



KMLZ VAT NEWSLETTER

Interest on taxes unconstitutional?!

1. Introduction

In our Newsletter 10/2018 of 07.03.2018 we outlined a judgment by the 3rd Senate of the Federal Fiscal Court. In this decision, the Senate assumed the fixed interest rate of 6% p.a., pursuant to sec 238 of the German Fiscal Code, to be constitutional (Federal Fiscal Court, decision of 09.11.2017 – III R 10/16). This decision confirmed what had been repeatedly decided by both the Federal Fiscal Court and the regional fiscal courts. Appeals submitted against interest assessments were deemed to have little chance of success. Now, the 9th Senate of the Federal Fiscal Court has surprisingly arrived at a different result (Federal Fiscal Court, decision of 25.04.2018 – IX B 21/18). It considers the interest rate of 6% p.a. to be unconstitutional. In doing so, it expressly objects to the judgement of the 3rd Senate of the Federal Fiscal Court. The decisive factor for this decision was a paper by the Research Service of the German Bundestag. Taxpayers should now appeal against each interest assessment on tax arrears, as well as applying for a stay of execution. Under certain circumstances, taxpayers might even be able to get paid interest refunded.

Federal Fiscal Court doubts constitutionality

The 9th Senate of the Federal Fiscal Court has voiced “serious doubts” as regards the constitutionality of the interest rate on tax arrears. The rate is 0.5% per month (i.e. 6% per year). The court considers the interest rate to be “unrealistic” and that it violates the general principle of equal treatment pursuant to Art 3 para 1 of the German Constitution. Furthermore, the court regards the interest rate as excessive, thereby infringing Art. 20 para 3 of the German Constitution. As a consequence, taxpayers should appeal against interest assessments on tax arrears and apply for a stay of execution.

2. Facts

The Federal Fiscal Court’s decision was taken within the framework of an application for suspension of execution of interest. The background was as follows: The tax office initially assessed income tax to be paid by a married couple for the year 2009, amounting to EUR 159,139.00. Following a later external audit, on 13.11.2017, the tax office increased the assessed income tax to EUR 2,143,939.00. This led to an additional tax payment of EUR 1,984,800.00. Further, the tax office assessed interest on tax arrears of EUR 240,831.00 to be paid with respect to the period 01.04.2015 to 16.11.2017.

The married couple appealed against both the income tax assessment and the interest assessment. Further, they claimed suspension of execution of the interest assessment, due to the fact that it was unconstitutional. The tax office and the court of first instance rejected the claim for suspension of execution. The married couple thereupon filed an appeal with the Federal Fiscal Court.



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3. Reasoning of the Court

The 9th Senate of the Federal Fiscal Court granted the couple's application. It expressed "serious doubts" as to whether the interest rate of 6% p.a., charged pursuant to sec 238 of the German Fiscal Code, was constitutional.

3.1 Infringement of the principle of equal treatment

To date, the fiscal courts have considered that the interest rate upholds the principle of equal treatment. The interest rates on tax arrears are based on the unifying assumption that a person, whose tax is completely or partly assessed later in time, has a cash-flow advantage and thus a potential financial advantage compared to a person whose tax is assessed at an earlier time.

However, the 9th Senate is of the opinion, that the unifying assumption must be adapted to a realistic standard case. A fixed interest rate of 6% per year would contradict this requirement. As of 2015, at the latest, Germany has been in a "sustainably stabilized" low-interest rate phase. Moreover, the fiscal authorities can nowadays assess interest based on a variable interest rate by using modern IT. In this regard, the 9th Senate refers to the Bavarian Community Charges Act. Here, community charges are assessed based on an interest rate of 2 percentage points above the base rate.

3.2 Infringement of the principle of proportionality

According to the 9th Senate, the interest rate also infringes the principle of proportionality laid down in Art. 20 para 3 of the German Constitution. Due to the low-interest rate phase the interest is a "sanctioning unduly additional payment". There is no factual justification for this.

4. Consequences for the practice

The 9th Senate's decision is a preliminary decision in proceedings concerning a suspension of execution. Nevertheless, the consequences of the decision are enormous.

Taxpayers should now appeal against each interest assessment for tax arrears. In this context, appeals must be expressly addressed to the interest assessment. It is not sufficient to merely appeal against the underlying tax assessment. Furthermore, taxpayers should file a separate application for a stay of execution of the interest assessment. Since no interest is imposed on unpaid interest, there is no financial risk involved. Where taxpayers have appealed against an interest assessment and paid the interest, they may ask for a preliminary reimbursement of the said interest. In this case, taxpayers need to claim for an annulment of the execution. On the other hand, it is unlikely that the tax authorities would grant a waiver of interest based on the decision of the 9th Senate.

There are currently six further proceedings pending before the Federal Fiscal Court as regards this legal question. Half of them will be decided by the 8th Senate. Thus, the 8th senate has a key role. In the end, it is up to the German Constitutional Court, who has the last say in this matter. It is certainly advisable for the legislator to take action now.