PKF DEUTSCHLAND

Newsletter 04|24

Key Issue

Sustainability reporting – A step-by-step guide

Part II – The materiality assessment

Dear Readers,

In the first report in this April edition of our newsletter we explain how companies can reduce **VAT-related risks** due to the incorrect statement of the VAT element in invoices to final consumers. The reason for this was provided by an ECJ judgement from 2022 whose key statement was recently adopted into the German application regulations by the Federal Ministry of Finance in its circular of 27.2.2024. Subsequently, in our Tax section, we provide an overview of the tax consequences of **real estate sales transactions** in the context of succession cases and own-use.

In the Accounting & Finance section we distinguish between **bridge loans and reorganisation loans** for companies in crisis situations and classify these loans according to the reorganisation phases. What particularly matters here, besides the term of the loan, is the extent to which it functions as a substitute for equity. Next up, as our Key Issue report, is the second part of our series on **sustainability reporting.** In the last issue of our newsletter, we provided an overview of the legal development and the overall requirements as well as of the first of the twelve new reporting standards; there now follows the first major practical challenge, namely, the **materiality assessment**, which requires a thorough examination of a company's own value chain.

The **ban on exports to Russia** has manifestly not yet produced the desired impact because goods are arriving there via circuitous routes. To plug this hole, the EU has issued a new provision that we discuss in our Legal section.

Finally, in short reports, as always you can find current information. Here, it could perhaps be of particular interest for holidaymakers that they can reclaim hotel costs if the poolside sun loungers are constantly reserved.

Then, through the illustrations that break up the reports from our experts, we make a brief visit to our PKF neighbours in the Netherlands.

We hope that you will find the information in this edition to be interesting.

Your Team at PKF

Tulip fields in Southern Holland

Front cover photo: Rotterdam skyline

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Maximilian Würth

Too high a VAT amount stated on invoices to final consumers – The new regulations

Up to now, under Section 14c (1) of the VAT Act *(Umsatzsteuergesetz, UstG)*, businesses have been obliged to pay VAT to their local tax offices even in cases where the amounts were incorrectly stated on the invoices and therefore too high. According to the previous regulations, this applied irrespectively of whether the invoice recipient was a business or a non-business. A recent ECJ judgement has changed how a supply to a final consumer should be treated. The German fiscal administration has now responded to this court ruling.

1. ECJ decision regarding situations where too high a VAT amount was stated

The case dealt with by the ECJ concerned an Austrian GmbH [a limited liability company under Austrian law] that operates indoor playgrounds. The GmbH issued invoices to its customers where VAT was charged at the standard rate even though the services supplied were only subject to a reduced rate of VAT. The competent local tax office required that the invoices be corrected, otherwise the VAT that was erroneously set too high would have to be paid. According to the ECJ judgement of 8.12.2022 (case: C-378/21) there is no risk of a loss of tax revenue because the final consumers of the playground operator's services do not deduct input tax. Moreover, Article 203 of the EU Directive on the VAT system is not applicable with the consequence that the VAT that was erroneously set too high is not payable.

2. Application of Section 14c (1) UStG is limited

The Federal Ministry of Finance *(Bundesministerium der Finanzen, BMF)*, in its circular of 27.2.2024 (refer-

Canals in Amsterdam

ence: III C 2 – S 7282/19/10001 :002), adopted this ECJ judgement into the German application regulations. According to this BMF circular, if a business charges the final consumer an incorrect amount of VAT for a supply that has actually been performed then no VAT will arise under Section 14c (1) UStG. The application of Section 14c (2) UStG remains unaffected, except for the small business regulation.

Please note: An unauthorised statement of the VAT element would however still result in a tax liability.

3. A distinction between invoice recipients

Final consumers as defined by the ECJ are not business owners and business owners not acting as such. Invoices to business owners for their business spheres do not fall under this judgement. In addition, it does not matter whether or not input tax was actually deducted. The theoretical possibility of input tax deduction alone would have adverse consequences for the application of the judgement. In such cases, according to the BMF circular, opting retrospectively and then a partial tax deduction pursuant to Section 15a UStG could not be ruled out and, consequently, there would be a risk of a loss of tax revenue.

