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Scope of Growth Opportunities Bill shrinks significantly in reconciliation process

Bundesrat to decide on the revised bill on 22 March 2024 – outcome open

Content

On 21 February 2024, the Reconciliation Committee agreed on a compromise for the Growth Opportunities Act, which is far less substantial than the package of measures originally passed in the Bundestag (lower house of parliament). The bill, which had started as the biggest corporate tax reform since 2008, has shrunk to a minor stimulus package. The Reconciliation Committee meeting became necessary after the bill was not approved by state governments in the Bundesrat (upper house of parliament) in late November 2023.

The compromise reached by the Reconciliation Committee was supported only by the votes of the governing coalition. As the parties of the German government do not have a majority in the Bundesrat, it is unclear if the law will be passed on 22 March 2024. ▸

Scope of Growth Opportunities Bill shrinks significantly in reconciliation process

Continued from page 1

The current compromise significantly reduces the volume of tax cuts from originally EUR 6.3 billion to just over EUR 3 billion per year. Consequently, major relief measures of the package were cut, such as the improved rules for loss offsetting and the climate protection investment premium. The planned mandatory disclosure rules for domestic tax arrangements have also been deleted from the bill.

The following proposals were adopted unchanged compared to the Bundestag resolution:

- A separate provision in the Foreign Tax Act (AStG) on intercompany financing according to which interest expenses for an intercompany cross-border financing relationship (defined as in particular loans as well as the use or provision of debt or debt-like instruments) can only be deducted if the taxpayer can demonstrate that (i) principal and interest payments can be serviced throughout the entire term of the financing period ("debt capacity / cash flow test") and (ii) there was a business need for the financing and the borrowed funds were utilized for that purpose ("business purpose test"). Additionally, the interest rate for the cross-border intercompany financing relationship transaction must not exceed the interest rate at which the group refinances itself vis-à-vis third parties unless it is demonstrated in an individual case that a credit rating derived from the group credit rating is in line with the arm's length principle. Further, the new provision includes a rebuttable assumption that any intercompany cross-border financing arrangements that are mediated, arranged or passed through are considered per se a low function and risk service. This is also applicable to captive treasury centers and captive financing companies performing, e.g., liquidity management, financial risk management for other group companies. How such low function and risk service should be remunerated is only briefly described in the explanatory notes. According to these, the remuneration for such transactions is determined based on the cost-plus method considering directly attributable operating costs without including refinancing costs in the cost base. A markup between 5% and 10% is considered as not unreasonable. In addition, refinancing costs with a risk-free return must be taken into account. Given that the explanatory notes do not provide further guidance, it is currently unclear how to interpret these potentially far-reaching new rules. The rules on cross-border intercompany financing will be applicable with retroactive effect for the tax assessment period 2024.
- VAT: The introduction of mandatory B2B eInvoicing in principle as of 1 January 2025. The general transition period covers two years from 1 January 2025 to 31 December 2026.

The following measures were revised during the deliberations and were included in an amended form:

- The improved loss carryforward annual offset percentage (Sec. 10d (2) sentence 1 Income Tax Act, EStG) is to be granted for four years (2024 to 2027) at a rate of 70% (instead of the 75% provided for in the Bundestag draft, and 60% under current rules). This also applies to corporate tax, but not to trade tax, contrary to the Bundestag bill. However, the loss carryback (Sec. 10d (1) sentence 1 EStG) will not be increased. There will also be no extension of the carryback period. As a result, the old maximum limits with a carryback period of two years will apply again from 2024.
- The maximum assessment basis for the research and development allowance will be increased from currently EUR 4 million to EUR 10 million instead of EUR 12 million. The other changes will remain unchanged but will only apply from the day after the law is promulgated and not as of 1 January 2024.
- The declining balance depreciation for movable fixed assets will only be granted for assets acquired or produced after 31 March 2024 and before 1 January 2025 and will only amount to a maximum of twice the straight-line depreciation and a maximum of 20%.

The following measures will not be implemented:

- The previously planned reporting obligation for domestic tax arrangements will not be introduced.
- The premium for climate protection investments will not be a part of the Growth Opportunities Act. It remains to be seen whether the coalition will present a revised investment premium at a later date, and in particular whether it will reflect the demand of the federal states not to use the state tax authorities to apply for and pay out the premium.

The Bundesrat will decide on the revised bill on 22 March 2024. In case the bill does not get sufficient support, further meetings of the Reconciliation Committee would be possible.

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Long awaited Government draft of the MLI Application Bill finally published

The long awaited BEPS MLI Application Bill has finally been published. The MLI was already signed in 2017 by Germany and entered into force in 2021. Unlike in most other countries, this second implementation step is required for the MLI to finally modify the covered German double-tax agreements (DTAs). The BEPS MLI Application Bill provides precise instructions regarding which MLI articles are to apply in each case for nine DTAs covered.

As Germany has started to gradually transfer the DTA relevant action points of the BEPS project into the German DTA network in bilateral DTA negotiations, only 14 German DTAs are currently covered by the MLI. Of these 14 DTA, the BEPS MLI Application Bill covers only nine DTAs, i.e. the DTAs with Croatia, the Czech Republic, France, Greece, Hungary, Japan, Malta, Slovakia and Spain. Assuming that the bill is passed in the second quarter of 2024, the nine covered DTAs could be modified by the MLI, in general, as of 2025.

New DTAs have become effective

In addition to the implementation of the BEPS MLI, Germany continues to negotiate DTA modifications bilaterally. As part of these efforts, the amending protocols to the DTAs with Austria, Bulgaria, Lithuania, Luxembourg and Sweden entered into force in late 2023 and became effective on 1 January 2024.

All DTA amending protocols implement treaty law measures of the BEPS project in the bilateral relationship between Germany and the contracting states. Some MLI measures that Germany frequently implements are, for example, an amended preamble and the introduction of a principal purpose test. Beyond BEPS, the new DTA between Germany and Austria includes, among other things, new rules for the treatment of cross-border commuters.

Sweden and Germany agreed in their amending protocol, among other things, to delete the articles concerning the inheritance and gift tax as Sweden abolished this tax in 2005.

Additionally, the protocol with Luxembourg contains a significant amendment regarding the taxation of fund structures. As of this year, investment funds in the legal form of a Luxembourg "Fonds Commun de Placement" (FCP) – which are frequently encountered in practice – should be eligible for treaty benefits. This may have an impact particularly on equity funds in the legal form of an FCP that generate income from securities lending and repo transactions with German shares over the dividend record date. In addition, the minimum standards of the BEPS project under treaty law and new rules for cross-border workers are to be implemented in bilateral relations with Luxembourg.

