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Negotiations for a new German government coalition started

Business tax reform included in the negotiations

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After the federal elections held on 23 February 2025, the conservative CDU/CSU parties and the Social Democrats (SPD) have started negotiations on forming a coalition. First results include a massive increase in public spending on defense and infrastructure and the announcement of tax reliefs.

While detailed talks on the tax policy agenda of the planned coalition are about to begin, a first paper released by the negotiators on 8 March 2025 already contains concrete tax-related plans. Most importantly, the parties announced that they will enter into a business tax reform during the legislative term. Such a reform would, if guided by the Conservatives' election manifesto, contain a 5% corporate income tax (CIT) rate reduction to reduce the combined tax rate of CIT and the local trade tax to 25% (on average). However, it is likely that such a tax cut would be implemented in several steps to reduce negative effects on tax revenues. In addition, and immediately after forming the government, the upcoming coalition intends to introduce new incentives for investments in Germany. Such incentives could be developed based on the Social Democrats' proposal for a 10% "made in Germany" tax credit on any kind of equipment investment. ▶

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Negotiations for a new German government coalition started

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Details of the final coalition agreement, which is expected to be available by the end of April, are eagerly awaited. First steps to implement agreed tax measures could be initiated before summer. However, a significantly delayed negotiation process is also possible, with the final agreement being postponed to May or even June.

Any business tax reform to be implemented by the new Government could – in addition to major cornerstones agreed by the coalition – contain measures as proposed by two expert commissions that published their reform proposals last summer. Established by the former Finance Minister Christian Lindner, both commissions consisted of reputable academics and leading German tax directors. The final reports of the commissions were well received in the professional community and shaped the tax policy discussion in the second half of 2024, before the old coalition fell apart.

The reform proposals included, among other things: a reduction and simplification of reporting and documentation obligations, the elimination of the 5% inclusion of dividend payments and capital gains for corporate shareholders, the improvement of the crediting of foreign taxes, better tax conditions for conversions and restructurings, the removal of double regulations under anti-hybrid rules, and a relaxation of the interest barrier.

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Conservative German state finance ministers and German business associations call for suspension of minimum tax

On 6 March 2025, a joint statement of 6 conservative CDU/CSU German state finance ministers (including ministers of the major states Bavaria, North Rhine-Westphalia and Hesse) was released, in which the ministers call for a suspension of the global minimum tax.

In their statement, the CDU/CSU finance ministers advocate suspending the agreed minimum taxation for companies until an internationally agreed solution is found. According to North Rhine-Westphalia's Finance Minister Marcus Optendrenk (CDU) "a global minimum tax is only fair and functional if it is adhered to globally." The finance ministers agree that the fundamental idea of a global minimum taxation to prevent profit shifting and harmful tax competition is still correct. However, the economic reality must also be acknowledged. In their statement the ministers underline that German companies are in international competition, and a minimum tax without the participation of the USA, China, and India represents a competitive disadvantage for the EU.

To achieve their goal, the finance ministers call for a new political initiative – at least at the European level – with Germany as the driving force. Whether the German Federal Minister of Finance, who is responsible for any talks on EU or OECD level, will take up the initiative depends on the outcome of the federal coalition negotiations between the CDU/CSU and the Social Democrats (SPD), which have just started. It is expected that a new federal government will be formed not before May 2025.

In parallel, a group of 8 leading German business associations approached the EU Commission with similar demands. In a *letter to the Directorate-General for Taxation dated 3 March 2025*, the German top associations advocate for direct negotiations between the EU and the USA to avoid US retaliatory measures against the minimum tax. As a first step, the application of the minimum tax should be suspended. In their statement, the associations also make several proposals to simplify EU tax law (e.g., the ATAD or the DAC).

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BMF publishes final version of the updated decree on German reorganization tax

The Federal Ministry of Finance (BMF) has published the final version of its updated decree on the German reorganization tax law, replacing the previous version from 2011. This new decree incorporates legislative changes and case law developments over the past 13 years. While it primarily includes updates and adjustments rather than major reforms, it addresses some concerns raised by associations during the draft phase.

One significant change is the removal of the requirement that involved entities must be EU/EEA entities for various types of tax-neutral reorganizations, allowing third-country entities to fall within the scope of the Reorganization Tax Act (RTA) for tax transfer dates after 31 December 2021. The decree maintains the need for strict comparability between foreign and domestic reorganizations for them to be considered under the RTA. A few minor reliefs are provided, nonetheless. For example, the tax authorities had previously held the view that the foreign merger had to take place under the legal principle of universal succession ("by act of law") to be comparable to a domestic merger. This is now no longer required.

