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Promulgation of the Act to Promote Private Investment and Germany as a Financial Centre

On 9 February 2026, the Act to Promote Private Investment and Germany as a Financial Centre was promulgated in the Federal Law Gazette. The legislative process is thus complete.

The Act focuses on measures to improve the financing conditions of companies and to make the financial sector more competitive in the areas of financial market law, commercial law, supervisory law and tax law, among other things.

A significant change in tax law concerns the roll-over of hidden reserves in corporation shares. The maximum amount for the transfer of realised hidden reserves from the sale of shares in corporations held as business assets to preferential reinvestment assets (e.g. shares in corporations or buildings) is raised from EUR 500,000 to EUR 2,000,000. The increased amount applies for the first time to capital gains arising in financial years beginning after 9 February 2026.

For further details see GTM October 2025.

Current Federal Tax Court Rulings on Employee Share Ownership Schemes

Employee share ownership schemes (such as shares, profit participation rights or a silent partnership in the employer's company) offer an attractive opportunity for employees to participate in the economic success of a company. Especially in times of rising costs and tight budgets, employee share ownership schemes can help to bridge the gap between cost reduction and talent retention. This is especially true when tax advantages can be used to achieve cost savings for the employer and a higher net income for employees.

Regarding the tax treatment of regular income from shareholdings in the employing entity, there is often a dispute between the tax authorities and the taxpayer as to whether this is income from employment or income from capital assets.

With its rulings VIII R 13/23 and VIII R 14/23 of 21 October 2025, the German Federal Tax Court has now published two decisions in which he makes important statements on the tax treatment of employee share ownership schemes, thereby creating greater legal certainty.

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Background

The Future Financing Act increased the tax allowance for employee share ownership to EUR 2,000 per year from 2024 onwards: granting employee share ownership generally results in a monetary benefit at the time of receipt. If certain requirements are met, an allowance of up to EUR 2,000 per year and employee can be claimed for this benefit. In addition, small and medium-sized enterprises (SMEs) can make use of deferred taxation, which prevents immediate tax deduction when shares are transferred.

Regarding the taxation of regular remuneration from shareholdings, a fundamental distinction must be made between income from employment and capital income.

Income from employment includes salaries, wages, bonuses, royalties, and other remuneration and benefits for employment in the public or private sector. Furthermore, income from employment is all income accruing to the employee from the employment relationship. The designation or form under which the income is granted is irrelevant. If benefits that are not based on the employment relationship are provided to an employee, this does not constitute income from employment.

Income from capital assets includes, among others, income from shares and from profit participation rights that are linked to the right to profits and liquidation proceeds of a corporation. If there is no participation in the liquidation proceeds of a corporation, this constitutes a so-called obligatory profit participation right, which generates income from other capital claims of any kind. Income from participation in a commercial enterprise as a silent partner is also capital income.

Principles underlying the current Federal Tax Court rulings

In its latest rulings, the Federal Tax Court has decided on cases relevant to practice and has classified the regular remuneration from employee shareholdings as income from capital assets.

Decision VIII R 14/23: Profit participation right

In case VIII R 14/23, the taxpayer (plaintiff) was employed by stock corporation B-AG. B-AG gave selected employees and managers the opportunity to acquire uncertificated profit participation rights in their company. The profit participation rights conferred a claim to interest, the amount of which depended on the company's business performance. The profit participation capital also participated in the company's losses but did not participate in the liquidation proceeds.

In its income tax assessment, the tax office recorded the profit participation distribution as income from employment. The taxpayer lodged an appeal and subsequently filed a lawsuit with the aim of having the profit participation interest classified as income from capital assets, which is subject to withholding tax with a separate tax rate.

The Federal Tax Court ruled in favour of the plaintiff and decided that regular remuneration from an obligatory employee profit participation right does not generally constitute income from employment.

According to the Federal Tax Court, these profit participation distributions rather constitute capital income. According to the Court, the profit participation rights in the case in question had no participation in the liquidation proceeds but were participation rights similar to bonds and other capital claims.

There was a special legal relationship under company law (in addition to the employment relationship) because a serious agreement existed and was implemented accordingly, and the special legal relationship had its own economic content in addition to the employment relationship. In this case, the regular payments were exclusively prompted by the special legal relationship and did not form part of the employee's wages. Regular remuneration from a obligatory profit participation right – as in the present case – constitutes income from capital assets and is subject to the separate tax rate.

Decision VIII R 13/23: Silent partnership

In the case underlying decision VIII R 13/23, the employee (plaintiff) and limited liability company B-GmbH concluded a "partnership agreement for a typical silent partnership". Among other things, this stipulated that the silent partnership would end upon termination of the silent partner's employment relationship without the need for notice of termination. There was no obligation under labour law to grant the employee the silent partnership.

The tax office assumed that the profit shares were part of the plaintiff's income from employment.

In this case, the Federal Tax Court also ruled in favour of the taxpayer, stating that the income from the employee participation was capital income.