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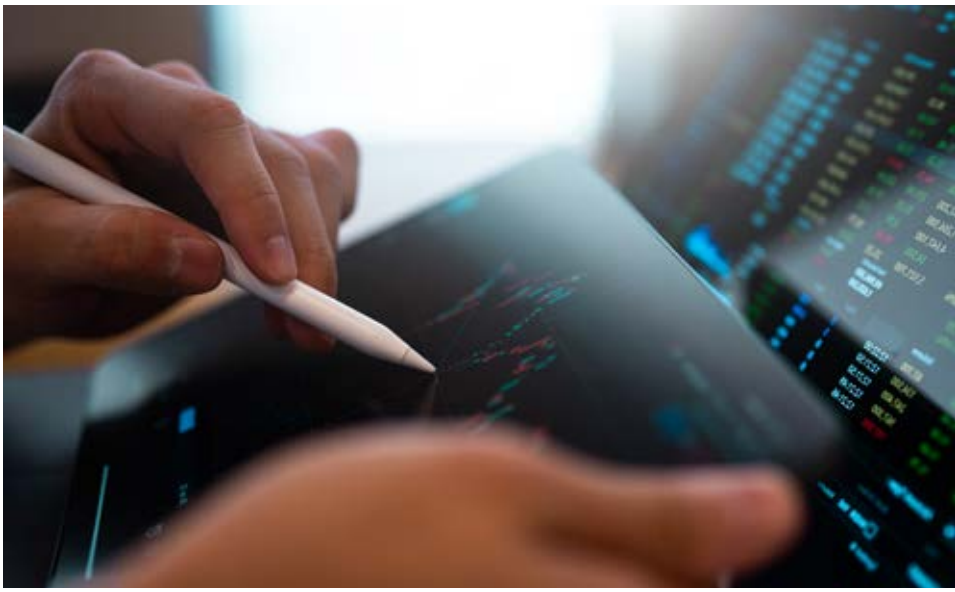

BEPS 2.0 Pillar Two legislation in force

While a number of other EU Member States had not yet passed final implementation bills by the end of the previous year, the global minimum tax came into force in Germany in December 2023.

After approval by the Federal Council (Bundesrat), it was promulgated in the Federal Law Gazette on 27 December 2023 and came into force on the day after its publication. The bill addresses the implementation of the Global Minimum Tax in accordance with the respective EU Minimum Tax Directive, the OECD Model Rules and the Agreed Administrative Guidance of February and July 2023.

With regard to Pillar Two, the Income Inclusion Rule (IIR) and Domestic Minimum Top-up Tax applies to financial years beginning after 30 December 2023, while the Undertaxed Profits Rule (UTPR) will generally apply to financial years beginning after 30 December 2024.

In addition to implementing the Base Erosion and Profit Shifting (BEPS) 2.0 Pillar Two rules into German tax law, the bill reduced the low-tax threshold from 25% to 15% for both the German controlled foreign company (CFC) rule and the German royalty deduction limitation rule.

The German implementation law does not yet address the clarifications in the third set of Agreed Administrative Guidance published in December 2023 by the OECD. It is expected that Germany will implement the guidance into national law in 2024. It is also assumed that editorial errors identified after the introduction of the law will be revised this year, e.g. as part of the Annual Tax Act 2024.

Further, the Federal Ministry of Finance is preparing a circular with additional guidance on the interpretation of the implementation law.

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Updates in German packaging law 2024 – new obligations for producers and retailers of single-use plastic products

The German Packaging Act (Verpackungsgesetz, VerpackG) regulates the placing of packaging on the German market and the responsibility of producers and retailers. The focus of the law is on plastic beverage packaging. For this, the law provides for the single-use deposit requirement, which has been gradually expanded. Since 1 January 2024, a deposit of at least EUR 0.25 must now also be charged for milk, mixed milk drinks and other drinkable milk products such as drinking yogurt, coffee drinks and vegan milk substitutes filled in single-use plastic bottles with a filling volume of 0.1 to 3.0 liters. Like other packaging in the single-use deposit system, packaging for these milk and mixed milk products must now be clearly marked as requiring a deposit and the retailer must show the deposit amount separately alongside the product price. Furthermore, single-use plastic bottles containing milk, mixed milk drinks and other drinkable milk products must be taken back after they have been emptied wherever drinks are sold in single-use plastic bottles.

Also on 1 January 2024, the Single-Use Plastic Fund Act (Einwegkunststofffondgesetz, EWKFondsG) and the specifying Single-Use Plastic Fund Ordinance (Einwegkunststofffondsverordnung, EWKFondsV) came into force. Littering, i.e. the careless disposal of waste such as products and packaging made from single-use plastic, is not only a problem for the environment, but also a financial burden for public waste disposal companies that collect this waste and dispose of it properly. The EWKFondsG now obliges producers and retailers of certain single-use plastic products such as containers, bags and films for food and beverages to register with the Federal Environment Agency's (Umweltbundesamt, UBA) new online register "DIVID" and to contribute to the costs of disposing of packaging and products by paying into a so-called single-use plastic fund from spring 2025. The amount of the levy depends on the type and quantity of products placed on the market by the respective producer or retailer. The UBA is currently still in the process of setting up the online platform "DIVID" for the single-use plastic fund. According to the UBA's current schedule, registration in the DIVID register should be possible from 1 April 2024. The revenue flows to certain public bodies, such as cities and municipalities, so that they can offset their costs for cleaning and disposing of single-use plastic waste in public spaces with the revenue from the fund. The public bodies must also register with UBA's platform "DIVID" and specify the type and scope of services in order to receive revenue from the fund.

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BMF publishes first draft of Accounting Data Interface Regulation

In Germany, the tax authorities have the right to inspect data stored in documents if they are created using a data processing system and are subject to retention obligations. Since 2002, a tax inspector has three different types of data access to choose from, which can also be requested cumulatively: Direct data access (Z1), indirect data access (Z2) to the IT system, as well as data carrier handover (Z3).

For the Z3 data access (data carrier handover), there have so far only been specific guidelines from the German tax authorities for payroll accounting systems ("DLS" interface) and cash register systems ("DSFinV-K" interface). For financial accounting systems, no exact minimum scope has been defined so far.

Among other things, DAC7 has now created the legal framework that a digital interface for a standardized export of tax-relevant data can be determined.

The Federal Ministry of Finance (BMF) has defined a first draft of this interface in the so-called accounting data interface regulation (DSFinVBV). The draft contains, among other things, general principles as to which data records must be included at least and in which format the data should be delivered. This is a standardization of the exported accounting data records. Also detailed is the data standard, which in particular regulates the designation of the fields and their content.

This draft was shared with selected associations on 1 December 2023 with a request for comments.

The draft describes the minimum standard which an accounting system must have. It also outlines in detail the general data standard. The taxpayer must therefore provide multiple CSV files and descriptive XML files and, if necessary, supplement them with additional fields and tables.

The regulation is scheduled to take effect on 31 December of the third year following its announcement and will apply for fiscal years that start after its effective date. In other words, if the regulation is passed in 2024, it will come into effect on 31 December 2027 and will apply to fiscal years beginning after 31 December 2027.

The tax administration foresees sanctions if these requirements are not met. If the data is not provided in accordance with these uniform digital interfaces, the so-called correctness presumption of accounting does not apply. In addition, further fines might apply.

It is therefore highly advisable to start the implementation process as soon as the present draft comes into effect. Companies should contact their software providers and, if necessary, plan for corresponding budgets and resources if this involves in-house development of the accounting system or if no adaptation is made by the software provider.

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BMF publishes final decree on the application of the new Foreign Tax Act

On 22 December 2023, the German Federal Ministry of Finance (BMF) published the final version of the decree on the application of the new Foreign Tax Act (AStG) following legislative amendments by the ATAD Implementation Act and the Defence against Tax Havens Act. The so-called AStG decree applies to the Foreign Tax Act in the version applicable from 1 July 2021. The updated AStG decree particularly includes revised provisions on the German taxation of Controlled Foreign Corporations (CFC taxation) and exit taxation for individuals. The draft version was published on 19 July 2023 and was subject to comments provided to the BMF by several institutions and associations (read more about the content of the draft in *German Tax & Legal Quarterly issue 3|23).*

Foto: Bundesministerium der Finanzen / Photothek

The final AStG decree contains several editorial amendments. Compared to the draft version as of July 2023 many of the BMF's views which were criticized within the statements submitted to the BMF remain unchanged. In some places, however, the BMF has adjusted its views. These adjustments mainly concern the CFC taxation, in particular the circumstances triggering CFC taxation as well as the definition of so-called passive income subject to CFC taxation (by interpreting the catalogue of so-called "active" income according to Sec. 8 para. 1 AStG).

