Debt Restructuring Measures
to overcome the Crisis

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The restructuring of companies often fails because of prohibitive tax implications caused by restructuring measures. Many of these can be avoided or at least be mitigated by proper tax planning.

Part A

Part A describes problems and possible solutions. Discretionary decisions are of considerable importance in this context (e.g. restructuring decree by the Federal Ministry of Finance). Experiences regarding restructuring measures and their implementation with regard to creditors and shareholders are illustrated. However, it is usually advisable - and, according to our experience, also possible - to get an advance ruling or at least a non-binding statement from the tax authorities.

Part B

Part B deals with different scenarios. Only very few of them are currently under review by the fiscal authorities. For some problems the current law does not offer satisfactory solutions. In this respect, tax law and administrative decrees should be amended.

Part C

Part C. I. summarizes typical scenarios and their potential tax implications. In Part C. II., a table illustrates possible implications of debt restructuring measures regarding the qualification of (former) debt instruments as debt or equity for tax and GAAP purposes.

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A. Need for Restructuring Measures in the current economic Situation and Need for Action by the Legislature and the Tax Administration

For many companies, restructuring measures are essential in the current economic crisis. Due to the decrease of revenues and incoming orders, it becomes increasingly difficult to fulfill the interest payment obligations. Debt has to be reduced and new equity has to be raised. In particular, highly leveraged multi-billion investments in German real estate have to deal with these issues.[1]

Besides the economic implications of restructuring measures, long-term tax consequences have to be analyzed carefully. An unconsidered tax burden can put the entire reorganization at risk – even after several years. Negative tax effects may occur not only at the level of the company but also at the level of the shareholders and the creditors and, thereby, may affect their willingness to participate in restructuring measures.

This paper shall give an overview on the tax treatment of certain restructuring measures, in particular equity injections from existing owners and new investors as well as the restructuring of debt. Due to the diversity of possible restructuring scenarios, the overview is not exhaustive.

This paper does not deal with issues concerning the relocation of the Center of Main Interest (CoMI) within the meaning of the insolvency law. Such relocation of CoMI to a foreign country could lead to the non-applicability of German insolvency law.[2]

I. Measures to increase Equity in the GAAP Balance Sheet

An impending insolvency can be averted through equity injections. In addition, the degree of creditworthiness will be improved. Negative tax effects can often be avoided when new equity is injected into the company.

The efforts to obtain necessary liquidity could be facilitated by measures that increase the equity in the commercial balance sheet, for example:

- profit-realizing but tax-neutral transfer / spin-off of
  - a business or separable part of a business Reorganization Tax Act ((RTA) sec. 20, 24) or
  - specific assets (sec. 6 para. 5 ITA));

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1 In Handelsblatt, 16 March 2009, p. 1: At the moment banks are reluctant to cancel credit agreements and to take over real estate portfolios, says Sal. Oppenheim analyst Thomas Rothäusler. That is the reason why most of them agree to follow-up financing even if the debt ratio agreed on or other agreements have been breached. “We try to develop practical solutions together with our clients so that they are not driven to foreclosure”, says a representative of Eurohypo with regard to extensions. The reason: There is hardly a bank which wants to exploit real estate portfolios by itself, especially as distress sales lead to a further decrease of market prices. “The amount of extended credit agreements has risen significantly” […]. “The question is, however, how long the debtors can rely on that”, says analyst Rothäusler. Even now there are exceptions to the rule. E.g., the Landesbank Berlin recently cancelled the credit agreement with Carlyle so that the financial investor sent the company founded for setting up the apartment and shopping center Ihme-Zentrum in Hannover into insolvency.

2 Cf. in detail Breuninger in: Arbeitsbuch zur 60. Steuerrechtlichen Jahresarbeitstagung 2009 der Arbeitsgemeinschaft der Fachanwälte für Steuerrecht e.V,. p. 197 et seq. with further citations.

- profit-realizing but tax-privileged transfer of shares within the group (sec. 8b Corporate Income Tax Act (CITA) (CITA)), however, subject to negative implications for existing loss carry-forwards (sec. 8c CITA).

Obviously, especially those assets with (still) substantial hidden reserves should be considered for such a transfer / spinoff, primarily real estate, but also intangible, (to this point) not capitalizable assets such as trademarks, patents, licenses. Such measures can be combined with sale-and-leaseback structures aiming at de-consolidation with the participation of third parties.[3]

II. Measures to utilize Losses for Tax Purposes

The offsetting of losses for income tax purposes has been curtailed substantially in recent years. According to sec. 10d para. 1 sentence 1 ITA, the loss carry-back is limited to € 511,500 (€ 1,023,000 for spouses filing jointly). The so-called “minimum taxation” applies to loss carry-forwards. According to sec. 10d para. 2 sentence 1 ITA, a loss carry-forward is permitted up to an amount of € 1 million (€ 2 million), but above this limit only in an amount corresponding with 60 % of the total taxable income. The remaining losses are not deductible, but may be carried forward to the next assessment period (sec. 10d para. 2 sentence 1 ITA). For trade tax purposes, only a loss carry-forward is permitted with corresponding limitations (sec. 10a Trade Tax Act (TTA)). In case of a change in ownership, loss carry-forwards from previous years and current-year losses can be partially or even completely forfeited (sec. 8c CITA, sec. 10a sentence 10 TTA).

Due to the restrictive loss offsetting rules, it may be beneficial to balance the losses with tax-relevant gains before starting the implementation of restructuring measures. This could be achieved through the amendment of existing contracts and / or internal procedures, particularly if such losses can be "converted" into future expenses.

Thus, the realization of hidden reserves can lead to a tax-efficient offsetting of losses and, simultaneously, to an increase in equity. Hidden reserves can be realized by selling or contributing an asset. However, due to new add-back provisions for trade tax purposes, formerly popular sale-and-leaseback arrangements might no longer be suitable and should, therefore, be critically examined.

In addition, the RTA allows the tax-neutral transfer of a profitable business or a separable part of a business (secs. 15, 20 RTA). Furthermore, the merger of a profitable company into a loss-generating company can be considered. It should be carefully analyzed whether such a measure is harmful according to sec. 8c CITA.

In some cases, a fiscal unity could be established in order to offset losses of a group company with profits of another affiliated company. The entire income of the participating companies will be attributed to the group parent company, leading to a pooling of profits and losses. Profits generated in a group company can be offset with loss carry-forwards of the parent company. Conversely, however, the offsetting of group companies’ loss carry-forwards with

[3] Cf. for example: “Verborgene Schätze”, in: brand eins, vol. 11, journal 3, March 2009, p. 98 et seq.

profits of the group parent is not permitted. Such pre-fiscal-unity losses can only be used after the termination of the fiscal unity.

The offsetting of losses generated in a foreign corporate subsidiary is not permitted by German law even if the loss cannot be offset anymore in the foreign jurisdiction. In this respect, the German provisions are not compatible with the decision of the ECJ in the Marks & Spencer[4] case.

III. Need for Action by the Legislature and the Tax Administration

Necessary equity contributions by existing shareholders and in particular by new investors as well as the restructuring of financial liabilities are hampered by unfavorable tax rules. There is an urgent need for action by the legislature, but also by the tax administration, especially in the following areas:

- Clarification regarding the applicability of the decree issued by the Federal Ministry of Finance with respect to the tax treatment of so-called “restructuring gains, in particular due to the waiver of a loan receivable, and the extension of these rules to shareholder loans. Preferably, the Federal Government or the top fiscal authorities should issue a decree on the basis of sec. 184 para. 2 General Tax Code (GTC) that provides for the immediate applicability of the income tax treatment also for trade tax purposes.[5]

- The unlimited use of losses and loss carry-forwards, if necessary also the extension of the currently extremely restricted use of loss carry-backs, at least in cases of restructuring. In this context it should also be considered that internal restructurings within world-wide operating groups of companies, which may in some cases even be mandatory under the law of foreign states as part of their rescue programs, cannot be “controlled” by domestic group companies.

- Ensuring that business-incurred expenses and losses are tax deductible. The fact that losses resulting from the decrease in value of a shareholder loan are irrelevant for tax purposes (sec. 8b para. 3 sentence 4 CITA), whereas the waiver of the loan leads to a taxable gain at the level of the financially suffering subsidiary, is inacceptable and results in unsystematic consequences which violate constitutional principles and also aggravate the crisis.

- Abolishment / suspension / reform of the interest barrier rule. Due to rescue measures of the German government (SoFFin) for the benefit of almost all relevant banks, hundreds of companies which are directly or indirectly state-owned might, at least in principal and, presumably also in reality, be negatively affected by the interest barrier rule. The banks might be also burdened with significant additional trade tax because it cannot be ruled out that rescue measures in the form of silent participations are in-fact atypical silent partnerships.[6]

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4 European Court of Justice, decision dated 13 December 2005, C-446/03.

5 Already factually in effect in the City State of Berlin; also cf. the recommendation made by the Bavarian Regional Tax Office, dated 8 August 2006, DB 2006, p. 1763.

6 No. 91 – 93 of the Decree of the Federal Ministry of Finance regarding the interest barrier rules, dated 7 July 2008, Federal Tax Gazette I 2008, p. 718 should not be applicable.

- Clarification that the acquisition of non-performing loans, especially by related companies, is not subject to Value Added Tax (VAT).

- No real estate transfer tax, at least on transactions within a group of companies, in particular on transactions with the purpose of financial restructuring. Not all transactions trigger real estate transfer tax, as special exemption rules may apply (e.g., sec. 5 Real Estate Transfer Tax Act (RETT Act)). Possibly, the spin-off of a business unit onto a new subsidiary partnership, which is transparent at least for corporate income tax purposes, is an alternative to be considered.[7]

IV. Legislative Initiatives

1. Interest Barrier Rule

Due to the crisis, most businesses have a lower EBITDA. Furthermore, an increase in interest rates leads to higher interest expenditures. Key interest rate reductions by the central banks are often not passed on to businesses, since in the course of a crisis, the number of debtors unable to repay is likely to rise. In light of this, the interest barrier rule appears to amplify the crisis due to an overall decrease in deductible interest expenditures.