4. Separation in mixed cases

According to the BMF circular of 27.2.2024, where there has been a supply to both a final consumer as well as to a business owner for their business (mixed cases) the ECJ judgement shall be applied solely to the final consumer. A separation shall be carried out.

As long as there is no loss of tax revenue, a distinction can be made on the basis of the type of service supplied as to whether the recipient is the final consumer or the business owner who is entitled to deduct tax. The catalogue of services in Section 3a.2(11a) of the ordinance on the application of VAT *(Umsatzsteueranwendungserlass, UStAE)* shall be used for the assessment. However, if it is clear from the outset that the business owner uses the service supplied for non-business purposes then the above-mentioned catalogue will not be used.

5. Business owner's obligation to provide proof

According to the amended UStAE, the business owner would have to provide credible proof to the local tax office that the invoice was issued to a final consumer. If it is not possible to reasonably determine whether the invoice recipient is a business owner or a final consumer then the ECJ judgement would not be applicable. Then again, the fiscal authority would have to establish whether the wrongly stated tax constituted either an incorrect or an unauthorised statement of the VAT element.

Outlook

The issue is how the ECJ judgement will be implemented. Separating between final consumers and businesses can be difficult and could entail administrative costs that are too high for businesses. Moreover, Austria's Supreme Administrative Court *(Verwaltungsgerichtshof, VwGH)* has referred further questions related to this matter to the ECJ. More details could once again be added to the judgement by the ECJ. At the Federal Fiscal Court there are two appeals pending regarding this matter (case references: V R 16/22, XI R 25/23). According to the BMF circular, the principles set out in the ECJ judgement shall be applied to all cases that are still open.

Private real estate sales in the context of succession cases and own-use

Recently, a number of new court rulings with respect to private sales transactions involving real estate were disclosed. The courts ruled on whether or not a taxable profit, as defined in Section 23 of the Income Tax Act, could be assumed within a community of heirs as well as in the case of the waiver of a usufruct right in exchange for consideration as well as in the case of own-used real estate.

1. Background

Private sales transactions involving real estate would generally be subject to tax if the time period between the purchase and sale is no longer than ten years. The only exception to this is for buildings that were used exclusively for own residential purposes during the period between acquisition and sale, or in

the year in which the sale took place and in the two preceding years.

2. Purchase of a share of the inheritance from a community of heirs

The Federal Fiscal Court *(Bundesfinanzhof, BFH)*, in its decision of 26.9.2023 (case reference: IX R 13/22), specified that if a member of a community of heirs purchases an additional share of the inherited estate that includes a property and sells this property at a profit within ten years then this would not be deemed to be a private sales transaction. Specifically, the case involved the inherited estate of a community of heirs made up of A and B; the testator's estate consisted of a property that he himself had used until his death. In 2020, A purchased one half of the share in the community from B for €250,000 and, in 2023, A sold the property for €600,000. From the above-mentioned BFH decision it thus follows that anyone who, as a member of a community of heirs, purchases a share of the inherited estate that includes a property that they then sell within ten years will not trigger a transaction under Section 23 EStG.

3. Waiver of a usufruct right

Furthermore, the Münster tax court, in its ruling of 12.12.2023 (case reference: 6 K 2489/22 E), decided that the waiver of a usufruct right in exchange for consideration did not constitute a sale as defined in Section 23 EStG. In the case in question, a usufruct right over a property was allocated to a taxpayer, in 2008, through a bequest. In 2012, she gave the property to a Kommanditgesellschaft [German limited partnership] in which, as a partner, she held a stake. The rental revenues constituted extraordinary operating income. After she left the Kommanditgesellschaft in 2018, she transferred the usufruct right at a value of €0 to her private assets and, from then on, treated the rental revenues as income from letting and leasing. In November 2019, she waived her usufruct right in exchange for a compensation payment.

