



KMLZ VAT NEWSLETTER

Federal Fiscal Court confirms 6% rate interest on tax arrears

1. Introduction

Following sec 233a and sec 238 German Federal Fiscal Code, a fixed interest rate of 0.5% per month (6% per annum) is applied to tax arrears. This is supposed to offset the financial benefit a taxable person has enjoyed by underpaying taxes. The interest rate was introduced in 1999. Meanwhile, however, the ECB's key interest rate has dropped to 0% per annum. Against this background, it is often questioned whether the interest rate in sec 238 German Federal Fiscal Code is still lawful. The Court has now again had the opportunity to comment on this matter. In its recently published decision of 9 November 2017 (case no: III R 10/16), the Court confirmed the rate in sec 238 German Federal Fiscal Code. However, the Court's judgement refers to income tax. As opposed to income tax, VAT is based on harmonised European law. So, the interest rate must comply with both the constitution, as well as the conditions set out by European law. Consequently, in the area of VAT, there is still hope for a breakthrough in the fight against interest on arrears of tax.

6% is constitutional and proportionate

According to the Federal Fiscal Court, a fixed interest charge of 6% per annum on tax arrears does not violate the general principle of equal treatment or the prohibition of excessiveness. Following sec 233a and sec 238 German Federal Fiscal Code, interest is due if a tax assessment leads to a subsequent payment in respect of an earlier tax assessment. Nevertheless, there is hope: The decision was applied to income tax in 2013. As VAT is based on European law, different stipulations could be applicable to it.

2. Facts

In the case at hand, the Plaintiff filed his income tax return for 2011 in December 2012. He expected income tax arrears of EUR 300,000. Therefore, the Plaintiff voluntarily paid EUR 366,400 to the tax office in July 2013. In September 2013, the tax office issued the income tax assessment, which resulted in tax arrears in the amount of approx. EUR 390,000. The tax office charged interest on the tax arrears pursuant to sec 233a and sec 238 German Federal Fiscal Code. The interest charges for the periods April 2013 to September 2013 amounted to approx. EUR 11,000. The taxable person filed a lawsuit against the interest assessment.

3. Legal appraisal

The Federal Fiscal Court decided that the interest rate stipulated in sec 233a and sec 238 German Federal Fiscal Code is constitutional and proportionate. Furthermore, the tax office was not required to remit interest on equitable grounds.



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3.1 Principle of equal treatment

First, the Court denies that the interest rate of 6% per annum violates the general principle of equal treatment as contained in Art 3 para 1 of the German constitution. It compared taxable persons who are required to pay interest with taxable persons against whom no interest was assessed. The Court could base its decision on the existing jurisprudence of the Federal Constitutional Court. The interest rates on tax arrears are based on the unifying assumption that a person, whose tax is completely or partly assessed later, has a cash-flow advantage and thus a potential financial advantage compared with a person whose tax was assessed at an earlier time. Therefore, these two groups cannot be compared with each other. Moreover, within each group, the same regulations can be applied. In this respect, the principle of equal treatment is not violated.

3.2 Proportionality

According to the Court, the interest level does not violate the constitutional principle of proportionality. In this context, the Court analysed interest rates for different short and long-term deposits and credits based on data provided by the German Central Bank. For 2013, interest rates ranging from 0.15% to 14.70% were the result. Consequently, the legal interest rate was considered to be set within the range of realistic reference values.

3.3 Remission on grounds of equity

Ultimately, the tax office was not required to remit interest on arrears of tax on equitable grounds. The Plaintiff claimed that the tax office had delayed the issuance of the tax assessment.

The Court points out that the interest on tax arrears is deliberately set independently of the behaviour of both the taxable person and the tax office. In general, a tax remission on equitable grounds cannot be based on any specific behaviour.

4. Consequences

This judgement once again demonstrates that a legal remedy, which seeks to attack interest on tax arrears based on constitutional concerns expressed against the interest rate, has little chance of success. Hence, taxable persons should ensure that they pay taxes in full and on time. A granted suspension of execution does not freeze the accrual of interest.

Nevertheless, there is still hope for VAT. Although, constitutional arguments have little chances of success. Interest rates on arrears of VAT must comply with principles of the EU VAT Directive. The ECJ recently confirmed this. (ECJ judgement of 28 February 2018 – Rs. C-387/16 – *Nidera*, Tz. 25). Especially, the principle of VAT's neutrality can be violated by a fixed interest rate. In this context, the ECJ has decided that German interest charged on tax arrears infringed the EU VAT Directive if they have an effect like that of a fine and where they punish the taxable person for breaching formal requirements of VAT law (ECJ, judgement of 15 September 2016 – Rs. C-518/14 – *Senatex*, Tz. 42). The case concerned the refusal of a retroactive input VAT deduction from invoices with missing invoicing requirements that were subsequently corrected. On the other hand, a generalized interest rate charged with respect to tax claims is permitted, according to the ECJ, at least with reference to VAT refunds (ECJ, judgement of 28 February 2018 – Rs. C-387/16 – *Nidera*, Tz. 36).