In its statement dated 3 April 2009 regarding the Citizen Relief Act (*Bürgerentlastungsgesetz*), the German Federal Council (*Bundesrat*) proposed to temporarily raise the exemption limit in sec. 4h para. 2 sentence 1 ITA from 1m € to 3m € (*BR-Drucksache* 168/09). Thus, the interest barrier rule, which limits the deductibility of business expenses for interest expenditures to 30 % of the fiscal EBITDA, would not be applicable, if the net interest expenditures of the business do not exceed 3m €. This is to exempt medium-sized companies from the interest barrier rule.

In a joint amendment request, the CDU/CSU and SPD parliamentary groups in the Federal Parliament (*Bundestag*) agreed on 26 May 2009 upon implementing this measure. The Parliament passed the respective amendments of the government bill regarding the *Bürgerentlastungsgesetz* on 19 June 2009. The Federal Council passed the bill on 10 July 2009. The increase of the threshold to 3m € will come into force with the promulgation in the Federal Law Gazette and shall be limited to the assessment periods 2008 and 2009 (contrary to the original proposal made by the Federal Council to extend the applicability until 2010).

2. Loss Carry-forwards

Sec. 8c CITA (which was introduced by the tax reform in 2008) causes the forfeiture of existing loss carry-forwards at the time of a substantial shareholder change. In case of a transfer of more than 50 % of the subscribed capital, of membership rights, ownership rights (*Beteiligungsrechte*) or of the voting rights in a corporation to a buyer (or closely related persons thereof) within 5 years, the losses would be entirely eliminated, whereas in the case of a transfer of 25 % to 50 %, the losses would be eliminated pro-rata at the respective percen-

[7] With regard to the disputed trade tax liability of this trust scheme cf. pending decision of the Federal Tax Court (IV R 26/07, previously Regional Tax Court of Düsseldorf, dated 19 April 2007, 16 K 4489/06). The decision of the Federal Tax Court is expected in 2009.

tage. Unlike the previous provision (sec. 8 para. 4 CITA, former version), sec. 8c CITA does not contain a reorganization clause.[8]

The elimination of the loss carry-forwards pursuant to sec. 8c CITA hinders restructurings in times of crisis.[9] It complicates the search for investors willing to reorganize a company. During its debates regarding the Financial Market Stabilization Act (*Finanzmarktstabilisierungsgesetz*), the Federal Government (*Bundesregierung*) had identified the negative effects of sec. 8c CITA and decided that sec. 8c CITA shall not be applicable to certain measures according to sec. 14 para. 3 Financial Market Stabilization Act.

In its statement dated 3 April 2009 regarding the *Bürgerentlastungsgesetz*, the Federal Council had called for a temporary implementation of a general reorganization clause (sec. 8c para. 1a CITA-draft), which in its prerequisites follows the reorganization privilege of sec. 39 para. 4 sentence 2 Insolvency Act.[10] On 19 June 2009, the Federal Parliament decided (with the votes of the CDU/CSU and SPD parliamentary groups) to temporarily create a reorganization privilege within sec. 8c CITA effective until 31 December 2009. The Federal Council passed the bill on 10 July 2009. The reorganization clause will come into force with the promulgation in the Federal Law Gazette.

A new paragraph 1a will be added to this provision. An acquisition of shares "with the purpose of a reorganization of business operations of the corporation" would thus not cause an elimination of the losses. According to the bill, a reorganization is "a measure aiming to avert or remedy an inability to pay or an over-indebtedness, while maintaining the significant business structures".

The reorganization clause contains complex rules (which to some extent require interpretation) regarding the question whether a measure qualifies as a reorganization. Either, an employer/workers council agreement containing specific employment arrangements needs to be complied with or the total of the relevant annual wages may not fall below 400 % of the initial total amount of wages within 5 years of the acquisition of shares (the intention here being – through a reference to the wage clause in sec. 13a Inheritance and Gift Tax Act – to avoid new terms possibly differing from those contained in the inheritance tax provision). Alternatively, new business assets (which equal at least 25 % of the assets stated in the balance sheet of the previous financial year) would have to be injected by way of contributions within 12 months of the acquisition of the shares. If less than 100 % of the shares are transferred, a reduced percentage of assets has to be contributed, respectively.

It is problematic that the advantageous reorganization clause in the modified sec. 8c CITA requires the contribution of assets in order to avert the elimination of the loss carry-forwards. Curiously enough, this might lead (at least in the transition period of sec. 34 para. 6 sentence 4 CITA) to the applicability of the former sec. 8 para. 4 CITA. This would cause the forfeiture of the loss carry-forwards.[11]

The waiver of debt by the buyer of shares or by a closely related party thereof is considered to be a contribution of assets – however, only to the extent the debt is valuable.

8 Cf. Wiese, DStR 2007, p. 741, for a critical review thereof.

9 Cf. Rödder, in: Arbeitsbuch zur 60. Steuerrechtlichen Jahresarbeitstagung 2009 der Arbeitsgemeinschaft der Fachanwälte für Steuerrecht e.V., p. 83 et seq. and p. 91 et seq. with further citations, also for a critical review thereof.

10 Cf. Fey/Neyer, AG 2009, p. 322; Altrichter-Herzberg, GmbHR 2009, p. 466.

11 Cf. Breuninger, Arbeitsbuch zur 60. Steuerrechtlichen Jahresarbeitstagung 2009 der Arbeitsgemeinschaft der Fachanwälte für Steuerrecht e.V., p. 136 et seq., p. 140.

In contrast, the reorganization clause is not applicable if the company carrying the losses had almost closed its business operations at the time of the acquisition of the shares or if the company starts a business in a different industry sector within 5 years after the acquisition of the shares.

3. Add-backs to the Tax Base for Trade Tax Purposes

The provisions regarding add-backs to the tax base for trade tax purposes result in an artificial increase of the costs of debt financing.[12] Pursuant to sec. 8 no. 1 TTA, interest, rent and lease payments are partially added back to the tax base. Especially in the current economic situation, this can lead to tax payments even if the company has negative operating income.

So far, neither the Federal Government nor the Federal Council have proposed an elimination of sec. 8 no. 1 TTA. It has so far only been proposed by the FDP parliamentary group on 27 March 2009.

[12] For a critical review cf. Schaumburg, in: Arbeitsbuch zur 60. Steuerrechtlichen Jahresarbeitstagung 2009 der Arbeitsgemeinschaft der Fachanwälte für Steuerrecht e.V., p. 106 et seq. with further citations.

B. Possible Restructuring Measures

This part provides

- a list of debt restructuring measures important in practice (B. I.),
- a summary of the tax issues associated with those measures (B. II.), and
- an overview table (B. III.).

In part C., certain details of debt restructuring measures and their tax implications are discussed (C. I.). Such measures can lead to a requalification of debt instruments into equity for tax and / or GAAP balance sheet purposes. A table provides an overview (C. II.).

I. Restructuring Measures by a Creditor

1. Full or partial Waiver of the Loan Receivable

The creditor fully or partially waives the loan receivable against the debtor company (debt cancellation agreement) in order to avoid or eliminate the insolvency (over-indebtedness or inability to pay) of the debtor company.

2. Full or partial Waiver of the Loan Receivable in combination with a Debtor Warrant (conditional Waiver)

As above 1., but the waiver of the loan receivable is combined with a so-called “debtor warrant” (*Besserungsschein*), i.e. the loan receivable is waived under a resolutory condition. In case of an improvement of the financial situation of the debtor company, the claim will be reinstated (fully or partially). The specific terms of the warrant are a matter of negotiations between the creditor and the debtor company - often, however, the possibility of a reinstatement is restricted to a certain number of years.

3. Repurchase of the Loan Receivable by the Debtor Company below Par Value (“Debt-Buy-Back”)

The creditor assigns the loan receivable to the debtor company and, as consideration receives a payment of an amount lower than the nominal value of the loan receivable.

4. Purchase of the Loan Receivable below Par Value by a Company affiliated to the Debtor Company

The creditor assigns the loan receivable to a company related to the debtor company for payment of an amount which is lower than the nominal value of the loan receivable. A similar case is the assumption of debt by a parent company for the benefit of its subsidiary in combination with a waiver of recourse claims against the subsidiary to prevent a potentially taxable restructuring gain at the level of the subsidiary.

5. Waiver of the Loan Receivable against an Equity (or similar) Participation in the Debtor Company („Debt-Equity-Swap“)

The creditor receives an equity (or similar) participation in the debtor company for waiving its loan receivable. Alternatively, the investor exits through a transfer of all shares in the debtor company to the creditor (or a trustee) for a minimal consideration (€ 1) in combination with a participation in subsequent sale proceeds.

6. Contribution of the Loan Receivable into a Company affiliated to the Debtor Company against an Equity Participation

The creditor assigns its loan receivable to a company affiliated to the debtor company. The assignment is treated as a contribution in kind in return for shares in the affiliated company.

7. Temporary Cancellation of Interest on the Loan Receivable

The creditor agrees with the debtor company to cancel the obligation to pay interest on the loan for a certain period of time.

8. Debt-Mezzanine Swap

In lieu of a transformation into an equity participation (Debt-Equity-Swap), the loan receivable of a creditor can be transformed into a mezzanine financial instrument.