A usufruct is an in rem right of use detached from the aggregate of rights involved in the ownership of an encumbered object and, therefore, constitutes an asset within the meaning of Section 23 EStG. In 2018, the taxpayer thus withdrew the usufruct right by transferring it to her private assets. However, the waiver of the usufruct right in exchange for consideration in 2019 did not constitute the sale of the usufruct. This is because a sale requires not only the payment of a consideration for the transfer transaction but also a change in the owner of the right to the asset that has been sold. Consequently, the waiver of the usufruct right would not result in this asset being transferred (back) to the property owner but, instead, to its expiry. In this respect this constitutes a permanent withdrawal of an asset in its substance and, therefore, a transaction akin to a sale that is however not covered by Section 23 EStG.

Please note: Up to now, there has not been a BFH ruling on whether the waiver of a usufruct right in exchange for consideration constitutes a sales transaction or merely a transaction akin to a sale in the context of Section 23 EStG. That is why the Münster tax court permitted an appeal.

4. Own-use real estate

Furthermore, in the context of own-use real estate, the courts also recently ruled on tax exemptions for the sale of a garden plot as well as of a residential property that had been used by the mother(-in-law).

4.1 Sale of a garden plot

The BFH, in its ruling of 26.9.2023 (case reference: IX R 14/22), made a decision on real estate that was almost 4,000 sq. m in size and which was used mainly as a garden. The real estate was subdivided into two sub-areas and, firstly, was used as a residence and then, secondly, sold within the ten-year divestment period. In its new ruling, the BFH clarified in relation to the second sub-area that the tax exemption would only apply if the taxpayer had lived at the property. However, when there is no building on a plot of land then it is not possible to live on the undeveloped plots so that the exemption will not apply. This would also be the case even if part of the plot that had previously been used as a garden is separated off and then sold. Dividing up a previously single asset of land gave rise to the creation of two new assets (plots) whose use for own residential purposes has to be considered separately in each case.

4.2 Provision of an apartment

Furthermore, the BFH, in its ruling of 14.11.2023 (case reference: IX R 13/23), had to rule on an apartment that had been provided to the mother(-in-law) of spouses. After the death of the mother(-in-law), the couple sold the apartment within the ten-year time limit and claimed a tax exemption for the capital

gain on the grounds of own use because the use of the apartment by the mother(-in-law) should be regarded as their own use. In the view of the BFH, the general assumption behind the term 'use for own residential purposes' is that the taxpayer themself will live in the property. The taxpayer themself has to, at least, also use the building. The only situation that would not be detrimental from a tax point of view would be if the taxpayer lived there together with their family member or a third party. Use for own residential purposes would be deemed not to have occurred, in particular, if the apartment had been provided not just to a child who has to be taken into account for income tax purposes but, at the same time, to a third party (e.g., the child's mother).

ACCOUNTING & FINANCE

Nico Deutsch / Dominik Römer

Company rescue via a bridge loan and/or a reorganisation loan

The distinction between a bridge loan and a reorganisation loan plays a fundamental role in business financing. In the following section we first define both types of loan in order to gain better insights into the financing options of companies that have entered a state of crisis. In doing so, the specific features and purposes of the loans will be examined in order to understand their respective roles in the business reorganisation process.

1. The purpose of a bridge loan ...

Bridge loans play an important role as a financing option for companies that are faced with temporary liquidity shortages. This financial instrument makes it possible to bridge the period until there is a decision on the company's ability to reorganise.

Please note: It should be stressed that bridge loans

The Hague – First Chamber building of the States-General against the modern skyline

are not primarily intended for a radical reorganisation. Instead, they can be used as short-term financial support while the review of the company's ability to reorganise is carried out and before the option of an actual reorganisation loan can be considered.

The term of a bridge loan is normally, at most, four weeks. During this period, a great deal of work is carried out on the reorganisation. Bridge loans are generally unsecured and the lenders can call them back at any time, especially if the planned reorganisation fails.

... is not the same as that of a reorganisation loan

Banks or other lenders will grant reorganisation loans to companies that are undergoing a reorganisation or restructuring process. The principal aim of such a loan consists in averting an impending insolvency or eliminating the causes of insolvency proceedings that have already been initiated in order to restore a company's business capability.

A reorganisation loan would be granted with the explicit focus on the upcoming reorganisation, especially if there is a situation of imminent illiquidity. Here, the company would be classified as being in need of reorganisation if, without support measures, the substance of the company that is required for continuing business operations and the fulfilment of existing obligations cannot be maintained. Linking the reorganisation loan to the purpose of the reorganisation can be agreed explicitly or implicitly.