The decree also clarifies several aspects of mergers, spin-offs, and contributions. For mergers, it states that shares of the transferring entity in the acquiring entity are considered part of the transferred assets. For spin-offs, it specifies that assets used by multiple business units should be allocated to the unit where they are predominantly used. Additionally, disproportionate spin-offs, where a shareholder does not receive shares in the acquiring entity, are included within the scope of the RTA. Further, with regards to Sec. 13 RTA (taxation of the shareholders of the transferring entity), the tax authority has deviated from its view that a tax-neutral exchange of shares is excluded in the case of a value shift between the involved shareholders. According to the new decree, a tax-neutral exchange is possible both in proportionate and disproportionate reorganizations (consequences regarding gift tax, withdrawals, hidden profit distributions/contributions must still be examined).

Further adjustments pertain to the post-spin-off-disposal-restriction rule, i.e. the provision that denies the tax neutrality for spin-offs that are deemed to be "in preparation of a disposal", with the tax authorities closely adhering to the wording of the (new) law (Sec. 15 para. 2 RTA) and the explanatory memorandum. However, some clarifications requested in practice were not included.

Regarding contributions, the decree clarifies that partnership interests are the subject of contributions when changing legal form from a partnership to a corporation. It also addresses tax retroactivity and valuation options, ensuring that withdrawals and contributions during the retroactive period are considered.

The decree introduces extensive changes for tax groups, aligning with the Federal Tax Court's 2023 decisions. It broadens the impact of the "following in the predecessor's footsteps" principle (Fußstapfentheorie) and aligns with the court's perspective on financial integration and the allocation of stakes in controlled companies.

The updated decree applies to all pending cases and replaces the 2011 decree. If the legal situation has significantly changed between the taxable event and the publication date of the final decree, the new decree applies only if it does not contradict the relevant legal situation in individual cases.

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German BMF issues updated Administrative Principles 2024 on transfer pricing, including final guidance on new rules for intercompany financing

In 2024, the German legislature introduced new regulations on intra-group financing relationships and financing services, particularly new limitations on deductible interest expenses on intercompany financing. Since then, several questions concerning the practical application of the newly introduced rules regarding intercompany financing have remained unanswered. Therefore, on 12 December 2024, the German Ministry of Finance (BMF) issued updated Administrative Principles 2024 on transfer pricing. Taxpayers with intercompany financing transactions involving Germany should carefully review whether the rules and their interpretation by the BMF could affect their current financing.

Furthermore, the guidance also comments on the application of Amount B of the OECD/Inclusive Framework's Pillar I project in Germany. Accordingly, the guidance clarifies that for in-scope transactions of Amount B, the transfer price can be determined according to the simplified and streamlined approach. However, this only applies to transactions with certain jurisdictions.

For more detailed information, please refer to the *EY Global Tax Alert dated 23 January 2025*.

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New BMF circular on VAT treatment of fuel deliveries within fuel card systems

On 21 January 2025, the German Federal Ministry of Finance (BMF) issued a new circular with respect to fuel deliveries within fuel card systems.

Within fuel card systems, vehicle users are provided with a fuel card that allows them to refuel the vehicle. In such transactions, for VAT purposes, regularly a chain transaction is assumed: The fuel card issuer purchases the fuel from the fuel supplier and subsequently sells it to the fuel card holder.

The VAT treatment was often adopted under consideration of the criteria set out by a BMF circular issued 20 years ago for cases of fuel deliveries in the vehicle leasing sector (BMF circular dated 15 June 2004). This circular distinguishes between two potential VAT treatments based on the contractual conditions between the lessor and lessee. It is either a chain transaction with two deliveries (one between the oil company and the lessor, and another between the lessor and the lessee) or it is a direct fuel delivery from the oil company to the lessee, accompanied by a financing service between the lessor and lessee.

However, in 2019, the ruling of the European Court of Justice (ECJ) in the case "Vega International Car Transport and Logistic" (C-235/18) led to a huge uncertainty whether the regularly applied VAT treatment as a chain transaction is still valid. One crucial point was how it can be proven that the fuel card issuer receives the power of disposition over the fuel.