II. Overview: Tax Implications (in parentheses: Measures acc. to I.)

1. Loan receivable ceases to exist / confusion of rights (1, 3, 5, 8; under a resolutory condition 2)

2. Generally taxable "waiver gain" (1, 2, 3, 5, 8; possibly 7); as the case may be, tax-exempt restructuring gain by means of a discretionary decision by the tax authorities

3. Taxable interest income (4, 6)

4. Problems associated with the interest barrier rule (4, 5, 6)

5. Potential risk of elimination of loss carry-forwards (5, 6, 8)

6. Equity participation of the creditor / valuation problems (5, 6)

7. Potential risk of constructive dividends (4, 6)

8. Application of sec. 6 para. 1 no. 3 ITA (gain from the discounting of liabilities also for a taxpayer only subject to limited taxation? Application of CFC rules? (1, 2, 7)

9. Potential VAT burden caused by an acquisition of non-performing loans (4)

III. Overview of possible Tax Implications

		Waiver gain at the level of the debtor possible	Tax-exempt restructuring gain? (Restructuring decree)	Taxable interest income at the level of the purchaser of the loan receivable possible	(Additional) tax burden due to interest barrier rule at the level of the debtor possible	Elimination of losses / loss carry forwards possible	Preservation of capital / valuation / contribution in kind	Constructive dividend possible	Taxable discounting profit possible	Taxable passive income possible (Foreign Tax Act)	Potential VAT burden?
A.	**Measures by a creditor**										
1	Full or partial waiver of the loan receivable	**X**	**X**							**X**	
2	Full or partial waiver of the loan receivable in combination with a debtor warrant (conditional waiver)	**X**	**X**							**X**	
3	Repurchase of the loan receivable by the debtor company below par value	**X**	**X**								
4	Purchase of the loan receivable below par value by a company affiliated to the debtor company			**X**	**X**			**X**			**X**
5	Waiver of the loan receivable against an equity (or similar) participation in the debtor company ("Debt-Equity-Swap")	**X**	**X**		**X**	**X**	**X**			**X**	
6	Contribution of the loan receivable into a company affiliated to the debtor company against an equity participation			**X**	**X**	**X**	**X**	**X**			
7	Temporary cancellation of interest on the loan receivable	**X**	**X**			**X**			**X**	**X**	
8	Debt-Mezzanine-Swap	**X**	**X**		**X**	**X**	**X**			**X**	
B.	**Measures of a seller with outstanding vendor note**	**In principle, as described above, but depending on the respective "restructuring measure"; as the case may be also adjustment of purchase price (base for depreciation) with / without retroactive effect for commercial and / or tax balance sheet**									

C. Discussion / Issues / Ramifications

I. Typical Scenarios and Tax Implications of Debt Restructuring Measures

1. Full or partial Waiver of the Loan Receivable

a) Waiver by a third-party Creditor

The gain arising at the level of the debtor company as a result of the waiver of liabilities is generally subject to tax. According to formerly applicable sec. 3 no. 66 ITA, such gains were not subject to tax if they qualified as restructuring gains under this provision. Since loss carry-forwards were not offset with a restructuring gain, there was a double benefit resulting in the repeal of the provision.[13] Under current tax law, the tax authorities may waive the tax claim or defer the tax payment on such waiver gains only based on a discretionary decision (sec. 222 and 227 GTC). The conditions for a tax waiver or a deferral of tax payments as outlined in the so-called "restructuring decree"[14] of the Federal Ministry of Finance (Restructuring Decree) are similar to the conditions under the former provision of sec. 3 no. 66 ITA.

As a result of the waiver, the third-party creditor has to record a tax-effective business expense in the amount of the waived portion of the receivable, if the latter is part of the so-called "business assets" (*Betriebsvermögen*).

b) Waiver of a Shareholder Loan granted to a Corporation

- **Waiver of the valuable Portion of the Loan Receivable**

According to Federal Tax Court decisions, the waiver of the valuable portion of the loan receivable has to be treated as a constructive equity contribution into the corporation by the shareholder.[15] It is recorded as extraordinary income which has to be neutralized outside the balance sheet in accordance with sec. 8 para. 3 sentence 3 CITA. Accordingly, the measure results in a tax-neutral swap of debt into equity. At shareholder level, the acquisition cost of the shares has to be increased by the amount of the valuable portion of the waived receivable. Insofar, it is a neutral asset swap.[16] However, the valuable portion of a shareholder loan receivable may also be waived for operational business reasons (*betrieblich veranlasst*), if a third party acting as a prudent businessman would have also waived the loan receivable.[17]

- **Waiver of the non valuable Portion of the Loan Receivable**

According to the Federal Tax Court, the waiver of the portion of the loan receivable which is not valuable will never be *societatis causa* but due to operational business reasons.[18] Accordingly, such a waiver will not be treated as a tax neutral swap of debt into equity. Rather, with regard to the corporation the waiver for operational business reasons will lead to an increase of income relevant for tax purposes, whereas the shareholder has to record a loss to the ex-

[13] Cf. Schäfer-Elmayer/Müller, StB 2009, p. 190, 191.
[14] Decree by the Federal Ministry of Finance, dated 27 March 2003, Federal Tax Gazette I 2003, p. 240.
[15] Federal Tax Court, decision dated 29 July 1997, VIII R 57/94, Federal Tax Gazette II 1998, p. 652 and decision dated 9 June 1997, GrS 1/94, Federal Tax Gazette II 1998, p. 307.
[16] Cf. Demuth, KÖSDI 2008, p. 16177, 16185.
[17] Federal Tax Court, decision dated July 31 1991, VIII R 23/89, Federal Tax Gazette II 1992, p. 375.
[18] Cf. Federal Tax Court, decision dated 29 July 1997, VIII R 57/94, Federal Tax Gazette II 1998, p. 652.

tent the receivable is not valuable. However, this does not apply if the shareholder is a corporation and the conditions of sec. 8b para. 3 sentence 4 et. seq. CITA are fulfilled. In such cases, waivers and write-offs of shareholder loan receivables result in expenses that are not relevant for tax purposes. Thus, according to current law, capital that is initially granted as a shareholder loan and subsequently converted into equity (by waiving the loan receivable), is treated unfavorably compared to capital which is granted as equity from the beginning because equity contributions can never trigger a taxable waiver gain. Such disparity contradicts the principle of equal treatment of equity and debt which sec. 8b CITA was supposed to promote.

The amount of the valuable portion of the loan receivable depends on the debtor's solvency and its willingness to pay.[19] It remains unclear how the fact that a company is not creditworthy on the general capital market should be interpreted.[20] In the case of an over-indebted corporation, the Federal Tax Court "generally" assumes a value of 0 €.[21] The waiver of such a non valuable loan receivable is therefore always caused by operational business reasons and never *societatis causa*.

- **Applicability of the Restructuring Decree**

If the waiver is not regarded as *societatis causa* but granted due to operational business reasons, the Restructuring Decree is generally applicable and, hence, a waiver of the tax on the resulting gain might be possible. In our view, this is the case even if the shareholder is the sole creditor of the company. If other creditors also materially participate in the restructuring and if there is a formal reorganization plan for the debtor company supported by the shareholder as well as the other creditors, the Restructuring Decree should be applicable to the waiver gain of the shareholder.[22]

c) Waiver of a Loan granted by a Partner to its Partnership

The treatment of a waiver of a partner's loan receivable towards the partnership which is treated as a "special business asset" (*Sonderbetriebsvermögen*) of the partner[23] has not yet been conclusively settled. According to the prevailing view in literature, this depends on whether the waiver is *societatis causa* or whether it is granted due to business reasons.[24]

If the waiver is *societatis causa*, the asset "receivable" will be transferred from the special assets of the partner to the assets in the balance sheet of the partnership. The transfer is recorded tax-neutrally (at book value) in accordance with sec. 6 para. 5 sentence 3 no. 2 ITA

[19] Regional Tax Court of Niedersachsen, DStRE 2005, p. 1062, 1064.
[20] Due to the cautious issuing of loans by the banks as a consequence of the financial crisis, Scheunemann/Hoffmann (DB 2009, p. 983, 985) do not consider this as evidence for the worthlessness of a claim.
[21] Federal Tax Court, decision dated 31 May 2005, I R 35/04, Federal Tax Gazette II 2006, p. 132.
[22] Cf. also Knebel, DB 2009, p. 1094, 1095; also compare Federal Tax Court, decision dated July 31 1991, VIII R 23/89, Federal Tax Gazette II 1992, p. 375.
[23] Pursuant to sec. 15 para. 1 no. 2 sentence 2 ITA, which according to the jurisdiction of the Federal Tax Court is an "income attribution rule", cf. Federal Tax Court, decision dated 19 May 1993 – I R 60/92, Federal Tax Gazette II 1993, p. 714. For the waiver of shareholder's purchase price claims, which under certain conditions are not considered a "special asset" of the shareholder, cf. Pyszka, BB 1998, p. 1557 et seq.
[24] Cf. also Wacker, in: Schmidt, ITA Commentary, , sec. 15, ann. 550; Hottmann, in: Beck'sches Steuer- und Bilanzrechtslexikon, 2009, keyword "Gesellschafterdarlehen", ann. 12; Pyszka, BB 1998, p. 1557. Critically: Demuth, KÖSDI 2008, p. 16177, p. 16184 et seq., who always assumes a tax-neutral treatment.

regardless of the value of the receivable. This treatment should also apply in the extraordinary case in which the "receivable" of the partner against "its" partnership is recorded in the special balance sheet with a lower value than the nominal value of the corresponding liability in the partnership's balance sheet (e.g., previous acquisition of the receivable from a third party below nominal value).

In case of a "business-reason" waiver (e.g., restructuring of the partnership to continue existing business relationships), the case law relevant for corporate entities shall be applied accordingly. The partnership records a taxable gain and the partner incurs a tax-deductible expense equal to the amount of the non-valuable portion of the receivable. The waiver is tax-neutral to the extent the receivable is valuable.

d) Requirements for a tax-privileged Treatment of a Restructuring Gain pursuant to the Restructuring Decree

A gain which arises as a result of the waiver of liabilities constitutes taxable income at the level of the debtor company. A tax-privileged restructuring gain pursuant to the Restructuring Decree requires the need for and the feasibility of the restructuring, the creditors' intent to restructure and the suitability of the waiver of debt for the restructuring.