The term of the loan would normally be oriented towards the purpose of the reorganisation; during this period, the aim would be to achieve the defined objective of the reorganisation as per the reorganisation plan.

2. Accounting treatment of bridge loans and ...

Short-term bridge loans are temporary financing measures and do not constitute any long-term components of business financing. Consequently, bridge loans are not considered to be a substitute for equity. This opinion is based on various court rulings and administrative principles where it has been noted that such loans are not automatically considered to be equity equivalents.

The famous cheese market in Gouda

Reporting bridge loans as debt on the balance sheet hinges on the short-term repayment of the loan having to be seriously intended and determined on the basis of objective criteria. If that is the case then the legal rules on equity substitution would not apply. The reason for this is that, under these conditions – irrespective of a company's creditworthiness -, even a neutral lender would be willing to grant a loan.

However, if there are no objective points of reference for 'short-term bridging' (normally four weeks at most) then the equity substitution rules under German company law would have to be applied.

... reorganisation loans

Reorganisation loans are granted when a company clearly needs to be reorganised and has difficulty in raising loans – potentially an indicator that the company is unworthy of credit. Frequently, reorganisation loans serve as a substitute for equity notably if, in view of the crisis situation at the company, external lenders would not have granted a loan without such security.

The accounting treatment will change in the event of a positive forecast for a company's ability to continue as a going concern and a reorganisation through debt. However, if a reorganisation loan is taken out only after an insolvency administrator has filed an insolvency petition on behalf of the company, then, under the Insolvency Code *(Insolvenzordnung, InsO)*, this would be considered to be a claim against the insolvency assets. On the balance sheet, such InsO claims against the insolvency assets have the status of preferential debts and would be paid in preference to the ordinary unsecured debts.

Please note: Such preferential treatment aims to ensure that the claims of creditors that are closely linked with the insolvent company are satisfied before those of others and prior to the insolvency assets being divided among the other creditors.

Conclusion

In practice, it is necessary to clearly differentiate between the two financing instruments. Bridge loans are used for short-term financial support while the review of the company's ability to reorganise is carried out; the aim of reorganisation loans is to avert insolvency and to actively restructure the company. Purposely choosing between these types of loan – frequently also used one after another – can enable companies to ensure their financial stability even under difficult circumstances and, ultimately, to achieve sustainable growth once again.

WP/StB [German public auditor/ tax consultant] Dr Matthias Heinrich

Sustainability reporting – A step-by-step guide

Part II – Selection of topics to be reported in the context of the materiality assessment

While in the first report in our multi-part series of articles we provided a basic overview of sustainability reporting in accordance with the EU's so-called Corporate Sustainability Reporting Directive (CSRD) as well as of the European Sustainability Reporting Standards (ESRS), in the second part of this series we discuss the so-called materiality assessment, which is at the heart of sustainability reporting. A materiality assessment is used to define the individual topics that are to be reported within the scope of the sustainability reporting. Moreover, a materiality assessment provides the company with an overview of the sustainability-related topics that impact on the company's long-term business success. The data that are compiled in this way can also be used strategically in order to ensure the sustainable development of the company.

1. Content and objectives of the materiality assessment

The aim of the materiality assessment is to identify topics that are most important for an organisation and its stakeholders in terms of environmental, social and governance (ESG) issues. In addition, the impacts, risks and opportunities of the respective individual topics are considered. From this a company can derive the topics that it actually has to


University of Groningen

report on. Yet, companies should also use the materiality assessment to define topics for which they would like to build a sustainability strategy. In doing so, objectives will be defined, measures derived and metrics determined that will allow a company's sustainability performance to be evaluated and then about which there will have to be regular and detailed reports in the future.

2. Double materiality – different perspectives for determining the material topics

In order to determine whether or not an ESG topic constitutes a material issue it is necessary to carry out an analysis from two perspectives, namely,

- the inside-out perspective (impact materiality) – the impact of the company on people and the environment;
- the outside-in perspective (financial materiality) – the (financial) opportunities and risks for the company due to external sustainability impacts, i.e., impact on the business, its financial returns and its (enduring) viability.

