had no retroactive effect.

Finally, the Court also ruled that the present case does not constitute an abuse of law within the meaning of article 42 of the General Tax Act. The Court considered that AB Ltd. merely used statutorily possible structuring options, which did not constitute abuse. The Court observed that the bank decided not to wait

for the receipt of the dividend payments but instead decided to commercialize its future dividend entitlements earlier by selling them.

Therefore, the Court decided that AB Ltd. did not violate the legislature's intent but only made use of an opportunity granted by the law at that time by selling the dividend claims before the dividends were paid out. The Court noted that a legal structure is only inappropriate if the taxpayer does not use the structure stipulated by the legislature to achieve a specific economic goal, but instead chooses an artificial structure which, according to the legislator's assessment, should not receive its intended goal. This did not apply to the given case. The fact that the dividends were sold shortly before the distribution was also irrelevant because the law did not prescribe any time limit in this respect.

The full text of the decision (IR 11/20) is available [here](#) (in German only).

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