- **Need for Restructuring**

  The need for restructuring has to be assessed *ex ante* at the time of issuance of the waiver.[25] A company, therefore, needs to be restructured, if without a restructuring a successful continuation of the business was not possible.[26]

- **Feasibility of Restructuring**

  The restructuring of a company is feasible, if according to the estimated development of the earnings, the continued existence of the company is realistic.[27]

- **Suitability of the Waiver of Debt for the Restructuring**

  "Suitability of the waiver of debt for the restructuring" means that the waiver of the liabilities has to be suitable to ensure the survival of the company on a stand-alone basis or in connection with other measures.[28]

- **Creditors' Intent to restructure**

  As a general rule, a liability is considered as waived for restructuring purposes if the debtor company needs to be restructured and the waiver is suitable for the restructuring. In case of a waiver by all creditors the intent to restructure is assumed. But also in case of a waiver by a single creditor the restructuring gain should be tax-exempt if this

[25] Geist, BB 2008, p. 2658, 2661.
[26] Cf. Federal Tax Court, decision dated 25 October1963, I 359/60 S, Federal Tax Gazette III 1964, p. 122.
[27] Cf. Federal Tax Court, decision dated 16 May 2002, IV R 11/01, Federal Tax Gazette II 2002, p. 854.
[28] Cf. Federal Tax Court, decision dated 20 February 1986, IV R 172/84, BFH/NV 1987, p. 493, 494.

creditor waives a substantial portion of its receivable with the intention to prevent the debtor's collapse.[29]

The Restructuring Decree limits the tax relief to that portion of the restructuring gain which cannot be offset with current losses, loss carry-forwards and loss carry-backs (but notwithstanding any normally applicable restrictions with respect to losses, e.g. the minimum taxation rules). The tax payment will initially be deferred until the amount of the restructuring gain will be finally determined.

The Restructuring Decree generally facilitates the waiver of liabilities since taxes are not triggered at the level of the debtor company. However, due to contradictory lower tax court decisions (appeals still pending at the Federal Tax Court)[30], there is currently uncertainty regarding the tax treatment of restructuring gains. In practice the authorities are willing to apply the Restructuring Decree.[31] However, it is recommended to obtain an advance ruling from the tax authorities.

For the decision whether restructuring gains can also be exempted from trade tax, the municipalities where the permanent establishments are located are competent. The current practice shows that the municipalities also follow the approach of the Restructuring Decree. However, it is recommended to discuss the restructuring measures in advance with the municipalities.[32]

e) Specific Issues under the Annual Tax Act 2009 for Corporations owning German Real Estate subject to limited Taxation

Until 31 December 2008, foreign corporations letting domestic real property usually derived income from renting and leasing (sec. 49 para. 1 no. 6 ITA). Within the framework of income from renting and leasing, the waiver of a financial liability caused a non-taxable increase of the net assets, as both the real properties as well as the financial liabilities incurred for their acquisition are not included in the income determination according to the cash-basis method used to determine the income from renting and leasing (even if the disposal of real properties

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29 Cf. Federal Tax Court, decision dated 26 November 1980, I R 52/77, Federal Tax Gazette II 1981, p. 181, and decision dated 16 May 2002, IV R 11/01, Federal Tax Gazette II 2002, p. 854.

30 Cf. Regional Tax Court of Cologne, decision dated 24 April 2008, 6 K 2488/06, DStRE 2008, p. 1445 (still pending, Federal Tax Court: X R 34/08); Regional Tax Court of Munich, decision dated 12 December 2007, 1 K 4487/06, DStR 2008, p. 1687 (still pending, Federal Tax Court: VIII R 2/08). The Regional Tax Court of Munich argues, that due to a non-existent legal base, the Restructuring Decree would generally not be applicable. The Regional Tax Court of Cologne, however, follows the preconditions of the Restructuring Decree; cf. Bauschatz, GmbHR 2008, p. 1204, p. 1207 et seq.; Eilers/Bühring, DStR 2009, p. 137; Geist, BB 2008, p. 2658; Gondert/Büttner, DStR 2008, p. 1676 et seq.; Knebel, DB 2009, p. 1094; Kronig-er/Korb, BB 2008, p. 2656; Schäfer-Elmayer/Müller, StB 2009, p. 190, 192; Wagner, BB 2008, p. 2671 et seq.

31 In this context, reference is made to a letter by Federal Minister of Finance, Peer Steinbrück, to the State Ministers of Finance, in which the tax authorities are asked to display leniency towards entrepreneurs in times of crisis. Especially regarding applications for a delay of payment, a waiver or an adjustment of advance payments, the tax authorities should use their discretion of judgement, if possible. cf. http://www.bundesfinanzministerium.de/DE/Wirtschaft__und__Verwaltung/Finanz__und__Wirtschaftspolitik/Foederale__Finanzbeziehungen/280509__Kulanz__Haupt.html?__nnn=true. The Ministry of Finance of Baden-Württemberg agreed in a press release in this regard. There, the State Minister of Finance, Mr. Stächele, declares, that in their discretionary decisions, the tax authorities in Baden-Württemberg would consider all individual aspects, that they would act accordingly in individual emergencies and that they would find practicable solutions within the scope of the legal base; cf. http://www.finanzministerium.baden-wuerttemberg.de/de/Aktuelle%20Pressemitteilungen/209925.html?referer=110369&template=min_meldung_html&_min=_fm.

32 Cf. also Eilers, GWR 2009, p. 3, 4.

by a corporation led to the non-recurring income determination according to sec. 49 para. 1 no. 2 lit. f) sentence 2 ITA-former version).

With effect from 1 January 2009, foreign corporations deriving income from letting domestic real property are deemed to have business income and are subject to taxation in Germany even if the income cannot be attributed to a permanent establishment (see sec. 49 para. 1 no. 2 lit. f) sentence 2 ITA). As a consequence, such foreign corporations do no longer earn income which is determined according to the cash-basis method but income which is generally determined according to the balance-sheet method under sec. 4 et seq. ITA.

Because of the shift to the balance-sheet method it is now doubtful whether a waiver of a loan receivable could result in a taxable waiver gain in Germany. "Technically", this would be the case if the liabilities would have to be recorded under the balance-sheet method. Due to these “technical” reasons, a gain would, therefore, not arise when the income is determined under the cash-basis method in accordance with sec. 4 para. 3 ITA. The cash-basis method can be applied if the foreign corporation is not obligated to keep business accounts in accordance with sec. 141 GTC (if certain revenue or profit thresholds are not exceeded) or it is not voluntarily keeping business accounts according to German law. An obligation to apply the balance sheet method will only arise after the notification of the tax office, however, at the earliest in 2010.

Even in the event that the balance sheet method is mandatory, it is, nevertheless, questionable whether the liabilities obtained for the acquisition of real property were considered to be German business debt. Sec. 49 para. 1 no. 2 lit. f) ITA includes, as before, income from the sale of domestic real properties and, as a new addition, also rental income. Therefore, the provision apparently refers to two different sources of income. It is unclear whether this income shall be determined separately or uniformly. In a separate determination of the income the real properties as well as the financial debt incurred for their acquisition would not be included in the determination of income from renting and leasing.

Furthermore, it is questionable whether the income resulting from the waiver of the loan receivable is actually income within the meaning of sec. 49 para. 1 no. 2 lit. f) sentence 2 ITA because it is not directly derived from the letting of German real property. In addition, it is doubtful whether this income is attributable to “income derived from the direct use, letting, or use in any other form of immovable property” within the meaning of article 6 para. 3 OECD Model Convention. This also applies if the respective loan was incurred for the acquisition of the real property. Germany does not have the right of taxation if this pre-condition as provided in the tax treaty is not fulfilled.

f) Waiver of the Loan Receivable and CFC Rules

If a creditor of a foreign company waives the loan receivable the question whether or not a taxable, a tax-privileged or tax-exempt gain arises is generally to be answered according to the domestic tax law of the country of residence (regarding the constellation that the debtor company earns domestic income see above a)). If the debtor company’s shareholders are German residents the question arises whether or not the CFC rules according to the German

Foreign Tax Act apply. In our opinion, they do not apply to such a foreign waiver gain. The German tax authorities are not deprived of any passive low-taxed income. There is no real profit that could be distributed to the shareholders. Technical profits are not subject to the German CFC rules.

g) Subsequent Acquisition Cost pursuant to sec. 17 ITA caused by the Shortfall of Shareholder Loans

If a taxpayer holds a participation within the meaning of sec. 17 ITA, shareholder loans granted after the acquisition of the participation can constitute subsequent acquisition cost pursuant to sec. 17 para. 2 ITA.

Pursuant to the Federal Tax Court the granting of the shareholder loan has to be *societatis causa* in order to fulfill the criteria of sec. 17 para. 2 ITA. This is the case if at the point in time of the granting or the prolongation of a shareholder loan the company is either on the brink of bankruptcy or the repayment of the shareholder loan is - given the financial situation of the company - at risk.[33] The latter shall be fulfilled if a prudent businessman (*ordentlicher Kaufmann*) would not have granted a loan under the same conditions.[34] According to the court rulings of the Federal Court of Justice concerning loans which replace equity (*Eigenkapitalersatz*) this depends on whether a third party would have granted a loan to the company at arm's-length conditions.

According to a new court ruling of the Federal Tax Court[35], shareholder loans which fall short of repayment can also constitute subsequent acquisition cost, if pursuant to sec. 32a para. 3 sentence 3 Limited Liability Company Act (in the version before the amendment by the *MoMiG*) the rules concerning loans which replace equity are not applicable.

Due to the abolishment of the law concerning loans which replace equity it is not certain whether or to which extent the criteria of the law concerning loans which replace equity will still be applicable to determine whether shareholder loans are granted *societatis causa*. To accentuate the latter, with the granting of the shareholder loan a subordination should be declared. Furthermore, the loan receivable which has declined in value can be sold to a corporation. Thereby, tax-relevant losses would occur, which could be charged against taxable income from investments pursuant to sec. 20 para. 2 no. 7 ITA. As well, instead of debt, an equity participation, potentially with a preferential treatment with respect to liquidation proceeds, could be granted.