The Federal Tax Court assumed that the income (in this case from the typical silent partnership) did not trigger income from employment, as there was a tax-effective special legal relationship. The

Court also emphasised the requirement for effective justification, serious agreement and implementation, and that this special legal relationship must have its own economic substance in addition to the employment relationship in terms of its structure.

Regular remuneration from a typical silent partnership of the employee in the employer's company, which is based on this special legal relationship, is therefore subject exclusively to taxation as capital income.

Practical information

In the case of profit participation rights granted to employees, the income is generally subject to withholding tax, as it constitutes income from capital assets.

For the employer, this means that no wage tax is deducted, as the income is not considered income from employment.

The current case law is also significant beyond the individual cases that have been decided. Despite the existing case law on employee participation, careful and well thought-out structuring of participation models is essential. This is the only way to effectively avoid disputes in the context of tax audits. Otherwise, the employer runs the risk of being held liable retrospectively for wage tax amounts not withheld.

Lower Tax Court of Berlin-Brandenburg (10 K 10106/23): Crediting Foreign Withholding Tax Against Domestic Trade Tax

In its judgment dated 14 January 2026, the Lower Tax Court of Berlin-Brandenburg has determined that withholding tax (WHT) levied in the USA on dividends can indeed be credited against the trade tax of the domestic recipient.

The corporate income tax and trade tax treatment of cross-border dividend income at the level of a domestic shareholder depends on the size of the shareholding.

Corporate Tax: When the participation level reaches **at least 10%** (known as **holding participation**), dividend income is 95% exempt from corporate tax, with the remaining 5% subject to a 15% corporate tax rate.

Trade Tax: If the participation level is **at least 15% at the start of the assessment period** (typically the calendar year), dividend income enjoys a 95% exemption from trade tax, with 5% taxed at approximately 15%.

Credit for Foreign WHT: It is important to note that German tax laws do not allow for the crediting of foreign WHT against German trade tax. Furthermore, credit against corporate tax in the case of holding participation is not feasible. However, in instances of portfolio dividends (where participation is less than 10% and thus fully taxed with corporate tax), foreign WHT can be credited against domestic corporate tax.

In the case at hand, the plaintiff, a German corporation, held approximately 26% in a US corporation during the dispute year 2020, though not at the beginning of the calendar year. Consequently, the dividend income was **fully subject to trade tax for the plaintiff**, while corporate tax was not applicable due to exemption. The plaintiff claimed the crediting of US WHT against its trade tax obligations.

The Lower tax Court of Berlin-Brandenburg granted this credit, despite the absence of a national legal basis. The method article of Art. 23 Double Tax Treaty (DTT)-USA (aimed at avoiding double taxation) mandates the crediting of US WHT. According to the DTT-USA principles, trade tax is also considered an income tax. The method article of the DTT does not explicitly differentiate between corporate, income, and trade tax, thus establishing the "whether" of crediting through the DTT. The Lower Tax Court of Berlin-Brandenburg addressed the gap in the Trade Tax Act regarding the "how" by applying the crediting provisions for income and corporate tax purposes (Section 34c Income Tax Act in conjunction with Section 26 Corporate Income Tax Act).

Previously, the Lower Tax Court of Hesse had ruled in its final judgment on 26 August 2020 (8 K 1860/16) that Canadian WHT could also be credited against domestic trade tax, provided the relevant DTT allows for its crediting against domestic income taxes.

It remains to be seen whether the tax office will appeal to the Federal Tax Court in the case at hand, and how the Federal Tax Court will rule, as well as how the legislator will respond.

Federal Ministry of Finance: Draft Guidance on the Tax Authorities' Principles for the Concept of Permanent Establishments

Dated 13 February 2026, the Federal Ministry of Finance (MoF) sent a draft guidance on the administrative principles for the definition and justification of a permanent establishment in domestic and international tax law to certain associations.

Content of the MoF guidance:

1. General information (including the relationship between domestic tax law and treaty law, the definition of a permanent establishment under domestic law, the definition of a

permanent establishment under treaty law, similarities and differences between the definition of a permanent establishment under domestic and treaty law)

2. Individual cases
   a. Activities in external premises or in third-party premises
   b. Service or management companies
   c. Market stalls
   d. Children's room
   e. Home office (exercising management functions in the home office, representative's permanent establishment, definition of permanent establishment under treaty law in the home office)
   f. Influencer
   g. Ships
   h. Provision of personnel or pure transfer of an operating facility

The MoF draft guidance also refers to the recently revised paragraphs 44.1 to 44.21 of the OECD Model Commentary on Art. 5 OECD Model Tax Convention regarding the concept of a permanent establishment under tax treaty law in the area of home offices and distinguishes between inbound and outbound cases in this respect.

Rules of application:

The MoF guidance dated 24 December 1999, last amended by the MoF guidance dated 22 December 2016, is repealed insofar as it contains statements on the definition and justification of a permanent establishment in domestic and international tax law. Otherwise, the above-mentioned MoF guidance continues to apply insofar as the administrative principles for the allocation of permanent establishment profits stipulate this.

The regulations are to be applied in all open cases, insofar as this does not conflict with statutory regulations.

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