Particularly noteworthy are the changes to the definition of active trading activities and clarifications on "harmful participation". Compared to the draft version, the final AStG decree defines trade as the commercial acquisition and sale for consideration of goods and merchandise that are not subject to any significant change in their substance. With this extension, the BMF is no longer limited to the sale of goods but also includes the acquisition in the trade definition. Furthermore, the BMF clarifies that the mere provision of computing capacities or digital platforms does not necessarily constitute a "harmful participation" that would lead to passive trade income.

In addition, the AStG decree now also includes the possibility to fulfill the so-called motive test in cases of outsourcing to related parties as long as they are located in the same state, which was still qualified as being harmful in the draft version. In addition, it now appears to have been clarified that the regulations on a taxable transfer of assets through a mere change of taxing jurisdiction ("Entstrickung") do not apply in the context of the CFC taxation.

However, the very restricted view of the BMF relating to the control concept triggering the CFC taxation according to which taxpayers can also be subject to CFC taxation with only minority shareholdings remains mainly unchanged. The same applies to the BMF's views on foreign reorganizations leading to passive income (for example, blocking periods according to Sec. 22 UmwStG – i.e. detailed German reorganization regulations – are considered relevant also in the case of foreign reorganizations).

It should be noted that the AStG decree still refers to the low-tax threshold based on an effective tax rate of 25%. Due to the implementation of the Global Minimum Tax, which came into force on 28 December 2023, this threshold was reduced to 15%.

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New cross-border commuter regulation for employees in the private sector – new protocols to tax treaty between Germany and Austria

The amended cross-border commuter regulation for employees in the private sector has been effective since 1 January 2024 (Art. 15 para. 6). It was introduced to better meet the requirements of the changing working environment, such as more flexible working conditions and working from home. The tax authorities in Austria and Germany concluded a consultation agreement in this regard on 19 December 2023, which the Federal Ministry of Finance (BMF) published in a letter dated 20 December 2023. In the letter, the BMF also addresses the new cross-border commuter regulation for public sector employees. However, the following comments are limited to the information on Art. 15 para. 6.

According to Art. 15 para. 6 of the double tax agreement (DTA), salaries, wages and similar remuneration received by a resident of a contracting state from employment may only be taxed in the state of residence if this person:

a) has his or her principal place of residence in that contracting state in the vicinity of the border and
b) normally carries out their employment in the vicinity of the border.

According to the BMF, the main residence is where the center of life is located.

The protocol to the DTA stipulates that "near the border" refers to municipalities whose territory is wholly or partially up to 30 kilometers away from the border. The BMF letter lists the towns and municipalities that meet this requirement in its annexes.

The activity is usually performed in the border zone if it is performed outside the border zone in whole or in part on not more than 45 working days and on not more than 20% of the actual working days. In the case of part-time employees who are only employed on a daily basis (e.g. Monday to Wednesday), the maximum limit is to be determined using only the 20% method.

In addition to sick days and vacation days, the BMF letter also lists days of parental leave, care leave, flex time and days of leave within the framework of part-time models (e.g. block model for partial retirement) as days not to be taken into account. Weekends or public holidays, on the other hand, are also considered working days if the work is performed and remunerated by the employer on these days.

The tax authorities point out that each employment relationship must be considered in isolation. This is to be welcomed as an isolated consideration makes practical handling much easier. In contrast, cross-border commuter status under the DTA between Germany and Switzerland must be assessed uniformly for all employment relationships in the respective year. According to the BMF letter, a change of residence within the border zone should also lead to the respective periods being considered in isolation. In our opinion, this does not follow either from the DTA or from the protocol to the DTA. It remains to be seen whether this view is confirmed by case law if subject to a future court procedure.

In the case of employees who are employed by the same employer for at least five days a week throughout the year, the BMF does not object if only the 45-day limit is checked.

Employers of (potential) cross-border commuters between Austria and Germany should consider the BMF view when treating these situations for payroll tax purposes. The list of affected cities/municipalities should make things much easier for employees and companies. A further simplification is the restriction to the 20% rule for year-round employment on five working days per week. Under certain circumstances, it may make sense to waive this simplification, for example if the cross-border commuter regulation is not to be applied and the 45-day limit may be exceeded.

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Latest guidance provided by the Ministry of Finance on question when a home office qualifies as a permanent establishment

The German Ministry of Finance (BMF) provided guidance on whether a home-office can establish a permanent establishment (PE) in its letter dated 5 February 2024, which amended the application decree to the German Fiscal Code (AEAO).

In general, the qualification of a home office as a PE depends on whether the employer has the power of disposal over the home office. The BMF states in its amendment to the AEAO that from a German tax perspective a home office in principle does not constitute a PE of the employer due to the lack of power of disposal (If, however, an employee performs management activities and these convey the company's power of disposal, a place of management PE may be created). This even applies if

- the employer assumes the costs for the home office and its equipment;
- a rental agreement for the employee's domestic premises between employer (tenant) and employee (landlord) is concluded, unless the employer is actually authorized to use the rooms for other purposes (e.g. to send other employees to the premises or a right to enter the rooms outside of work safety inspections);
- the employee is not provided with another workplace by the employer.

According to the amendment this also applies to the German interpretation of a PE under tax treaty law.

The German view on the "power of disposal" criteria thus deviates from the OECD view expressed in Art. 5 in the OECD Commentary, which applies a wider definition of the "power of disposal" criteria. According to OECD Commentary, a home office may under certain circumstances (e.g. home office is used continuously and the employer does not provide an office) establish a PE.

Due to the fact that this OECD interpretation of the "power of disposal" is to some extent shared by other European countries (e.g. Austria and France), a qualification conflict may arise leading to potential double taxation. Therefore, even if Germany provides for some simplifications compared to other countries in relation to the home office treatment, the qualification of the home office still plays a vital role in remote-work situations.

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Revised BMF interpretative letter published on tax treatment of wages and salaries under double tax agreements

On 12 December 2023, the revised interpretative letter of the Federal Ministry of Finance (BMF) on the tax treatment of wages and salaries under double tax agreements (DTAs) was published. Comprising 427 paragraphs (previously 372), the letter is now significantly more extensive and contains numerous changes. In the letter, the BMF explains its view of the tax treatment of income from employment in accordance with the OECD Model Tax Convention (OECD MTC) and in places also deals specifically with DTAs concluded by Germany. It applies to all open cases, i.e. also to matters from 2023.

The following changes are particularly worth mentioning:

- The letter contains additional comments on the determination of residence, including new examples indicating that the German tax authorities will assume a change of residence less frequently than is customary in other countries, especially in Europe. In case of secondments out of Germany this will lead to partial double taxation in many constellations. In the case of secondments to Germany, part of the income would be taxed by none of the contracting states. However, in this case, Sec. 50d (9) Sent. 1 No. 1 German Income Tax Act (a national switch-over clause) applies and Germany taxes this portion of the remuneration.
- Another change increasing the risk of double taxation regards the taxation of stock options income. The Finance Ministry stresses that for the criterion of treaty residency (Art. 4 OECD MTC), the date on which the income is received is always relevant (applying the principles of Federal Tax Court judgment of 21 December 2022, I R 11/20). According to the feedback we received from our local tax specialists, a significant proportion of the other countries do not agree with and are unable to follow this approach. They base the assessment of treaty residence on the residence during the entire vesting period (instead of the sole receipt date). Lengthy mutual agreement procedures would be necessary to resolve the double taxation.
- A (potential) challenge for employers is the implementation of extended documentation requirements in connection with the determination of the economic employer and the assumption of costs.