2. Full or partial Waiver of the Loan Receivable in combination with a Debtor Warrant (conditional Waiver)

The waiver of the loan receivable along with a debtor warrant also results in the cancellation of both the loan receivable and the respective debt from the accounts of the creditor and the

33 Cf. Federal Tax Court, decision dated 24 April 1997, VIII R 16/94 - Federal Tax Gazette II 1999, p. 339; decision dated 4 November 1997, VIII R 18/94, Federal Tax Gazette II 1999, p. 344 and decision dated 10 November 1998, VIII R 6/96, Federal Tax Gazette II 1999, p. 348.

34 For a good summary of the principles applied by the tax courts cf. decree by the Federal Ministry of Finance dated 8 June 1999, Federal Tax Gazette I 1999, p. 545.

35 Cf. Federal Tax Court, decision dated 19 August 2008, IX R 63/05, DStR 2008, p. 2215.

debtor and, therefore, will cause a waiver gain at the level of the debtor. However, the payment of the respective tax on the waiver gain (the remaining portion after offsetting of losses) may be deferred until the expiration of the recovery period if the requirements of the Restructuring Decree were met (see 1.d)). The tax claim will only be waived if the recovery turns out to be impossible.[36]

In case of the recovery of the debtor company and the resurgence of the loan receivable, payments of the debtor company to the creditor cannot be deducted as business expenses according to sec. 3c ITA, but must be offset against the restructuring gain.[37] However, recovery payments should be deductible to the extent they exceed the formerly calculated restructuring gain because there has been no respective waiver of tax claims insofar.

3. Repurchase of the Loan Receivable by the Debtor Company below Par Value ("Debt-Buy-Back")

a) Liquidity

The direct repurchase of the loan receivable by the debtor company requires sufficient funds even though the value of such loan receivable against the debtor company has decreased below its par value. An affiliated company could provide liquidity by way of a capital contribution or a new loan. However, the tax consequences of granting a new loan to the debtor company have to be observed carefully, especially with respect to the application of the interest barrier rule at the level of the debtor company.

b) Confusion of Rights / Exemption for securitized Loan Receivables

The acquisition of the loan receivable by the debtor company results in the extinction of such loan receivable by way of confusion of rights. This is also true if the creditor bank initially intended to sell the loan receivable to third parties. There will be no extinction and confusion of rights regarding the loan receivable, however, if they are securitized and can still be traded.[38] In this case, it should be possible that such securities are capitalized as assets of the debtor company not resulting in a confusion of rights. However, the „redemption" of these securities will lead to the extinction of the loan receivable and result in a respective gain.

c) Taxation / Tax Exemption of Waiver Gain (see above 1.)

The repurchase of the loan receivable by the debtor company below par value and the resulting extinction of the loan receivable leads to a taxable gain to the extent of the difference between par value and purchase price. If, however, the requirements of a tax-privileged restructuring gain are met (see above 1.d)) such gain from the repurchase of the loan receivable below par value should be tax-privileged because the repurchase has the same effect as a partial waiver of the loan receivable by the creditor.

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[36] Cf. decree by Federal Ministry of Finance dated 27 March 2003, Federal Tax Gazette I 2003, p. 240, ann. 5.
[37] Cf. decree by Federal Ministry of Finance dated 27 March 2003, Federal Tax Gazette I 2003, p. 240, ann. 5.
[38] Cf. Schultz, Status: Recht 2009, p. 97, 98.

4. Purchase of the Loan Receivable below Par Value by a Company affiliated to the Debtor Company

The loan receivable may also be acquired below par value by an affiliated company of the debtor company. Thus, there is no extinction of the loan receivable by way of confusion of rights and neither a taxable gain at the level of the debtor company nor at the level of the acquiring company while a profit has to be shown for group accounting and IFRS purposes. Another advantage of such an acquisition by an affiliate company is the internal control of the group over the loan receivable without influence from third-party creditors.

a) Constructive Dividend?

A constructive dividend requires a decrease of a corporation's assets *societatis causa* (or a prevention of a potential increase of its assets *societatis causa*, respectively) which is not based on a shareholder resolution for the distribution of profits and which results in a tax balance sheet difference according to sec. 4 para. 1 sentence 1 ITA.[39] Whether the acquisition of a loan receivable by a shareholder of the debtor corporation may lead to a constructive dividend has been subject of several tax court decisions. In these cases, the requirements of a constructive dividend may be fulfilled for two reasons: the acquisition of the loan receivable below par value as such or its subsequent full repayment at par value.

According to the Regional Tax Court of Schleswig-Holstein[40], the subsequent repayment of a nearly worthless loan receivable against a limited liability company that has been acquired far below par value along with the purchase of the company's shares results in a constructive dividend. The loan receivable was acquired by the wife of the purchaser of the company and held among her private assets. In the taxpayer's opinion, the subsequent repayment of the loan receivable at par value (a multiple of the purchase price) by the company was not subject to income tax. The Regional Tax Court of Schleswig-Holstein stated that the subsequent repayment of a nearly worthless loan receivable acquired in connection with the purchase of a limited liability company may constitute a constructive dividend if the acquisition of the loan receivable must be disregarded because a seller of a company acting reasonably had waived the worthless loan receivable prior to the sale of the debtor company.[41] In such cases, the (tax) planning of the parties involved does not lead to a reasonable debt restructuring of a company but only to a tax-advantageous utilization of a worthless loan receivable in connection with the acquisition of a company.

The Regional Tax Court of Munich[42] considered already the acquisition of a loan receivable as such by a parent company of the debtor company below par value as a constructive dividend based on the so-called business opportunity rule (*Geschäftschancenlehre*). The parent company utilized a business opportunity that was actually attributable to the debtor company,

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[39] Sec. 36 para. 1 sentence 1 CITA Guidelines.
[40] Regional Tax Court of Schleswig-Holstein, dated 17 April 2002, EFG 2002, p. 1142.
[41] Regional Tax Court of Schleswig-Holstein, dated 17 April 2002, EFG 2002, p. 1142; cf. also Federal Tax Court, dated 1 February 2001, IV R 3/00, DStRE 2001, p. 649; Gosch, StBp 2001, p. 180 for a critical review thereof.
[42] Regional Tax Court of Munich, dated 18 February 2000, EFG 2001, p. 457.

namely to dispose the debt at a favorable price. For leaving this opportunity to its parent company, the debtor company should have asked for a reasonable third-party compensation. The omitted claim of such compensation may be regarded as a prevented increase of the debtor company's assets *societatis causa* and, therefore, constitute a constructive dividend. The Federal Tax Court, instead, refused the idea of a constructive dividend. The acquisition of loan receivables below par value by affiliate companies of the debtor company does not result in a constructive dividend, neither at the time of the acquisition (based on the business opportunity rule) nor later at the time of the full repayment of the debt at par value.[43] The Federal Tax Court rejected also the reasoning of the Munich Tax Court according to which the acquisition of a loan receivable by the parent company was economically comparable to a waiver of the loan receivable resulting in a respective waiver gain at the level of the debtor company. The Federal Tax Court also stated that the willingness of the lender to sell the loan receivable does not constitute an opportunity for the debtor company to repurchase the debt or to leave it to the parent company against consideration. Instead, in case of a sale of the loan receivable, the debtor is simply confronted with a change of the creditor which it cannot influence (even if the purchaser is an affiliated company). Finally, the Federal Tax Court considered the acquisition of a loan receivable by a shareholder of the debtor company as an admissible practice and an alternative to the waiver of the loan receivable to avoid a taxable waiver gain. A constructive dividend may only be assumed in case of particular circumstances according to which the purchase of the loan receivable must be disregarded (e.g., if a worthless loan receivable is sold in connection with the sale of a limited liability company – instead of being waived – and subsequently repaid).[44]

b) Interest Income of the affiliated Company (subject to German Tax?)

The interest payments by the debtor company to the affiliated creditor company do not constitute constructive dividends if they are at arms' length. Interest income of a foreign creditor company is subject to German limited tax liability only in case the loan receivable is secured by German real property (sec. 49 para. 1 no. 5 lit. c) aa) ITA). If a Double Taxation Treaty is applicable, the right to tax the interest income will usually be attributed to the country of residence of the creditor company. Additionally, Germany has a limited right of taxation in some cases. If the debtor company is also domiciled abroad, its interest income will, in general, not qualify as interest income but as other income under the Double Taxation Treaty which is taxable only in the country of residence even if the loan is secured by German real property resulting in a limited taxation pursuant to domestic law.

c) Possible Tax Burdens caused by the Interest Barrier Rule

An additional tax burden caused by the interest barrier rule may arise due to the financing of the acquisition of the loan receivable by an affiliated company if this company belongs to the relevant group of companies for purposes of the interest barrier rule or if the interest payments to the affiliated company (participation > 25 %) exceeds the 10 %-limit according to sec. 8a para. 3 CITA.

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[43] Federal Tax Court, dated 30 January 2002, I R 13/01, GmbHR 2002, p. 748; affirmative Hoffmann, GmbHR 2002, p. 750; F. Hey, BB 2002, p. 2487.

[44] For a critical review cf. Hoffmann, GmbHR 2002, p. 750; Lange/Janssen, Verdeckte Gewinnausschüttungen, p. 791.

If the company which acquires the loan receivable belongs to the relevant group of companies the equity ratio within the group may be affected to the disadvantage of the debtor company depending on the financing of the acquiring company. With a tolerance of one percentage point, the equity ratio of the debtor company shall not fall below the equity ratio of the whole group. If the debtor company failed such equity ratio comparison test, the interest barrier would apply resulting in a limited deduction of interest expense of the debtor company.