2.1 Impact of the company

For impact materiality, first of all, it is necessary to identify the actual or potential impacts of the company on people or the environment while taking account of interest groups and stakeholders and then to determine whether or not these impacts are material issues by, for example, defining thresholds. In doing so, the entire value chain within the company has to be examined. This includes both upstream and downstream value chains that are directly linked through business relationships to the company's own business operations or to its own products and services.

Example: For a company that produces batteries it would be necessary to check what elements are used inside the battery (e.g., rare earths) and if their extraction is potentially linked to human rights abuses and the use of child labour.

Whether or not one of the examined topics needs to be classified as being a material issue will then be determined on the basis of

- the scale – how severe is the impact?
- the scope – how widespread is the impact (e.g., in which area can the impact be felt, or how many people are affected by it)?
- the (ir)remediability – can the negative impact be (fully or partially) eliminated?

2.2 Financial position of the company

In the context of financial materiality, data has to be collected on the risks and opportunities that could have an impact on the company's financial position. In this connection, the company shall check to determine whether there are dependencies on natural or human resources that could give rise to a financial risk. Moreover, a company's activities could, for example, have a negative impact on local communities that could result in stricter government controls or reputational damage. The materiality of existing risks and opportunities and their potential financial impacts shall be assessed on the basis of the following criteria:

» probability to materialise;
» scale of financial impacts, possibly taking into account thresholds.

Please note: The respective impacts shall be considered in the short-, medium- and long-term.

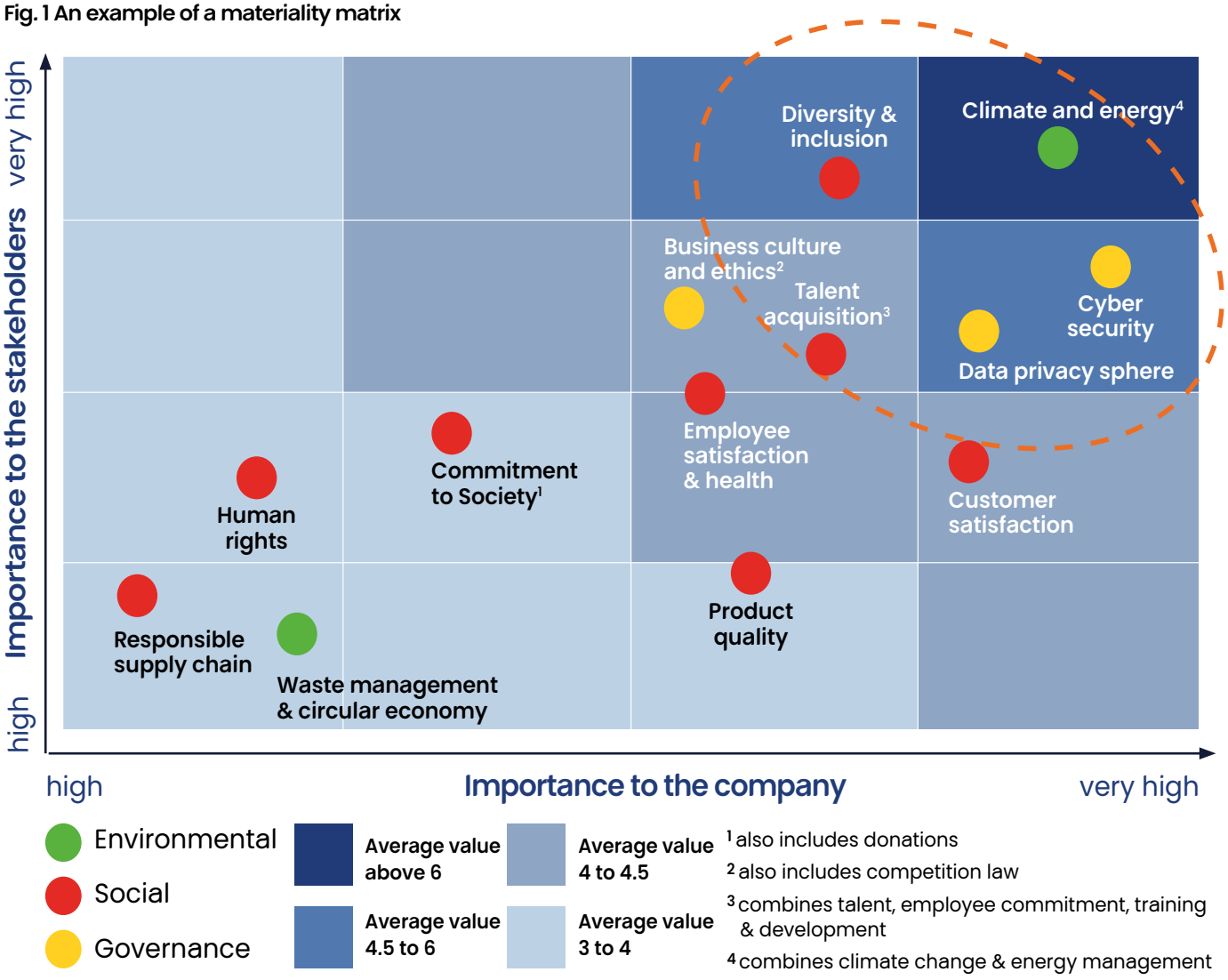
3. The individual steps of a materiality assessment