Identifying and documenting the economic employer

When determining which country, i.e. the employee's home or host country, has the right to tax the wages under the relevant DTA, various criteria have to be applied. One of these criteria is that of the so-called economic employer, which in turn has to be determined based on the following two criteria: The host company becomes the economic employer of the employee if the employee is integrated into the organization of the host company and the latter bears or should have borne the wages in accordance with the arm's length principle. Determining in whose business interest the employee is performing his/her activities is of central importance. According to the arm's length principle, the costs must be borne by the company in whose interest the performance takes place.

The new decree contains specific criteria for assessing the interests and detailed explanations on the allocation of possible performance-related costs. These must be documented comprehensively, both in terms of reason and amount, at the level of each individual employee and certified to the employees themselves.

Moreover, the updated decree contains supplementary information on determining the economic employer of executive employees (managing directors and supervisory board members) and the resulting wage tax deduction obligations. In such cases there should be a German tax liability, even if no separate remuneration is granted for the respective capacity.

The new documentation requirements do not only affect international assignments, but all constellations in which the change of an economic employer might be relevant.

Employers of international employees should determine what adjustments are required in light of the new interpretative letter and implement these as soon as possible. Individuals residing in Germany should, if necessary, with the support of a tax advisor, check the risks of double taxation of salary income based on the revised letter.

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German Ministry of Finance adopts European Court of Justice's VAT treatment regarding "control fees"

In 2022 the European Court of Justice (ECJ) ruled that fees assessed by private parking space operators in case drivers do not comply with the parking space terms for use (so-called "Kontrollgebühren" or "control fees") must be seen as consideration for a service (ECJ judgement dated 20 January 2022, C-90/20, Apcoa Parking Danmark). Thus, such service is subject to VAT.

The ECJ took the view that parking at a private parking space constitutes a legal relationship between the parking space operator and the driver. This comprises the observance of the terms of use of the parking space and thus includes the obligation to pay – besides the parking fee – "control fees" in case the driver does not comply with the terms of use. The ECJ assumes that such "control fees" constitute a remuneration for the parking service performed by the parking space operator as such fees have a direct connection with the parking service and the amount of the fee covers parts of the costs incurred with the performance of the service.

Up to now, the German tax authorities have treated "control fees" as compensation payments and thus out of scope of German VAT.

In a letter dated 15 December 2023 the German Ministry of Finance (BMF) now adopted the view of the ECJ. Consequently, the private parking space operators perform services subject to VAT when they assess "control fees". This view applies to all open cases, but it will not be objected if fees received until 15 September 2023 will be treated as compensation payments.

In practice this means that an entrepreneur may request an invoice showing VAT. Furthermore, the impact on similar cases such as the VAT treatment of increased transportation charges (erhöhte Beförderungsentgelte) should be observed.

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Federal Constitutional Court (BVerfG) on book value transfers between partnerships with identical partners

The Federal Constitutional Court (BVerfG) published on 12 January 2024 its long-awaited decision on book value transfers between partnerships with identical partners. According to the BVerfG, the provision of Sec. 6 para. 5 sentence 3 EStG (Income Tax Act) is unconstitutional insofar as it excludes a book value transfer between such partnerships (ruling of 28 November 2023, case reference: 2 BvL 8/13). The BVerfG obliges the legislator to introduce a retroactive new regulation and, until then, allows the (retroactive) possibility of a tax-neutral transfer of assets at book value between partnerships with identical partners.

Sec. 6 para. 5 sentence 3 nos. 1 to 3 EStG allows the transfer of assets at book value (without the disclosure of any hidden reserves) in return for the granting or reduction of company rights in the case of co-entrepreneurships in three cases. For example, Sec. 6 para. 5 sentence 3 no. 3 EStG regulates the tax-neutral transfer between the special business assets of a partner to the joint assets of the same or another partnership in which the transferor holds an interest or vice versa, provided that the taxation of hidden reserves is ensured. However, the wording of the law does not mention the case where an individual asset is to be transferred directly between the joint assets of sister partnerships free of charge.

Based on the wording of the law, the tax authorities have maintained the opinion that the latter cases do not constitute an application of Sec. 6 para. 5 sentence 3 EStG and therefore no transfer at book value takes place in these cases.

According to the Federal Ministry of Finance (BMF), this even applies in the case of sister partnerships with identical partners. However, the view of the tax authorities was challenged by the Federal Tax Court (BFH, decision of 15 April 2010, case reference IV B 105/09). As a result, the tax authorities have so far continued to take the view that the transfer of an asset of the joint assets of a partnership to a sister partnership with the same partners leads to the disclosure of hidden reserves when issuing assessment notices. Finally, the First Senate of the BFH referred the legal question to the BVerfG (decision of 10 April 2013, case reference I R 80/12) and suspended the relevant proceedings until the BVerfG decision.

With its decision, the BVerfG obliges the legislator to pass a new regulation retroactively for transfer transactions after 31 December 2000.

Taxpayers in affected cases should now approach the tax authorities on the basis of the ruling with a request for an amended assessment notice (transfer at book value without disclosure of hidden reserves).

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German Federal Tax Court grants full tax exemption to Luxembourg specialized property fund based on ECJ ruling in the "L Fund" case (C-537/20)

On 11 October 2023, the German Federal Tax Court (BFH) gave its final ruling in the case "L Fund" (C-537/20), granting a full tax exemption to a Luxembourg specialized property fund, saying that relevant Investment Tax Act provisions contravene the free movement of capital (Art. 63 of the Treaty on the Functioning of the European Union, TFEU).

L Fund was a property fund set up as a specialized investment fund under Luxembourg law (SIF-FCP), with neither its registered office nor its central administration in Germany. In the relevant years 2008 to 2010, L Fund received income from the rental of its properties and from the sale of some of them. L Fund claimed a full tax exemption under the applicable German Investment Tax Act provision for the relevant years. The tax authorities denied the tax exemption, arguing the German tax exemption regulation was only applicable to German resident funds.

On 27 April 2023, the European Court of Justice (ECJ) decided the request for a preliminary ruling and found that the different tax treatment of spezialized property funds resident and non-resident in Germany restricted the free movement of capital and was not justified by overriding reasons in the public interest, in particular the coherence of tax systems and the balanced distribution of taxing powers between Member States. The BFH applied this view, saying that the German Investment Tax Act exemption regulation must be interpreted in light of the free movement of capital and therefore also be applicable for non-German resident funds.

Like the ECJ decision in the L Fund case, the latest decision by the BFH also indicates that the German Investment Act legislation was not compatible with EU law until 31 December 2017. Further decisions by the BFH in other pending proceedings concerning a French FCP (I R 1/20) and a Luxembourg SICAV (I R 2/20) are expected to be issued shortly. The BFH has scheduled the oral hearing in these proceedings for 13 March 2024. Taxpayers who have filed protective claims in the past should monitor further developments and pursue pending refunds for the years in question.

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German tax court rules that the German dividend taxation of a Belgian life insurance company violates EU law

On 20 April 2023 the Cologne tax court (reference no. I R 53/23) ruled in favor of a Belgian life insurance company that the German withholding tax on dividends in the year 2009 was not in line with EU law and that wrongly levied taxes must be refunded.