If the loan receivable is acquired by a company affiliated with the debtor company but outside the relevant group of companies, the equity ratio comparison is, instead, not influenced by the financing of such company. Then, however, it must be observed that the application of the “escape clause” (equity ratio comparison test passed) will not be excluded due to a case of harmful shareholder financing according to sec. 8a para. 3 CITA. The statutory definition of harmful shareholder financing is quite broad and covers (i) all shareholders holding directly or indirectly more than 25 % in the shares of the debtor company or of any other company which belongs to the relevant group of companies, (ii) persons who are related parties within the meaning of sec. 1 para. 2 Foreign Tax Act to a shareholder under (i) and, finally, (iii) third parties having recourse to a person mentioned under (i) or (ii). The acquisition of the loan receivable by a company which fulfills one of the criteria mentioned under (i) to (iii) results in a harmful shareholder financing if the net interest expense owed to such company (and to all other persons who fulfill one of the criteria under (i) to (iii)) exceeds 10 % of the total interest expense of the debtor company. Argumentum e contrario, the debt restructuring in the latter case may include only a portion of debt carrying a maximum of 10 % of the total interest expense of the debtor company to avoid the application of the interest barrier rule.

The affiliated company should be able to acquire a larger portion of the debt, if it was possible to reduce the interest rates which apply to the relevant debt. If, nonetheless, the application of the interest barrier rule cannot be avoided, its consequences may be mitigated by current losses or the utilization of loss carry forwards.

d) Waiver Gain

The (subsequent) waiver of the acquired loan receivable by the affiliated company results in the extinction of the debt and, therefore, in a gain at the level of the debtor company. Such gain is, however, neutralized for tax purposes insofar as the waiver by the affiliated company constitutes a contribution into the debtor company. A waiver by a shareholder *societatis causa* constitutes a contribution only to the extent that the receivable is still valuable at the time of the waiver. Insofar as the receivable has lost its value the gain caused by the waiver cannot be compensated for by a respective contribution for tax purposes.

Nonetheless, such waiver gain should be tax-exempt if the requirements of the Restructuring Decree are met (see above 1. d)).

e) VAT Treatment of Sale of Loan Receivable

Currently, there are two dissenting decisions of the Regional Tax Courts of Hesse and Düsseldorf on the question whether the sale of a portfolio of non-performing loans must be treated – according to a decision of the European Court of Justice regarding factoring (without recourse) – as a taxable (and not tax-exempt) service of the purchaser to the seller of the loan receivable for VAT purposes.[45] The Regional Tax Court of Hesse[46] takes the view that a taxable service of a purchaser of a portfolio of non-performing loans – comparable to those rendered by a factoring entrepreneur – simply requires that the purchaser assumes the credit risk and collects the amount of debt. The collection by the purchaser seems to be crucial for assuming a taxable service rendered by the purchaser also in the view of the tax authorities (cf. sec. 18 para. 9 et seq. VAT Regulations). Then, the taxable consideration would be the difference between the purchase price and the economic value of the loan receivable assumed by the parties at the time of the sale. As a consequence, a bank as seller of a loan receivable would, in general, not be entitled to deduct such VAT as input VAT. If, however, the purchase price of the loan receivable equals its economic value (which has to be proved by the purchaser, cf. sec. 18 para. 12 sentence 12 VAT Regulations) the relevant consideration should be 0 €.

The sale of a portfolio of non-performing loans and, even more, the simple sale and transfer of a single non-performing loan receivable is, in our view, not comparable to the factoring business. The purchaser of the loan receivable does not render any service against consideration (factoring fee) to the seller and does not act like a typical factoring entrepreneur on the basis of a long-term relationship to the factoring client / seller of the receivable.[47] Consequently, there is no service rendered by the purchaser of the loan receivable to the former creditor (seller of the loan) for VAT purposes; the sale of the loan receivable by the seller remains a tax-exempt sale of a receivable. However, given the pending appeal to the Federal Tax Court (V R 18/08) against the decision of the Regional Tax Court of Düsseldorf, there is currently uncertainty regarding the VAT treatment.

f) Assumption of Debt by a Shareholder (Debt-Push-Up)

In order to reduce a company's debt, a shareholder can assume the debt pursuant to sec. 414 and 415 of the German Civil Code. The Federal Tax Court has thereto decided that the write-off of the liability at the company's level is neutral for tax purposes if the shareholder waives its right of recourse and takes over the liabilities without reserve.[48] When these conditions are fulfilled – regardless of the intrinsic value of the receivable – the assumption of debt is treated as a constructive equity contribution in the full amount of the receivable. Insofar the assumption of debt is treated differently than the waiver of a shareholder loan which is treated as a constructive equity contribution only to the extent of the valuable portion, see above 1.

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45 Cf. the decision of the ECJ regarding a factoring business, dated 26 June 2003, C305/01, „MKG-Kraftfahrzeuge-Factoring GmbH“, Federal Tax Gazette II 2004, 688 and the follow-up decision by the German Federal Tax Court, dated 4 September 2003, V R 34/99, Federal Tax Gazette II 2004, 667.

46 Decision dated 31 May 2007, 6 V 1258/07.

47 Cf. Regional Tax Court of Düsseldorf, decision dated 15 February 2008, 1 K 3682/05 U.

48 Federal Tax Court, decision dated 20 December 2001, I B 74/01, DStRE 2002, p. 257. The decision was not published in the Federal Tax Gazette.

The future tax treatment of the liability (repayment by shareholder or waiver by creditor) has exclusively to be decided at the level of the shareholder.

Hence, a taxable gain resulting from the waiver is not prevented but transferred from the company to the shareholder. If, however, sufficient loss carry-forwards are available at the level of the shareholder or if the shareholder benefits from a more favorable tax regime abroad, the measure of a debt assumption can be used to achieve a cash-neutral reorganization of the company. Typically, an abuse of law cannot be assumed in these cases.[49]

5. Waiver of the Loan Receivable against an Equity (or similar) Participation in the Debtor Company ("Debt-Equity-Swap")

a) Debt-Equity-Swap

Through a debt-equity-swap, the creditor's loan receivable will be converted into an equity participation in the debtor company and, therefore, will help to reduce its debt-equity-ratio. There are different ways to implement a debt-equity-swap[50]:

- The creditor contributes its loan receivable into the debtor company along with a capital increase by way of a non-cash capital contribution resulting in the extinction of the receivable through confusion of rights. The special requirements for a capital increase by way of a non-cash capital contribution have to be met, in particular regarding the valuation of the loan receivable.
- The debt-equity-swap may also be implemented through a transfer of shares by the existing shareholders to the creditor against the waiver of the loan receivable.
- It is also possible that the debtor company transfers own shares that have been repurchased and not redeemed by the debtor company to the creditor against the waiver of the loan receivable.

In any case, the debt-equity-swap requires the consent of (the majority of) the existing shareholders.

Insofar as the loan ceases to exist due to the debt-equity-swap there will be a restructuring gain at the level of the debtor company which might be tax-privileged (cf. above 1. d)).

In case the shareholders transfer their shares in the debtor company free of charge or against a symbolical purchase price to the creditor or a trust company, it might be advisable to agree upon a participation of the former shareholders in subsequent capital gains (in case the debtor company recovers and its shares are sold by the new shareholder) as well as on an unlimited transferability of such claim.

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49 Cf. WTS Tax Journal 02/2003; Schmidt/Hageböke, DStR 2002, p. 2150; Gosch, StBp 2002, p. 117; cf. also Schultz, Status Recht, 3/2009, p. 97, 98.

50 Cf. Mückl, FR 2009, p. 497, 498 et seq.; Redeker, BB 2007, p. 673 et seq.

If the former shareholders in the debtor company are individuals who held a material shareholding within the meaning of sec. 17 ITA, the subsequent participation in the capital gains will retroactively affect their income taxation of the year when they sold the shares (retroactive event according to sec. 175 GTC). Only insofar such follow-up proceeds exceed the acquisition cost of the shares that have been “written-off” at the time of the sale of the shares, the gain is taxed under the shareholder relief / participation exemption rules applying to individuals (partial exemption) and to corporations according to sec. 8b CITA. Previous tax benefits from the offsetting of such losses pursuant to sec. 17 ITA against other income at the time of the sale of the shares must be adjusted accordingly.

b) Subordination of Shareholder Loans

In case the creditor contributes only a portion of the loan receivable into the debtor company, the creditor will be both shareholder and lender of the debtor company. After recent modifications of the law concerning loans which replace equity, it must be analyzed whether the shareholder loan is subject to the subordination rule under insolvency law (sec. 39 para. 1 no. 5 Insolvency Act). There is, however, an exception to the subordination rule in case of restructuring measures (sec. 39 para. 4 sentence 2 Insolvency Act) which requires that the participation in the debtor company has been acquired after the debtor company’s inability to pay or its over-indebtedness and with the intention to restructure the debtor company. A further exception to the subordination rule applies to shareholders holding not more than 10% in the shares of the debtor company.

c) Interest Barrier in case of partial Contribution of Loan Receivable, Interest Payments to Creditor > 10 % and Participation of Creditor > 25 %

In case the creditor retains a portion of the loan receivable against the debtor company after the debt-equity-swap, the interest barrier rule could be applicable due to a harmful shareholder financing pursuant to sec. 8a para. 3 CITA. This is the case if the creditor holds more than 25 % in the debtor company’s equity and the interest expense owed to the creditor (and all other creditors within the meaning of sec. 8a para. 3 CITA) exceeds 10 % of the total net interest expense of the debtor company. As a consequence, a reduction of the interest rate which applies to the remaining debt should be considered in order to comply with the 10 %-limit.

d) Forfeiture of Loss Carry Forwards when Participation of Creditor > 25 % / 50 %

In case of a participation of the creditor of more than 25 % in the shares of the debtor company due to the debt-equity-swap, the existing loss carry forwards of the debtor company will cease to exist to the extent of the share transfer to the creditor (> 25 % up to 50 %) according to sec. 8c CITA. If more than 50 % of the shares are transferred to the creditor, the loss carry forwards will be forfeited entirely. This is also applicable for trade tax loss carry-forwards (sec. 10a sentence 10 TTA) and interest carry-forwards within the meaning of the interest barrier rule (sec. 4h para. 5 sentence 3 ITA).

Regarding the amendment of sec. 8c CITA, cf. A.IV.2.

e) Transformation of the Loan Receivable into an atypical silent Partnership

For tax purposes the transformation of the loan receivable into an atypical silent partnership is possible only to the extent the loan receivable is valuable. A contribution of the loan receivable at its par value is permitted by commercial law. Insofar as the loan receivable is not valuable, it will cease to exist resulting in a waiver gain at the level of the debtor company which may be, nonetheless, tax-privileged under the conditions of the Restructuring Decree (see above 1. d)).