3.1 Analysis of the business activities and identification of the stakeholders

The first step should be to create an overview of your own business activities and the entire value chain and link these to the relevant stakeholders. In addition, the individual business divisions, production processes as well as the business relationships are analysed and the stakeholders who might be affected are identified. Various parameters could play a role here, for example, the geographical and political situations, the specific environmental situation, regional shortcomings, etc. Besides the information available at the company, media reports should also be included whether about the company itself, about the industry or about the regional aspects.

When allocating the affected stakeholders, a distinction has to be made between internal stakeholders (employees, management, shareholders) and

Fig. 1 An example of a materiality matrix



external stakeholders (customers, investors, suppliers, NGOs, media, political actors, etc.). When allocating the stakeholders to the activities/processes, the groups of stakeholders should also be a ranked according to their importance since not all the groups will be equally important for the company and its sustainability-related decisions.

Please note: Classifying the stakeholder groups in this way should be done not solely from the perspective of the company's management, but rather the different business divisions should be involved in order to get as accurate a picture as possible of the most important external stakeholders.

3.2 Compiling the topics

In a second step, on the basis of the business processes and the stakeholders to be involved, a longlist of topics can be drawn up that will potentially include all the relevant topics with environmental, social and governance aspects. The definitions of the individual topics that have to be considered are set out in Appendix AR 16 to ESRS 1.

Please note: In this step, it is frequently helpful also to consult internal and external experts in order to identify the relevant topics. Moreover, an initial prioritisation of the topics also already occurs.

3.3 Identification of impacts, risks and opportunities

Now the impacts, risks and opportunities have to be determined for the topics on the longlist. This is usually done within the scope of a workshop and discussions with mixed teams in order to be able to collect and take account of the different views and priorities in an interdisciplinary way. Here, it would be possible to proceed as follows:

- identify dependencies on natural, human and social resources;
- identify the impacts on people and the environment;
- identify the sustainability-related opportunities and risks that arise from the identified dependencies and impacts;
- categorise the impacts, risks and opportunities, e.g., according to time horizons (short-, medium- and long-term);
- draw up a shortlist with all the topics for which impacts, opportunities and risks have been collected and validate this shortlist together with the respective key affected stakeholders.

3.4 Evaluation of the impacts, risks and opportunities

The topics on the shortlist will then be assessed on the basis of the criteria shown above in section 2.1, namely, scale, scope and irremediability for the impacts or the probability, and according to the influence on the financial opportunities and risks. Moreover, thresholds can be defined as to when a topic has to be categorised as a material issue.

Please note: In order to be able to carry out detailed assessments it could be a sensible course of action to involve the (external) stakeholders once again in this step, too.