In the relevant year, the Belgian life insurance company received portfolio dividends from several investments in German stock corporations. Similar to German life insurance companies, the Belgian life insurance company allocated the dividends to provisions for pension obligations that it had to pay in the future in its commercial balance sheet. All dividends were subject to German withholding tax. However, while German life insurance companies received a full deduction on their income in the amount of the pension obligations to be paid in the future and obtained a full credit or refund of the withholding tax in the German tax assessment procedure, the Belgian life insurance company could only reclaim two fifth of the withholding tax under the relevant German tax provision. The remaining amount was considered final. ▸

German court decisions

Following the judgment of the European Court of Justice (ECJ) in College Pension Plan of British Columbia (C-641/17), the Cologne tax court found that such less favorable treatment of the Belgian life insurance company restricts the free movement of capital (Art. 63 TFEU), which could not be justified by overriding reasons of the public interest. In this regard the court found it not to be decisive whether the Belgian life insurance company had recorded the provisions voluntarily or whether this was mandatory under Belgian law. Accordingly, the court granted the Belgian life insurance company a refund of the remaining three fifth of withholding tax.

The tax authorities have filed an appeal against the ruling of the Cologne tax court and the case is now under review of the German Federal Tax Court. In light of the decision of the Cologne tax court, non-German life insurance companies and pension funds should review their tax position for potential withholding tax refunds and consider filing withholding tax reclaims within the applicable timelines.

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German Federal Tax Court rules on prerequisites of cross-border loss recognition in Germany

In the decision dated 9 August 2023 in a case concerning cross-border loss recognition between a German parent and its French subsidiary, the German Federal Tax Court (BFH) had to conclude whether the parent company may seek such recognition based on the Freedom of Establishment of EU law. However, the question of the recognition of cross-border loss offsetting between companies by transferring the principles first established by the European Court of Justice (ECJ) in the Marks & Spencer ruling to the German tax group rules remains open after that decision. According to the BFH, this at least presupposes that the losses generated by the subsidiary have actually been borne by the parent company in accordance with national law, which was not given in the case at hand.

In the case, it was disputed whether the losses of the French subsidiary, which was dissolved in 2012, should be taken into account by the German parent company. The Schleswig-Holstein tax court denied the recognition of losses due to the lack of a domestic connection of the subsidiary and the absence of a binding agreement under the law of obligations between the subsidiary and parent company, which in any case had to include an obligation for the subsidiary to assume losses, similar to a profit and loss pooling agreement, which is a precondition for setting up a tax group in Germany (judgment of 13 March 2019, 1 K 218/15).

The decision in the first instance was now confirmed by the BFH in its ruling of 9 August 2023 (I R 26/19). The BFH states that cross-border loss offsetting requires at least the actual loss absorption by the domestic parent company (like in a tax group situation). The assumption of losses (only) at the time of finality of the losses in the year in dispute is not sufficient. The Court held that, in the absence of such a loss absorption, there was no basis for a Union law-based claim to recognize the final losses and thus there was no need to refer the case to the ECJ. The ECJ ruling in the Marks & Spencer case (dated 13 December 2005, C-446/03) does not indicate that the offsetting of losses could be possible without at least a de facto fiscal unity. Furthermore, the BFH held that an unconditional deductibility of final losses across the border neither arises from national law nor is it required under EU law. Thus, the BFH left open the question whether the final losses of the foreign subsidiary could, via an interpretation of Sec. 14 et seq. German Corporate Income Tax Act (KStG), waiving the requirement of a profit transfer agreement, be deductible in Germany. It further remains open to what extent the principles set out in the ECJ ruling of 22 September 2022 (C-538/20, W) on foreign permanent establishments would be applicable to the scenario of a foreign subsidiary with final losses. In the latter case the ECJ held as a general principle that taxpayers cannot demand on the basis of the Freedom of Establishment that final losses incurred in foreign permanent establishments to which the exemption method applies be recognized at the level of the head office.

Taxpayers seeking recognition of final losses incurred in an EU subsidiary can take from this decision that this is only potentially possible if the parent company has absorbed current losses of that subsidiary in the past 5 years before these losses became final. Only in that case would the BFH refer the case to the ECJ to provide guidance whether Germany would be obliged to recognize such final losses based on the EU law-based Freedom of Establishment.

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BFH decides on "majority of votes" criterion as precondition for income tax group integration

Under German (corporate) income tax law, a corporation can become a subsidiary in an income tax group if – among other conditions – the parent has held the majority of voting rights in the subsidiary since the beginning of its fiscal year (so-called "financial integration"). In a case recently decided by the Federal Tax Court (BFH, decision dated 9 August 2023, I R 50/20), the parent held 79.8% of the voting shares in a subsidiary GmbH. However, the GmbH's statutes – somewhat atypically - required a 91% majority for all shareholder decisions. Given that the shareholder's stake did not reach this threshold, the BFH concluded that the financial integration requirement was not met, as the majority shareholder could not effectively govern the affairs of the subsidiary, which would have been the intent of the law. The BFH left undecided whether a higher consent threshold only for specific decisions would have been harmful, although indicated that typical consent requirements for extraordinary matters, such as statute changes, should not impact the financial integration test.

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German Federal Tax Court decision concerning German principal and Bosnian toll manufacturer

On 9 August 2023, Germany's Federal Tax Court (BFH) dealt with an earlier decision of the Munich tax court dated 26 November 2019 (6 K 1918/16). This decision is important because the transactions under consideration are very common for many German taxpayers.

Specifically, the BFH confirmed or repealed decisions of the Munich tax court concerning the following aspects: The determination of profit mark-ups in cost-plus transactions, the attribution of locational advantages, and whether the transfer of a customer relationship qualifies as a business restructuring event.

Determination of cost-plus mark-ups
The Munich tax court considered the Bosnian affiliated manufacturer acting for a German principal as a toll manufacturer and concluded that a 10% profit mark-up is an arm's length remuneration for this function. This assessment was based on an analysis by tax examiners who researched industry publications. The examiners deemed this research necessary as the taxpayer had not provided any benchmarking analysis during the tax audit. However, the BFH dismissed this part of the Munich tax court ruling as the industry publications did not allow any conclusions whether the functional profile was comparable with that of the tested party.

The BFH confirmed the Munich tax court's decision concerning the 5% profit mark-up that the German entity charged to its Bosnian affiliate for procurement of materials, which the affiliate used in its own business relationships with third parties. The BFH decision indicates that possibly also a different value would have complied with the arm's length principle. However, the Munich tax court ruled in this regard without error and therefore, this point is not objectionable.

Attribution of locational advantages
The locational advantage resulted from the fact that the German principal was not able to conduct production in a profitable way. Due to lower labor costs, the toll manufacturer was able to earn profits. The resulting locational advantage has to be considered in arm's length transfer pricing. BFH, Munich tax court and tax examiners estimated the locational advantages by increasing the 10% profit mark-up for the locational advantage.

In this context the BFH confirmed the Munich tax court's approach to quantify the attribution of the location advantage on the basis of the facts and circumstances of the specific case. This finding is important because it contradicts a decision of the Münster tax court dated 16 March 2006 (8 K 2348/02 E) that had ruled to simply divide the advantages evenly between both parties.

German court decisions

Transfer of a customer relationship as a business restructuring event
The German taxpayer had transferred a client relationship to the Bosnian manufacturer, who then engaged in a direct business relationship with the client.

The Munich tax court decided that the transfer does not meet the definition of a business restructuring as defined by Sec. 1 Para. 2 Directive on business restructuring. The Munich tax court justified this assessment with the fact that competitive pressures led to the transfer, since the principal – unlike the toll manufacturer – was not able to earn profits from the client relationship. The BFH argues that this is irrelevant. Relevant for assessing a business restructuring is only whether a third party would have been willing to pay for the transfer of the client relationship. However, the BFH did not formally decide on whether a third party would have been willing to pay or not. According to the BFH this is not necessary as the client relationship under consideration does not meet the definition of a business function as required by Sec 1. Para. 3 Sentence 9 of the Directive. According to this legal definition, a function constitutes an organic part of a company. The BFH interprets "organic part" as meaning the taxpayer could have set up the production for the client as an independent part of the company. The BFH did not see any evidence supporting this view and returned this matter to the Munich tax court, which now has to assess whether a third party would have been willing to pay for the client relationship.