6. Contribution of the Loan Receivable into a Company affiliated to the Debtor Company against an Equity Participation

a) Constructive Dividend?

Due to the contribution of the loan receivable by the creditor into an affiliated company of the debtor company, the affiliated company will become a creditor of the debtor company (as in the case of the direct sale to the affiliated company; cf. above 4.). However, neither the acquisition of the loan receivable by the affiliated company below par value nor the full repayment of the loan receivable to the affiliated company should constitute a constructive dividend from the debtor company (see above 4.).

b) Taxation of Interest Income

Regarding the German taxation of interest income of the affiliated company cf. above 4. c).

c) Possible Tax Burden due to Interest Barrier Rule

Interest payments to the affiliated company may result in an (additional) tax burden caused by the interest barrier rule.

If the company into which the loan receivable is contributed belongs to the same group of companies as the debtor company the interest barrier may become applicable at the level of the debtor company due to a change of the equity ratio within the group.

In case the loan receivable is contributed to a company that does not belong to the same group of companies for purposes of the interest barrier rule, a harmful shareholder financing pursuant to sec. 8a para. 3 CITA will result in the application of the interest barrier if the interest expense owed to such company (and to all other creditors within the meaning of sec. 8a para. 3 CITA) exceeds 10 % of the total net interest expense of the debtor company. Again, it may be possible to reduce the interest rate on the relevant portion of debt (see above 4. d).

d) Interest Barrier in case of partial Contribution of a Loan Receivable

In case the creditor retains a portion of the loan receivable against the debtor company, there may be a harmful shareholder financing according to sec. 8a para. 3 CITA resulting in the application of the interest barrier. This is the case if the creditor holds indirectly more than 25 % in the debtor company's equity and the interest expense owed to the creditor (and all other creditors within the meaning of sec. 8a para. 3 CITA) exceeds 10 % of the total net interest expense of the debtor company. A reduction of the interest rate on the relevant portion of the debt might be considered.

e) Forfeiture of Loss Carry Forwards

In case of a participation of the creditor of more than 25 % - also indirectly - in the shares of the debtor company, the existing loss carry forwards of the debtor company will cease to exist to the extent of the share transfer to the creditor (> 25 % up to 50 %) according to sec. 8c CITA. In case of an indirect participation of the creditor of more than 50 % the loss carry forwards will be forfeited entirely (see above 5. d)). An advantageous amendment of sec. 8c CITA has recently passed the *Bundestag*, cf. A.IV.2.

Regarding the potential waiver gain in case of a contribution of the loan receivable downwards into the debtor company, see above 1.

7. Temporary Cancellation of Interest on the Loan Receivable

The economic situation of the debtor company may cause the creditor to reduce the interest rate or to cancel the interest payment obligation on the loan for a specified period of time.

It is important to note that for tax purposes a liability has to be discounted at a rate of 5.5 % if its term is longer than 12 months and it is not interest-bearing. In such a case, the debtor company has to record a taxable profit. In the subsequent periods, a corresponding expense will occur that needs to be allocated over the term of the loan (sec. 6 para. 1 no. 3 ITA).

In order to escape the discounting of the liability and the ensuing tax consequences, a lower interest rate can be agreed upon among the parties. In the view of the tax authorities, already a marginal interest rate is sufficient to prevent the discounting and, thus, the recording of a profit.

In case of a non-interest-bearing loan granted to a foreign debtor company subject to limited taxation, a discounting profit which is taxable in Germany only occurs if the liability is attributable to a German permanent establishment of the debtor company. In our view, sec. 6 para. 1 no. 3 ITA is not applicable to a foreign company subject to limited taxation determining its income by the cash-basis method.

In our opinion, sec. 6 para. 1 no. 3 ITA is also not applicable to rental income which constitutes deemed business income after the amendment of sec. 49 para. 1 no. 2 lit. f) ITA. A foreign special purpose company which derives business income from the letting of domestic real property is subject to taxation in Germany even if this income cannot be attributed to a permanent establishment in Germany (see above 1. e)). If the income of the foreign company is determined pursuant to sec. 4 para. 3 ITA (cash-basis method), a discounting profit will not be recorded. Even if the income of the foreign company will be determined in the future according to the balance sheet method (sec. 4 para. 1, sec. 5 ITA), a discounting profit is, in our opinion, not covered by the provisions for taxpayers that are subject to limited taxation. If the entire income constitutes deemed business income (in the absence of a permanent establishment), it is questionable whether the loan has to be recorded as a liability in the balance sheet. Also, it is doubtful whether the discounting profit is "income derived from the direct use, letting, or use in any other form of immovable property" within the meaning of the respective Tax Treaty.

Apart from that, the taxation of a discounting profit – as long as the liability cannot be attributed to a German permanent establishment – has generally to be determined according to the tax law of the country where the debtor company is resident and subject to unlimited taxation. If this company has shareholders which are subject to taxation in Germany, there might be an issue whether the CFC rules are applicable with respect to a discounting profit. In our opinion, this is not the case.

8. Debt-Mezzanine-Swap

In lieu of a transformation of a loan receivable into an equity participation (debt-equity-swap), a loan receivable can be transformed into a mezzanine financial instrument. Under certain circumstances, the latter allows to show equity in the German GAAP balance sheet and debt in the balance sheet for tax purposes. In particular, when a company suffers a crisis, this might be helpful. On the one hand, issuers can increase their equity for German GAAP purposes. On the other hand, they can deduct the expenses for German tax purposes. In addition, mezzanine financial instruments usually – depending on their construction – are not captured by the German rules concerning the limitation of the deduction of losses for corporate income and trade tax purposes (sec. 8c CITA and sec. 10a sentence 10 TTA).[51]

The qualification as equity for German GAAP purposes requires a junior ranking of the granted capital, a long-term capital commitment, profit-related payments for the capital commitment and a full participation in the losses.[52] In the tax balance sheet equity is only shown, if a participation in current profits as well as in liquidation proceeds is granted.[53]

In the literature participation rights are often proposed as adequate instruments.[54] If a participation right only grants a participation in current profits but not in liquidation proceeds, it constitutes – according to the above mentioned principles – equity for German GAAP purposes

[51] Cf. Federal Ministry of Finance dated 4 July 2008, decree regarding limitation of loss carry-forwards for corporations (sec. 8c CITA), Federal Tax Gazette I 2008, p. 736.
[52] IDW HFA 1/1994, IDW Fachnachrichten 1994, p. 269.
[53] Federal Tax Court, dated 19 January 1994, I R 67/92, Federal Tax Gazette II 1996, p. 77.
[54] Cf. Hofert/Möller, GmbHR 2009, p. 527, 528; Stadler, NZI 1993, p. 579, 580; Stegemann, INF 2005, p. 145, 149 et seq.

and debt for tax purposes. The Federal Ministry of Finance and the literature are of the opinion that sec. 8c CITA is not applicable to such participation rights.[55]

Furthermore, the granting of participation rights can help to offset loss carry-forwards with income before shares will be transferred and loss carry-forwards are thereby forfeited. If a profit participation right constitutes debt which is pursuant to sec. 5 para. 2a ITA not shown as such in the tax balance sheet, taxable income accrues in the fiscal year of the issuance of the profit participation rights. This taxable income can be offset with existing loss carry-forwards.[56] Thus, participation rights can be a suitable instrument for a tax-optimal restructuring.

Excursus: Another possibility to generate taxable income - for the purpose of offsetting it with loss carry-forwards - is to grant non-interest-bearing loans or to temporarily cancel the interest on existing loan receivables. The income occurs by discounting the nominal liability amount at a statutory rate of 5.5% in the tax balance sheet (gain pursuant to sec. 6 para. 1 no. 3 ITA). In the subsequent periods deductible expenses occur due to the addition of accrued interest.[57]

II. Requalification of Debt Instruments to Equity

The following table provides an overview of financial instruments and their qualification for tax and commercial law purposes.

Certain financial instruments have partly equity-like and partly debt-like characteristics. Therefore, the treatment for tax and / or GAAP purposes can be difficult.

In general, “Fixed Interest“ and “Loss Participation“ should exclude each other, “Repayment Claim” and “Loss Participation“ as well. Furthermore, “Repayment Claim = NO“ should generally go along with “Share in Liquidation Proceeds = YES“; investors would normally not accept to exclude both). In the event of identical economic interests of the indirect debtor (shareholder of the debtor company) and the creditor of the participation right, the share in liquidation proceeds might be excluded because the financial instrument could in this case be recorded in the tax balance sheet as debt and in the GAAP balance sheet as equity.

If “Fixed Interest = YES” goes along with “Repayment Claim = NO”, the instrument may qualify as equity (not as debt). In that case, an amount paid in as "loan" may be treated either as a (tax neutral) contribution to the equity reserves (*Rücklagen*; with specific tax issues when repaid) or as (taxable) business income with the subsequent amortization as deducti-

[55] Cf. Federal Ministry of Finance dated 4 July 2008 decree regarding limitation of loss carry-forwards for corporations (sec. 8c CITA), Federal Tax Gazette I 2008, p. 736, ann. 5 and 7. According to ann. 7, only participation rights providing a right in the liquidation proceeds (participation rights pursuant to sec. 8 para. 3 sentence 2 CITA) are a comparable instrument within the meaning of sec. 8c para. 1 sentence 1 CITA. According to some views in the literature, however, even these participation rights are not considered to be comparable, cf. Benz/Rosenberg, in: Blumenberg/Benz, Die Unternehmensteuerreform 2008, p. 175; Breuninger/Schade, Ubg 2008, p. 261, 264; Lang, DStZ 2007, p. 652, 653; Meiisel/Bokeloh, BB 2008, p. 808, 810; Streck/Olbing, CITA Commentary, sec. 8c, ann. 11; for a different view cf. Dötsch, in: Dötsch/Pung, CITA Commentary, sec. 8c, ann. 32.