3.5 Materiality matrix

In practice, the topics on the shortlist that have been assessed are frequently entered into a materiality matrix (cf. Fig.1). From this it is then possible to directly read off the topics that will be categorised as material issues. In a final step, these topics will also have to be validated once more by the management. After that, the company will have to report on the topics that have been categorised as material issues in its sustainability report while specifying strategies, objectives, measures and control parameters.

Takeaways

- The materiality assessment is at the heart of the new sustainability reporting on the basis of ESRS.
- The materiality assessment is used to define and substantiate the topics that are categorised as being material issues and discussed in the sustainability reports. This course of action requires special attention.
- The starting point is determining the impacts, risks and opportunities of the sustainability aspects.
- This is followed by an assessment of the materiality of the identified aspects that involves the stakeholders.

LEGAL

RA [German lawyer] Prof. Heiko Hellwege

‘No Russia clause’ – Western sanctions and the need for action by companies

On 26.2.2024 and previously on 18.12.2023, EU member states agreed on packages of further sanctions (no. 13 and no.12) against Russia. A particular focus of package no. 12 was combating the circumvention of the sanctions already in place.

1. The ‘No Russia clause’

In order to curb exports to Russia, the EU member states notably assented to introduce a requirement for exporters to agree a re-export clause for supplies to third countries (Article 12g of EU Regulation 833/2014). Under this clause, the contractual partners based in third countries have to give a commitment not to export the purchased goods and technology onwards to Russia. The background to this is that, in the first nine months of 2023, Russia imported €450m worth of technology that had been produced in the EU. At the same time, EU officials had found that following the Russian invasion of Ukraine the export of these goods from the EU to third countries had increased substantially.

The legal requirement to implement this clause has resulted in a considerable need for action by companies in terms of reviewing their own situation in this respect and formulating an appropriate clause that is adapted to the individual needs of the respective contracts.

The newly added regulation provides that when selling, supplying, transferring or exporting certain

Utrecht Old Town

goods and technologies to third countries exporters have to contractually prohibit the re-exportation of those goods to Russia or their use in Russia. Besides such a clause, the respective contract would also have to include provisions that would apply in the event of a contractual breach.

2. Affected goods

The controlled goods are itemised on the lists of goods that can be found in the Annexes to the Regulation. The clause affects

- the goods and technology referred to in Article 12g that are listed in Annexes XI (especially, goods used in the aerospace industry), XX (especially jet fuels and fuel additives) and XXXV (firearms) as well as
- common high priority items as listed in Annex XL to Article 12g (including circuits, semiconductor components and certain electrical devices).

3. Temporal scope of application and exceptions

The requirement to use such a clause does not apply to contracts concluded prior to 19.12.2023 that have to be fulfilled by 20.12.2024 at the latest or that expire before then (one-year transitional period). Consequently, there is notably a requirement to implement the clause subsequently if the contract does not fall under this transitional period. Sales or supplies to partner countries listed in Annex VII (currently the USA, Japan, the United Kingdom, South Korea, Australia, New Zealand, Norway and Switzerland) to the Regulation are excluded from the scope of application.

4. Ensuring compliance and the notification requirements in the event of breaches

Besides the requirement to use this clause, exporters also have to ensure that it is complied with. According to the guidance published by the EU, contracts also have to include reasonably severe consequences for a breach with the aim of deterring companies based in third countries from any breaches. For example, appropriate contractual penalties or special rights of cancellation could be considered. If a contractual partner learns about breaches, then this partner would have to report these to the competent authority. In Germany, the competent authority is the Federal Office for Economic Affairs and Export Control (Bundesamt für Wirtschaft und Ausfuhrkontrolle, BAFA).

5. Guidance and the EU's model clause

The guidance provided by the EU states that companies are themselves free to formulate their own appropriate wording for the 'No Russia clause', as long as the wording fulfils the requirements of Article 12g of the Regulation. Nevertheless, a model clause in English has been made available that, in the opinion of the EU Commission, meets the requirements.

Please note: If the model clause is used for contracts that would be subject to German law there would however be special requirements notably with respect to the use of general terms and conditions. For example, if the determination of the level of the contractual penalty is not clear in the model clause, then this would conflict with German law pertaining to general terms and conditions.