With the recently issued circular the BMF provides clarity and explicitly expands the principles and criteria outlined in the 2004 BMF circular to all fuel card systems in Germany.

This circular applies to all open cases. We recommend reviewing the actual contracts with respect to the criteria set out in the BMF circular issued in 2004. To the extent fuel cards can also be used outside Germany the VAT implications in the respective countries need to be considered. The new BMF circular does not explicitly encompass systems in which electricity for electric vehicles is purchased. However, in the ECJ case "Digital Charging Solutions GmbH" (C-60/23) the ECJ supports under certain conditions the view that a chain transaction can be assumed.

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German tax authorities

Germany issues final guidance on ATAD-based anti-hybrid rules

On 5 December 2024, the German Ministry of Finance (BMF) published the long-awaited final decree regarding the application of the German anti-hybrid rules. While the draft decree issued in July 2023 did not provide detailed practical guidance and mostly covered basic structures, the final version clarifies a couple of open questions in terms of the relevance of a controlled foreign corporation (CFC) regime and the application of the dual-inclusion exemption. More details can be found in our *EY Global Tax Alert dated 16 December 2024, "German Federal Ministry of Finance publishes final decree regarding the application of anti-hybrid rules"*.

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German court decisions

Cross-border change of legal form from third countries: current case law and practice

There are cases in which a foreign company shall be relocated to Germany while retaining its legal identity. The cross-border change of legal form from EU/EEA countries under preservation of legal identity is largely harmonized (Secs. 333 et seqq. of the German Transformation Act, UmwG).

According to Sec. 333 para. 1 UmwG, a cross-border change of legal form from or to third countries located outside EU or EEA (e.g. Switzerland) is not regulated, as the law is only applicable to companies founded under the law of EU/EEA states. An identity-preserving cross-border change of legal form from third countries to Germany can therefore not be implemented with legal certainty using the existing legal options of the UmwG. However, there are various approaches for achieving such a transformation by adding further (intermediate) steps.

A common method is the two-stage approach with (1) intermediate conversion via an EU/EEA state and (2) subsequent cross-border change of legal form to Germany. The two-stage approach requires for the foreign company to first relocate its registered office to an EU/EEA state that allows cross-border immigration from third countries (e.g. Liechtenstein, Luxembourg). In a second step, the relocation to Germany will then take place based on the then applicable and harmonized German transformation law. The admissibility of this approach is not entirely uncontroversial and has not been clarified by the Federal Court of Justice (BGH) so far. However, the Higher Regional Court of Karlsruhe (OLG) clarified in its decision of 24 April 2024 (case reference 1 W 40/23 (Wx)), that the possibility of a company changing its legal form cross-border to Germany in this two-stage approach depends solely on whether the company is treated under the law of the intermediate state like a company originally founded there. Hence, it should not be decisive that the actual original foundation of the company took place in an EU/ EEA state. Due to the aforementioned legal uncertainty, cross-border mergers into a newly founded company established under the laws of the intermediate state were often carried out as a first step to ensure that the company changing its legal form to a German corporate form in the second step was originally founded in an EU /EEA member state. The above decision of the Higher Regional Court of Karlsruhe could eliminate such need for a cross-border merger as an interim step instead of a cross-border change of legal form.

In view of the decision of the OLG Karlsruhe, the two-stage approach – even if associated with higher administrative effort – is likely to continue to be the practical solution for realizing an identity-preserving cross-border change of legal form from third countries to Germany. Nevertheless, cross-border changes of legal form from third countries directly to Germany under the UmwG can currently still not be implemented with legal certainty from a corporate law perspective. In cases of doubt, the legal requirements and single steps should be clarified and closely coordinated in advance with the competent German registry court until uniform case law or clarification by BGH has been established.

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BFH confirms that loss carryback in the retroactive period of a merger is not permitted

From a German tax perspective, a merger can be carried out with retroactive effect of up to 8 months. According to section 2 para. 4 sentence 3 Reorganization Tax Act (UmwStG), the offsetting of positive income of the transferring legal entity in the retroactive period with offsettable losses, remaining losses carried forward, and uncompensated negative income of the absorbing entity is not permitted.

The Federal Tax Court (BFH) had to decide in the event of a merger of a profit-making company with a loss-making company whether it is possible to offset profits of the transferring legal entity (profit-making company) during the retroactive period with a loss carryback of losses incurred in the year following the merger.