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Federal Tax Court comments on minimum shareholding with regard to application of exemption of income from corporations

In accordance with Sec. 8b (4) sentence 6 KStG (Corporate Income Tax Act), the acquisition of a shareholding of at least 10% is deemed to have taken place at the beginning of the calendar year, which is beneficial for the taxpayer. This is because the provision allows to apply the participation income exemption of Sec. 8b para. 1 KStG, even though the minimum participation of 10% is not actually present at the beginning of the calendar year. It was now disputed whether Sec.8b para. 4 sentence 6 KStG is also fulfilled if the acquirer acquires several participations in a company from several sellers and the minimum participation of 10% is only reached when the respective participations are combined. In the underlying case the acquirer acquired a shareholding of 5% from seller 1, a shareholding of 4% from seller 2 and a shareholding of 3% from seller 3. The Hessian tax court affirmed the application of Sec. 8b para. 4 sentence 6 KStG in the previous instance (decision dated 15 March 2021, case reference 6 K 1163/17) and thus contradicted the view of the tax authorities (Frankfurt/Main Higher Tax Authority of 2 December 2013, DB 2014, 329 f. and of 16 August 2021, DB 2021, 2255).

The Federal Tax Court (BFH) confirmed the legal opinion of the lower tax court in this specific case (BFH ruling dated 6 September 2023, case reference I R 16/21). However, the following aspect was important to the BFH for its decision: Sec. 8b para. 4 sentence 6 KStG only applies in such cases if, from the acquirer's perspective, there is a single economic acquisition transaction. In the underlying case the purchaser had acquired the shareholding on the basis of a uniform decision and through a uniform legal transaction under the law of obligations.

Taxpayers should thus be careful to ensure that several minor shareholdings are acquired through a single notarial deed.

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Foto: Bundesfinanzhof, Andreas Focke

BFH decides whether swap expenses qualify as interest expenses for the add-back rules for trade tax purposes

With its decision dated 16 November 2023, the German Federal Tax Court (BFH) resolved a long-standing controversy regarding the treatment of swap expenses in favor of the taxpayers.

In the case at hand, the BFH had to decide if swap expenses qualify as interest expenses in terms of the add-back rules for trade tax purposes.

The case comprised a variable-interest investment loan with a consortium of banks to fund wind farms, where at the same time, the taxpayer entered into swap agreements with some of these banks to hedge a certain loan amount against interest rate fluctuations. As a result of the tax audit for the years 2010 and 2011, the tax auditor concluded that any expenses from the hedging must be considered as interest expenses for trade tax purposes. Thus, 25% of the swap expenses would have been considered as add-backs for trade tax purposes with a permanent effect.

The taxpayer supported by EY objected to this conclusion and won the case at the tax court of first instance in Brandenburg. This decision has now been confirmed by the BFH.

In addition, according to the reasoning of the BFH, swap expenses can only be added back for trade tax purposes if the initial intention was to economically conclude a loan agreement with a fixed interest rate. This would lead to offsetting the hedge result with the variable interest rate but would, nevertheless, not allow to consider only expenses from the hedge result. The following three criteria were evaluated by the court to decide if swap and loan agreements can be treated as a combined agreement: 1) same contractual partner, 2) same contract period, 3) same contractual amount.

In the case at hand the syndicated loan amount exceeded the hedged amount, but looking at each single hedge agreement, the hedged amount exceeded the loan amount provided by the contracting bank. Furthermore, the contract periods differed significantly, and the contractual amounts developed independently over time. Against this background, the BFH concluded that the three criteria were not met and, correspondingly, expenses from the swap agreement could not be considered interest expenses for trade tax purposes.

For corporate income tax purposes there is currently a second case pending before the BFH, but the current decision is leading the way.

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Update on German exit tax: Legal classification of the "Wächtler" decision of the ECJ by the German BFH

German exit taxation presumes a sale of at least 1% of shares in a company if a taxpayer previously subject to an unlimited German tax liability for at least 7 years within the last 12 years gives up their residence. Following the entry into force of the ATAD Implementation Act, the previous option of permanently deferring the German exit tax without interest for relocations within the EU/EEA was abolished for relocations after 31 December 2021.

The current case refers to a relocation under the old legal framework to Switzerland, which is not part of the EU/EEA. In the "Wächtler" decision, the European Court of Justice (ECJ) had to decide whether the German exit tax in case of a relocation to Switzerland was contrary to the freedom of establishment guaranteed in the Agreement on the Free Movement of Persons between Switzerland and the EU dated 21 June 1999 (in the following: FMPA). In this regard, the ECJ ruled that the German exit tax in relation to Switzerland violated the freedom of establishment guaranteed in the FMPA and that any exit tax should therefore be deferred permanently and without interest.

The German Federal Tax Court (BFH) now stated that the principles of the ECJ ruling were clear and unambiguous. The Wächtler decision constituted a "binding snapshot" which had to be considered independently of the ECJ case law up to that point. The BFH thus issued a clear rejection of the defendant tax office and the Federal Ministry of Finance, which had intervened in the proceedings and had demanded a new submission of the case to the ECJ with reference to some of the older case law of the ECJ. However, it is also worth mentioning that the BFH dismissed the lower court's decision, which had gone beyond the "Wächtler" decision and argued that the German exit tax should not only be deferred permanently without interest, but that its assessment was already unlawful.

In view of the fact that the possibility of deferring the German exit tax on relocations within the EU on a permanent and interest-free basis ceased to exist as of 1 January 2022, the aforementioned principles of the judgment are of considerable importance and should also apply to relocations in the EU due to the comparability of the freedom of establishment under the FMPA to the freedom of establishment within the EU. However, it remains to be seen how the German tax authorities and the German legislator will react to the current decision of the BFH. Taxpayers who triggered the German exit tax as of 1 January 2022 by relocating within the EU should in any case request an interest-free and permanent deferral of the German exit tax with reference to the BFH case law. Also, taxpayers who relocated to Switzerland under the old legal framework should apply for a refund of taxes paid.

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Federal Tax Court on debt waiver of a claim acquired below nominal value in a partnership structure

The German Federal Tax Court (BFH) decision dated 16 November 2023 (IV R 28/20) addresses the tax implications of a shareholder's waiver of a profit-sharing right claim acquired below nominal value. The court determined that when such a claim is partly waived, a taxable gain occurs in the partnership's assets due to the reduced liability, which cannot be neutralized by a tax equalization item.

The case involved a limited partnership (GmbH & Co. KG) that was part of a group facing financial difficulties. To avoid insolvency, the shareholders acquired a profit-sharing right claim against the partnership at a price below its nominal value. Subsequently, the shareholders waived the claim in an amount of the difference between the nominal value and their acquisition costs. In the tax audit, the tax office treated this partial waiver as a gain at the level of the partnership due to a reduction of the partnership's liabilities and increased its taxable income accordingly. ▸

The plaintiff argued that under the principles of corresponding accounting, the tax value of the claim – which was treated as a special business asset of the shareholders and hence formed part of the combined tax balance sheets of the partnership – and the tax value of the debt should always be equal. In such case, the debt waiver would not have had an impact in the partnership's combined tax balance sheet. However, the BFH judgment clarifies that the principles of corresponding accounting do not apply if the acquisition costs are below the nominal value. Moreover, no tax equalization item can be formed to neutralize this income, as there is no rule in the tax code justifying such item.