[56] Cf. Haarmann, in: Arbeitsbuch zur 60. Steuerrechtlichen Jahresarbeitstagung 2009 der Arbeitsgemeinschaft der Fachanwälte für Steuerrecht e.V., p. 146, 151 et seq.

[57] Ibid.

ble business expense in case of repayment of the principal amount (sec. 5 para. 2a ITA). A "loan” term of more than 30 years indicates equity treatment.

The table seems to show a strong preponderance of “Participation Rights” / “Jouissance Rights” (*Genussrechte*). Although they are frequently used in practice, there is no predominance over any of the other instruments. There is, however, much legal leeway in structuring them; some of the subtle differentiations that have developed are reflected in the table.

Equity / Debt Qualification of certain Financial Instruments (Assumption: Target / Borrower = German Corporation)

	Remuneration / Interest	**Loss Participation**	**Repayment Claim**	**Share in Liquidation Proceeds**	**Consultation and Controlling Rights**	**German GAAP Treatment**	**German Tax Treatment as ….**	**Income Character**	**Domestic Withholding Tax (plus 5.5% SOLI thereon)**	**Relevant German Income Tax Rules**	**Reduction under Domestic Law down to 15% WHT (sec 44a IX) + 5.5% SOLI thereon**	**German limited tax liability of non-German Lender / Investor**	**Treatment as "xxxx" under German Tax Treaties as a rule (may provide for further reduction of German Withholding Tax)**
Equity (Eigenkapital)	Profit related	YES	NO	YES	YES	EQUITY	EQUITY	Dividends	25%	secs 20 I 1 / 43 I 1 / 44a IX / 50 d III / 49 I 5 a) ITA	15% Substance Requirements	YES / WHT	Dividends
Equity (Eigenkapital)	Fixed	YES	NO	YES	YES	EQUITY	EQUITY	Dividends	25%	secs 20 I 1 / 43 I 1 / 44a IX / 50 d III / 49 I 5 a) ITA	15% Substance Requirements	YES / WHT	Dividends
Jouissance Right / Participation Right (Genussrecht)	Profit related	YES	NO	YES	YES	EQUITY	EQUITY	Dividend treatment	25%	secs 20 I 1 / 43 I 1 / 44a IX / 50 d III / 49 I 5 a) ITA	15% Substance Requirements	YES / WHT	Dividends
Jouissance Right / Participation Right (Genussrecht)	Profit related	YES	NO	YES	NO	EQUITY	EQUITY	Dividend treatment	25%	secs 20 I 1 / 43 I 1 / 44a IX / 50 d III / 49 I 5 a) ITA	15% Substance Requirements	YES / WHT	Dividends
Jouissance Right / Participation Right (Genussrecht)	Profit related	YES	NO	NO	NO	EQUITY	DEBT	Interest	25%	secs 20 I 7 / 43 I 2 / 44a IX / 50 d III / 49 I 5 c) bb) ITA	15% Substance Requirements	YES / WHT	Interest
Jouissance Right / Participation Right Economically like PPL	Profit related	NO	YES	NO	NO	DEBT	DEBT	Interest	25%	secs 20 I 4 / 43 I 3 / 44a IX / 50 d III / 49 I 5a ITA	15% Substance Requirements	YES / WHT	Dividends; Interest or no reduction (e.g. Canada, France; Italy, USA)
Jouissance Right / Participation Right (Genussrecht)	Fixed	NO	YES	NO	NO	DEBT	DEBT	Interest	25%	secs 20 I 7 / 43 I 2 / 44a IX / 50 d III / 49 I 5 c) bb) ITA	15% Substance Requirements	YES / WHT	Interest
Jouissance Right / Participation Right (Genussrecht)	Fixed	NO (YES)	YES (NO)	NO	NO	depends on details re loss participation	DEBT	Interest	25%	secs 20 I 7 / 43 I 2 / 44a IX / 50 d III / 49 I 5 c) bb) ITA	15% Substance Requirements	YES / WHT	Interest
Atypical Silent Partnership	Profit related	YES	NO	YES (share in hidden reserves)	YES	DEBT	EQUITY	Business Income	Ordinary IT (45%) or CT (15%) Trade Tax (PE: 7%-17%)	secs 15; 49 I 2a ITA	n.a.	Yes / German PE Business Income	Business Income
Typical Silent Partnership	Profit related	YES (NO)	NO (YES)	NO	NO	DEBT	DEBT	Interest	25%	secs 20 I 4 / 43 I 3 / 44a IX / 50 d III / 49 I 5a ITA	15% Substance Requirements	YES / WHT	Dividends or no reduction
Profit Participating Loan (PPL)	Profit related	NO	YES	NO	NO	DEBT	DEBT	Interest	25%	secs 20 I 4 / 43 I 3 / 44a IX / 50 d III / 49 I 5a ITA	15% Substance Requirements	YES / WHT	Dividends; Interest or no reduction (e.g. Canada, France; Italy, USA)
"Ordinary" Loan	Fixed	NO	YES	NO	NO	DEBT	DEBT	Interest	none; full net taxation if loan secured by mortgage	sec 20 I 7; mortgage: sec 49 I 5c) aa) ITA	n.a.	generally none except loan secured by mortgage	Interest; in case of loan secured by mortgage: reduction of net taxation to maximum WHT under treaty
Preferred Stock	Profit related	YES	NO	YES	NO	EQUITY	EQUITY	Dividend treatment	25%	secs 20 I 1 / 43 I 1 / 44a IX / 50 d III / 49 I 5 a) ITA	15% Substance Requirements	YES / WHT	Dividends
Preferred Stock	Fixed combined with profit related	YES	NO	YES	NO	EQUITY	EQUITY	Dividend treatment	25%	secs 20 I 1 / 43 I 1 / 44a IX / 50 d III / 49 I 5 a) ITA	15% Substance Requirements	YES / WHT	Dividends

Appendix: Jurisdiction, Administrative Decrees and Literature regarding the respective Subject Matters

1. Full or partial Waiver of the Loan Receivable

Decisions of the Federal Tax Court: dated 26 November 1980, I R 52/77, Federal Tax Gazette II 1981, p. 181; dated 20 February 1986, IV R 172/84, BFH/NV 1987, p. 493; dated 9 June 1997, GrS 1/94, Federal Tax Gazette II 1998, p. 307; dated 29 July 1997, VIII R 57/94, Federal Tax Gazette II 1998, p. 652; dated 16 May 2002, IV R 11/01, Federal Tax Gazette II 2002, p. 854.
Administration: Federal Ministry of Finance, decree dated 27 March 2003, Federal Tax Gazette I 2003, p. 240.
Literature: Bauschatz, GmbHR 2008, p. 1204; Demuth, KÖSDI 2008, p. 16177; Drews/Götze, DStR 2009, p. 945; Eilers/Bühring, DStR 2009, p. 137; Geist, BB 2008, p. 2658; Gondert/Büttner, DStR 2008, p. 1676; Kohlhaas, GmbHR 2009, p. 531; Knebel, DB 2009, p. 1094; Kroniger/Korb, BB 2008, p. 2656; Scheunemann/Hoffmann, DB 2009, p. 983; Schäfer-Elmayer/Müller, StB 2009, p. 190; Wagner, BB 2008, p. 2671.
Commentary: Dötsch/Pung, CITA, sec. 8b, ann. 142.

3. "Repurchase" of the Loan Receivable by the Debtor Company below Par Value

Literature: Schultz, Status: Recht 2009, p. 97.

4. Purchase of the Loan Receivable below Par Value by a Company affiliated to the Debtor Company

Decision of European Court of Justice: dated 26 June 2003, C305/01 - *MKG-Kraftfahrzeuge-Factoring GmbH*, Federal Tax Gazette II 2004, p. 688.
Decisions of the Federal Tax Court: dated 4 September 2003, V R 34/99, Federal Tax Gazette II 2004, p. 667; dated 20 December 2001, I B 74/01, DStRE 2002, p. 257.
Decisions of the Regional Tax Courts: Hesse, dated 31 May 2007, 6 V 1258/07; Düsseldorf, dated 15 February 2008, 1 K 3682/05 U.
Literature: WTS Tax Journal 02/2003; Schmidt/Hageböke, DStR 2002, p. 2150; Gosch, StBp 2002, p. 117; Schultz, Status: Recht 3/2009, p. 97.

5. Debt-Equity-Swap: Waiver of Loan Receivable against an Equity Participation in the Debtor Company

Literature: Mückl, FR 2009, p. 497; Redeker, BB 2007, p. 673.

7. Contribution of the Loan Receivable into an affiliated Company

Literature: Scheunemann/Hoffmann, DB 2009, p. 983; Altrichter-Herzberg, GmbHR 2009, p. 466; Neyer, AG 2009, p. 322.

8. Debt-Mezzanine-Swap

Decision of the Federal Tax Court: dated 19 January 1994, I R 67/92, Federal Tax Gazette II 1996, p. 77.
Administration: Federal Ministry of Finance, decree dated 4 July 2008 regarding the limitation of loss carry-forwards for corporations (sec. 8c CITA), Federal Tax Gazette I 2008, p. 736.
IDW: HFA 1/1994, IDW Fachnachrichten 1994, p. 269.
Literature: Benz/Rosenberg, in: Blumenberg/Benz, Die Unternehmensteuerreform 2008, p. 175; Breuninger/Schade, Ubg 2008, p. 261; Haarmann, in: Arbeitsbuch des DAI zur 60. Steuerrechtlichen Jahresarbeitstagung 2009, p. 146; Hofert/Möller,

GmbHR 2009, p. 527; Lang, DStZ 2007, p. 652; Meiisel/Bokeloh, BB 2008, p. 808; Stadler, NZI 1993, p. 579; Stegemann, INF 2005, p. 145.
Commentary: Streck/Olbing, CITA, sec. 8c, ann. 11; Dötsch, in: Dötsch/Pung, CITA, sec. 8c, ann. 32.

Glossary