The dispute was whether the acquiring legal entity (which emerged from the merger) could be refused a corporate income tax loss carryback of losses incurred exclusively in the year following the merger back to the assessment year of the merger with reference to section 2 (4) sentence 3 UmwStG.

According to this section, the offsetting of positive income of the transferring legal entity in the retroactive period with offsettable losses, remaining losses carried forward, and uncompensated negative income is not permitted. It was undisputed that the losses of the loss-making company existing in the retroactive period may not be offset against the taxable income of the profit-making company existing at that time.

In its ruling of 13 March 2024 (case reference: X R 32/21), the BFH decided that such a loss carryback is also covered by the offsetting prohibition of section 2 (4) sentence 3 UmwStG. The standard is specifically aimed at preventing any offsetting of losses against the positive income of the transferring company generated in the retroactive period and ensuring that the company is finally taxed.

The BFH also states that a loss carryforward remains possible under section 10d(2) of the German Income Tax Act (EStG). The regulation of section 2(4) sentence 6 UmwStG should also not be overlooked in this context. Accordingly, the disputed restriction on loss offsetting does not apply if the transferring and acquiring legal entities are affiliated companies within the meaning of section 271(2) of the German Commercial Code (HGB) before the expiry of the tax transfer date. Since the lower court had not yet examined the conditions of this group clause, the BFH referred the case back to the tax court.

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Case law update on German real estate transfer tax rules for share deals

The Federal Tax Court and lower tax courts have lately published several decisions in which they clarify their view on the application of the German real estate transfer tax (RETT) rules for share deals. In simplified terms, Germany applies two different tests as to whether RETT is triggered:

- Unification of shares rules: Irrespective of the percentage of shares being transferred, RETT is triggered if an acquiror for the first time unifies 90% or more of the shares in a real estate holding company (directly and/or indirectly). The RETT triggering event is the signing of the SPA.

- Transfer of shares rules: Irrespective of the percentage a single acquiror holds, RETT is triggered if 90% or more of the shares in a real estate holding company are transferred within 10 years (directly and/or indirectly). The RETT triggering event is the closing of the SPA.

Both rules apply to the acquisition or transfer of partnership interest accordingly.

With respect to these rules, the most important recent decisions are:

- Federal Tax Court decision dated 21 August 2024: When applying the transfer of shares rules, interposing or eliminating a partnership at the indirect level is disregarded to the extent that the partners behind the partnership remain the same (economic view).

- Lower tax court of Baden-Wuerttemberg decision dated 26 April 2024: In contrast, the interposition or elimination of a partnership or company as the direct shareholder always needs to be considered for the calculation of the 90% (strictly legal view).

- Lower tax court of Hesse decision dated 16 January 2024: If the economic ownership in shares is acquired prior to the legal ownership (even if based on the same SPA), RETT under the transfer of shares rules may be triggered twice.

- Lower tax court of Baden-Wuerttemberg decision dated 26 April 2024: If an asset purchase agreement is signed in the interim phase between signing and closing, RETT is triggered on the closing date (i.e. effectively twice due to the APA signing and the SPA closing).

- Lower tax court of Muenster decision dated 16 January 2025: When applying the transfer of shares rules to property owning partnerships, the historic view was that the 90% were calculated on a per capita basis. Therefore, even if the economic share between two partners was 100% vs. 0%, no unification of shares would have been assumed. Based on an obiter dictum in a Federal Tax Court ruling, the lower tax court of Muenster has decided that the economic share is decisive.

- Lower tax court of Münster decision dated 16 January 2025: For share deals until 5 December 2024, a property shall be attributed exclusively to the parent company with the SPA signing if such parent unifies 90% or more of the shares. Consequently, the acquired subsidiary would no longer be deemed to be property holding on the subsequent closing, resulting in the transfer of shares rules being non-applicable.

It should be noted that appeals against almost all the lower tax court decisions have been filed so that the cases will be finally decided before the Federal Tax Court.

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BFH clarifies valuation of shares in non-listed companies for tax purposes

When valuing shares in non-listed companies for tax purposes, the net asset value (Substanzwert) is generally considered as the minimum value of the company. It was previously unclear whether this minimum value also applies when the value of the shares is derived from sales to third parties. According to the tax authorities, the net asset value should be considered the minimum value in this case as well. However, the German Federal Tax Court (BFH) has now clarified in two decisions (II R 15/21, II R 49/22) that the net asset value does not always represent the minimum value of the company. Instead, the BFH concluded that the net asset value can be lower if the alternative value is determined through contemporaneous sale transactions with third parties.