Thus, the decision clarifies the tax treatment of debt waivers in partnerships, especially when claims are acquired below their nominal value and later waived. This issue applies similarly to debt waivers in corporate structures. Shareholders that acquired receivables against their company below nominal value should therefore carefully consider alternative structural measures in case of financial difficulties of the company, such as a debt assumption by another solvent creditor.

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First lower tax court cases on extraterritorial IP taxation pending

Since 2020, the German tax authorities' assumption of a German tax nexus for non-resident taxpayers through mere IP (patent or trademark) registrations in a German IP register has led to controversy, and significant assessments have been issued against foreign groups in several instances. Since late 2023, the first case is now pending in front of the Cologne and Munich tax courts. The case only deals with German royalty withholding tax, and not with a transaction that could be subject to capital gains tax. The courts' views will be of particular interest for all open extraterritorial IP taxation cases, as the courts may provide legal assessments on disputed topics such as:

- The constitutionality of the extraterritorial tax regime;
- Its compliance with German obligations under the US-Germany Friendship Treaty and/or the bilateral double tax agreement;
- European law, notably a potential infringement of the Freedom of Services;
- The intent of the law;
- A potential expiration of the statute of limitation;
- The legality of the top-down estimation method used by the tax authorities to allocate tax basis to Germany.

Whatever the outcome of the court judgments will be, it can be expected that the case will be further appealed to the highest German tax court (BFH), and possibly further to the Constitutional Court or the European Court of Justice.

Taxpayers still at the appeals stage may potentially request and obtain a stay of proceedings pending the court cases' resolution; the pros and cons of this approach should be discussed on a case-by-case basis.

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Tax court of Cologne grants treaty based withholding tax relief based on motive test

Under the revised German anti-treaty shopping rule, which was enacted in June 2021 and which applies to all open cases, a taxpayer may show that none of the main objectives to implement the holding company were of a tax nature. In a recently published decision, the tax court of Cologne applied the motive test in favor of a taxpayer in a case concerning convertible bonds. The case has been pending before the courts for quite some time. The question whether the remuneration on convertible bonds was subject to German withholding tax at all had been the question of preceding court proceedings and had been answered to the affirmative by the Federal Tax Court (BFH). The BFH then referred the case back to the tax court of Cologne to gather more facts to be able to decide on the treaty eligibility of the recipient of the payments.

This is what was now done before the tax court of Cologne and the court upheld the treaty eligibility of the Cyprus resident recipient of the payments. The court left the personal and factual eligibility for treaty benefits open and focussed on the motive test. In its decision, the tax court mainly based its arguments on the fact that the entity was not a pass-through entity, i.e. the taxpayer could demonstrate that the payments received by the Cyprus resident holding company were in fact reinvested in the group. Moreover, the court also argued that outsourcing of management to a related party in the same country (Cyprus) as well as the fact that the immediate parent companies were resident in Liberia and other entities in the group were resident in Panama and Bermuda was not considered harmful because – especially in the shipping industry – these organization structures are common and used for valid economic reasons other than tax reasons. Concluding that none of the main objectives of the interposition were of a tax nature, the tax court of Cologne argued that treaty entitlement should be granted. The tax court considered the case sufficiently clear and denied an appeal before the BFH. The tax authorities did not accept this and the question whether the decision can be appealed is now pending before the BFH (I B 31/23).

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Bremen tax court case highlights complexities in using partnership holding companies

In a landmark decision, the Federal Tax Court (BFH) had held in 2017 (decision dated 29 November 2017, I R 58/15) that shares in a (German) corporation held by a German limited partnership (GmbH & Co. KG) with foreign limited partners could be allocated either to the (deemed) permanent establishment created for the foreign partners in Germany by virtue of their KG investment, or to their home country permanent establishment, depending on the answer to the question to which permanent establishment there was a stronger functional connection. The allocation matters for the German tax burden, as only in the case where the shares in the subsidiary corporation are allocable to a German permanent establishment, an income tax group could be established or dividend withholding tax that arises on distributions could be fully refunded or credited. The BFH had referred the 2017 case back to the lower tax court of Bremen at the time to assess whether in the facts of the given case, there was a stronger link between the German GmbH subsidiary and the German KG permanent establishment or the (in the case Chilean) limited partner corporations. The Bremen court's findings have now been published (decision dated 29 April 2021, 1 K 111/18), and are interesting, as they shed light on the criteria to test regarding the functional allocation of shares in similar cases. In the case, the court decided to allocate the shares in the indirectly (through the KG) held German GmbH to the foreign (Chilean) permanent establishment of the KG's limited partners, thereby denying a dividend withholding tax refund or credit. A decisive factor for the court's decision was that the majority partner in the KG was an active trading entity in Chile, which exercised strategic leadership over several entities, and was in the position to control the KG and thus indirectly the German subsidiary GmbH. The KG itself neither had an own trading activity, nor could it demonstrate an active own management role. The case, however, leaves open whether the share allocation could have occurred differently, had the limited partner entities been mere holding companies, as will often be the case in other investment structures. In any event, any foreign investor contemplating using a German KG structure to hold German corporate investments is well advised to take the new case law into account in the design of the structure, so that the benefits of such holding structures and in particular the potential to repatriate German profits free from German withholding tax can indeed be achieved.

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New reporting obligations for German listed companies from 2025

Over the course of the last ten years, legislators and international organizations have been quite active in terms of developing and implementing reporting obligations for companies with regard to tax relevant data. Examples include FATCA, CRS (DAC2), CbCR (DAC4), UBO Registers (DAC5), MDR (DAC6), and DAC7, just to name a few.

Starting from 2025, German listed companies will now be under scrutiny. In essence, domestic listed companies will be required to report certain information about their shareholders to the German Federal Central Tax Office (BZSt) as of the date of the dividend resolution.

For this purpose, listed companies will need to compile certain data, including, but not limited to name and address of the single shareholder, the number of shares held by the shareholder, as well as the beginning date of the shareholding.

The listed companies need to request this information from central securities depositories (basically Clearstream) or other intermediaries within the intermediary chain (e.g. custodial institutions). This information request is based on the Shareholder Rights Directive II (EU) 2017/828, which was transposed into German law in 2020. The process will be standardized to allow interoperability and fully automated processing.

Once the data has been received from the intermediaries, the listed company needs to prepare the data for the electronic transmission to the BZSt in an XML format via the mass data interface "ELMA" without undue delay.

Companies falling under the scope of the new law must inform their shareholders about the data being disclosed. In addition, special data recording and retention regulations apply.

The new obligation will first apply to dividends that are distributed after 31 December 2024. Hence, in practice, the law will in most cases start affecting listed companies from their 2025 annual general meeting onwards.

Domestic listed companies should therefore quickly start to develop a strategy and processes for requesting, processing, reporting and storing the necessary data and for ensuring the required information about the reporting to the shareholders. In addition, the IT technical requirements have to be met.

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Bumpy start for DAC7 reporting

With the first reporting period – namely the year 2023 – in the books, the actual submission of DAC7 reports became reality in the first quarter of 2024. Operators of digital platforms, starting from 2023, are facing several obligations. The rules go back to the penultimate amendment of the EU Directive 2011/16/EU on improving administrative cooperation in the field of taxation, the so-called DAC7. In Germany the rules were implemented through the Platform Tax Transparency Act.

In essence, operators of platforms facilitating legal contracts with the contents of the sale of goods, rental of property, or rental of any mode of transport or personal services need to collect data of the respective sellers or service providers. In addition to personal and tax data such as the address and the tax identification number, this also includes the consideration generated via the platform. This data must be reported to the local competent tax authority. Then, through an EU-wide information exchange, the data is made available to the competent tax authority for each single provider of a listed service. With that, the EU intends to prevent tax fraud, tax evasion and tax avoidance. Other jurisdictions already follow this approach. Further jurisdictions are likely to also participate in this kind of international information exchange.