Recommendation: On account of such specificities and in view of the possible sanctions, we would recommend that before using the model clause it should be adapted to the individual requirements of the respective contracts.

6. Penalties for a failure to enforce

If a 'No Russia clause' is not included in the contract with a customer then under German civil law the customer would be under no corresponding obligation and there would thus also be no penalty should the customer supply to Russia insofar as there is no embargo under the jurisdiction applicable to the customer. The EU-based exporter however would, in this case, be in breach of its obligation under the EU Regulation and this could result in administrative and criminal penalties for the company as well as for the persons acting on its behalf. If the non-EU foreign customer refuses to accept the clause, then it may not be supplied.

Conclusion

In view of the scope of the affected goods, companies need to check whether and if so, which contracts will be affected by the requirement to implement a 'no Russia clause'. In view of the risk of penalties in the event of a breach and the fact that such a clause will depend on the requirements of the respective contracts, careful and case-specific formulation of the appropriate wording would be advisable.

IN BRIEF

Sale of partnership interests – Earn-out payments only have to be taxed when they are received

When stakes in a partnership are sold, besides a fixed purchase price, the contracting parties sometimes also agree variable purchase price components that are based on the company's (subsequent) profits or revenues. According to a more recent ruling by the Federal Fiscal Court *(Bundesfinanzhof, BFH)*, these so-called earn-out payments only have to be taxed at the time when they are actually received by the vendor. Therefore, they may not be included – also not retroactively – in the gain on the date of the sale (no retroactive effect).

According to a BFH ruling of 9.11.2023 (case reference: IV R 9/21), claims for payment of the purchase price that are profit-related and sales-related may only be reported when the vendor realises them on the date they are received. They constitute purchase price claims subject to a condition precedent where, initially, it is not yet clear whether or not the claims will arise and in what amount. In the view of the court, these uncertainties justify excluding these types of payments from the calculation of capital gains as at the closing date.

Outcome: Earn-out payments have to be taxed as subsequent operating income at the time when payments are received. As in the case in question, this might even be several years after the sale of the stake.

Travel regulations – Poolside sun loungers that are constantly reserved could constitute defective performance

Recently, the Hanover District Court had to rule on the consequences of a dispute at a hotel pool. The subject of the dispute was the poolside sun loungers that were reserved for hours on end but never used. The court had to decide if and when such 'marking behaviour' by certain holidaymakers constitutes defective performance that can trigger corresponding claims.

In the case that was decided by the Hanover District Court, in its ruling of 20.12.2023 (case reference: 553 C 5141/23), a man (M) had booked a package holiday to Rhodes, for himself and his family, worth more than €5,000. The hotel had several swimming pools and around 500 poolside sun loungers. Moreover, rules of behaviour had been laid down according to which guests were not allowed to reserve the sun loungers for more than 30 minutes without using them. However, only a few guests observed this requirement. M therefore complained several times about the behaviour to the hotel management who did not however do anything about the breaches of the rules of behaviour. Ultimately, M demanded a refund of a portion of the price of the holiday in the amount of almost €800. The tour operator disagreed with the opinion that this constituted defective performance.

The District Court awarded the holidaymaker M compensation in the amount of €322.77. In the view of the Hanover District Court, a package holiday would be unsatisfactory if the hotelier in a hotel complex either makes too few poolside sun loungers available, or does not intervene when other guests reserve these, by means of a towel, for longer periods without actually using them. Admittedly, a tour operator or a hotelier acting on its behalf are not obliged to make a sun lounger available to every hotel guest. Nevertheless, the number of sun loungers should be in reasonable proportion to the hotel occupancy and thus the number of hotel guests. However, if there are not enough sun loungers so that, as in this case, they effectively cannot be used by some holidaymakers because of the behaviour of others then the hotelier or the tour operator would be obliged to intervene.

AND FINALLY...

“When we do our best, no one can beat us.”

John Joseph Donahoe II (born on 30.4.1960, in Evanston, Illinois/USA) was CEO of eBay from 2008 to 2015. He has been the CEO of Nike since 2020. Donahoe celebrated the kit supplier deal with the German Football Association (DFB) with the above-mentioned quote.

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