With the reports of the calendar year 2023 in general due on 31 January 2024, all platform operators had to submit their reports to their competent tax authorities. This submission, which needs to comply with the requirements of the XML-schema, caused major (technical) problems in most EU Member States. To our knowledge, nine Member States therefore granted an extension on the submission by a couple of days or even by a couple of months depending on the Member State. Technically, Germany did not extend the deadline, but published a non-objection to late filing of certain reports and notifications prescribed in DAC7. Several tax authorities have communicated technical problems which make the actual submission difficult.

Next to the DAC7 reporting requirements stand the reporting requirements for payment service providers. These service providers will be required to provide information on cross-border payments from Member States and on the beneficiary ("payee") of these cross-border payments per quarter. Also in this context, the German authorities issued a non-objection to filings until 31 July 2024.

For more information, please refer to our *EY Global Tax Alert dated 19 January 2024.*

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CBAM – Have you already filed your first report?

The European Union's Carbon Border Adjustment Mechanism (CBAM) is introduced to establish a fair price for greenhouse gas emissions emitted during the manufacturing of certain carbon-intensive goods entering the EU. The logic behind it is to achieve a competitive level playing field in terms of carbon pricing for these goods in the EU economic zone as EU established manufacturers have to pay for greenhouse gas emissions through the purchase of carbon certificates under the EU Emissions Trading System (EU-ETS), too. Both systems, EU-ETS and CBAM, are not fully congruent but aim for similar treatment, which shall serve the EU Commission as a key argument in expected discussions about the nature and legality of the measure at the level of the World Trade Organization.

CBAM currently applies to a wide range of imported products in the categories of cement, iron and steel, aluminum, fertilizers, electricity, and hydrogen. In total, CBAM currently affects the import of goods covered in 749 tariff lines of the EU's Combined Nomenclature (the customs tariff).

CBAM in its "transitional phase" was appliable first from 1 October 2023, requiring the importers of CBAM goods to take and organize records and come up with the first CBAM report on 31 January 2024 to report on a quarterly basis the embedded emissions stemming from goods imported in Q4/2023. After the authorities opened the possibility for importers to register in the CBAM portal, and other governmental portals authenticated users late and also taking account for a number of issues with the CBAM portal itself, the authorities offered a late filing opportunity of 30 days upon application, an extension which ended on 1 March 2024. ▸

EU law

Based on media reports, however, only a very small portion of CBAM reportable businesses have actually fulfilled their new obligation so far. The president of the German national CBAM authority informed that by 31 January 2024 only about 10% of businesses had filed the report, the Swedish authorities stated a number of about 11%. The customs authorities in Finland quoted that by the end of February about 30% of Finish businesses had reported. In short: Many businesses are still in the process of establishing their CBAM reporting or have not realized that they have to report.

It is to be noted that the first CBAM reports are fairly simple as importers are allowed to use so-called emission standard values for the emission calculations. Also, many operators have filed incomplete reports, just to meet the filing deadlines. Given the need for extensive data which is to be collected from suppliers, basically all operators will have to file supplementary, i.e. corrective reports by 31 July 2024 at the very latest. From then, it will also be necessary to report a much more extensive data set, which makes the process much more burdensome for importers. In any case, importers have to start collecting information from suppliers, respectively the manufacturing installations, right now. While this is a challenging task that involves a structured process with the procurement department and information of the suppliers about the new requirements, many non-EU manufacturers are overwhelmed with the new requirement to calculate emissions in accordance with the new EU methodology. Hence, most of the time there is also a practical requirement for knowledge transfer and supplier enablement (e.g. provision of guidance, workshops and so on).

To manage the resources and the workflow burden of CBAM, there are a number of structuring and optimization possibilities available. The possibilities range from a more central reporting approach, to the possibly of outsourcing, changes to the customs import setup or changes in procurement itself. EY has gained significant practical experience in CBAM projects with more than 150 clients in the past months and can provide effective advisory and operational assistance support.

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Update on the European Company (Societas Europea, SE)

The SE was introduced in 2001 to enable companies throughout the EU to form a legal entity with national branches and to promote the European single market. Over 4,000 companies have opted for the SE to date, including well-known names such as Allianz, BASF, SAP, and Siemens.

According to the provisions of the applying SE Directive (Council Directive 2001/86/EC of 8 October 2001), negotiations on employee participation procedures must be conducted prior to the formation of an SE. A case before the European Court of Justice (ECJ) now concerns the question of whether such an employee participation procedure must be caught up on if the SE was initially founded by companies without employees and later takes control of subsidiaries with employees. In his opinion dated 7 December 2023, the Advocate General of the ECJ, Mr. Jean Richard de La Tour, made a fundamental statement regarding this obligation. He argues against the need to catch up on the employee participation procedure and argues that the applying SE Directive does not provide for such an explicit obligation. This follows from the compromise on the before-and-after principle. The before-and-after principle states that the status quo of co-determination of a company to be converted into an SE is maintained even after the change of legal form. This applies regardless of whether the SE may subsequently exceed the number of employees relevant for co-determination. The previous status quo is therefore "frozen". If the company was not co-determined before the change of legal form to an SE, it will not be co-determined afterwards either. The Advocate General states that only in exceptional cases and in cases of abuse would it be possible to make up for the employee participation procedure. This would mean that the employee participation procedure would only have to be repeated in these (abusive) cases. However, it remains to be seen whether the ECJ will follow the Advocate General's recommendations. His opinion is not binding. Nevertheless, the ECJ's judges are often guided by it.

It is also unclear whether the ECJ ruling will then also apply to shelf SEs. In this case, there is the particularity that various formation regulations must be applied again when a shelf SE is capitalized. If it then gains employees or employees are brought in via subsidiaries, this could possibly be treated as a new formation, which in turn would generally lead to an employee participation procedure.

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State Labor Court rules that burden of proof for overtime worked still lies with the employee

In the case, a former employee claimed compensation for overtime arising from a terminated employment relationship. The State Labor Court (LAG) Hamm ruled in its judgment of 24 May 2023 (case reference 9 Sa 1231/22) that the plaintiff had not provided sufficient information on specific hours worked beyond the normal working hours.

In principle, a so-called graduated burden of proof applies to the assertion of overtime claims, i.e. the employee must first specifically present their overtime hours. The employer must then respond to this and explain in detail what work had been assigned to the employee. If the employer does not submit anything or does not provide any substantiated information, the working hours submitted by the employee are deemed to be admitted. If, on the other hand, the employer makes a substantiated submission, the burden of proof lies with the employee, who has to provide conclusive evidence regarding the overtime worked.

In the present case, the defendant substantiated the claim by submitting the monthly journals from the electronic time recording system. These showed that the plaintiff had only worked a total of 165.25 hours of overtime and not the 299.5 hours of overtime claimed by the plaintiff. The defendant also submitted that an error was made on its part, in particular by a responsible employee, which resulted in an overtime balance of 299.5 hours being incorrectly transferred to an Excel spreadsheet. However, this additional submission was not relevant for the decision.

The basis of a claim for remuneration is always only the hours actually worked by the plaintiff. Previous errors in the calculation and payment of overtime do not affect any aspect relevant to the decision. The plaintiff had the opportunity to counter the defendant's submission and to state specifically on which days he had worked beyond the scope shown in the monthly journals of the electronic time recording system. However, he failed to do so. Therefore, the plaintiff was not entitled to higher overtime pay.

This decision shows that the burden of proof for overtime worked still lies with the employee. This also applies if there is an electronic time recording system in the employer's company and also if errors occur when using this system.

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