For the value of the company to be based on sales to third parties, certain conditions must be met. Such a sale must occur at a price that is achieved in ordinary business transactions. This price must be based on market principles of supply and demand, considering individual circumstances. Additionally, the parties involved must be acting voluntarily and in their own interest.

In the cases reviewed, however, these conditions were not met. In one decision (II R 15/21), the BFH found that, given the overall circumstances, no proper price formation took place because the same price based on the nominal value had been consistently used for the shares over the years. Changes in the financial situation of the company and its subsidiaries were ignored.

The second decision (II R 49/22) involved a family holding company, whose articles of association contained specific provisions regarding the sale of shares. For example, the sale of shares required the approval from individual shareholders, and a brokerage had to offer the shares to other family members in a predetermined order. Under these conditions, the BFH concluded that a sale in ordinary business transactions could not be assumed, as the contracting parties could not act freely and in their own interest. Furthermore, a constant holding discount of 20% had been applied to the share price over several years. The BFH stated that such a constant holding discount is not usually seen in ordinary business transactions. Actual changes in the holding discount would have been necessary to adequately reflect the specific facts and circumstances.

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BFH refers questions to the ECJ for a preliminary ruling on the determination of the customs value

The German Federal Tax Court (BFH) has referred important customs law questions to the European Court of Justice (ECJ) for clarification. The focus is primarily on the determination of costs and their impact on the customs value of goods. The answers to these questions are likely to be of significant practical relevance for importers.

In a decision dated 17 September 2024 (VII R 28/21), the BFH submitted four questions to the ECJ for clarification (preliminary ruling) regarding the customs valuation treatment of printing templates for containers, contributions, as well as purchasing commissions related to contributions and the customs value of goods assemblies (Hauptzollamt A, T-28/25). Specifically, the BFH seeks clarification on the following points:

1. Printing templates (Article 71(1)(a)(ii) and (b)(iv) UCC)
Should the value of printing templates created within the EU and provided free of charge to manufacturers in third countries be added to the customs value of the goods? A distinction is made as to whether these costs are to be considered part of the cost of packing or as a so-called "engineering, development, artwork, design work, and plans and sketches" as defined in Article 71(1)(b)(iv) UCC. Intellectual services are only to be added according to Article 71(1)(b)(iv) UCC if they were provided outside the EU.

2. Materials and services (Article 71(1)(b)(i) UCC)
Are intangible components incorporated into the imported goods for the production of supplied materials (e.g., decals) also included in the value of these materials and do they thus increase the customs value of the goods?

3. Purchasing commissions (Article 71(1)(b)(i) UCC)
Are commissions paid for the purchase of supplied materials to be included in the customs value even if they do not directly relate to the imported goods?

4. Goods assemblies (Article 71(1)(a)(ii) UCC)
Are cork coasters and gift boxes to be classified as "contributions" according to Article 71(1)(b)(i) UCC or as "containers" in the meaning of Article 71(1)(a)(ii) UCC, and must they be treated as being one, for customs purposes, with the goods in question (porcelain mugs)?

In the specific case, the applicant imported porcelain mugs, cork coasters, and gift boxes from China. The designs for these were created in Germany and sent free of charge as PDF files to suppliers in Taiwan and Hong Kong. These suppliers produced the decals, cork coasters, and boxes and sent them to the manufacturers of the porcelain mugs in China. The applicant paid licensing fees for the designs but did not declare these in the customs declaration. The German Customs Authorities demand that the licensing fees and purchasing commissions be included in the customs value.

In essence, the BFH wants the ECJ to clarify how the provisions of Article 71(1)(a) and (b) UCC should be interpreted, particularly regarding the distinction between costs of containers and intellectual services, the consideration of services provided within the EU and the inclusion of purchasing commissions in the customs value.

The outcome is crucial for the calculation of the customs value and thus for the amount of import duties. In particular, the first point is likely to have significant practical relevance for many other importers.

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BFH allows the recognition of higher pension provisions for employer-financed securities-linked pension commitments

The recognition of pension provisions in the German tax balance sheet is particularly regulated and restricted by Sec. 6a German Income Tax Act (EStG). This provision also covers securities-linked pension commitments (wertpapiergebundene Pensionszusagen) where the benefits promised by the employer depend in whole or in part on the value of certain securities.

According to the German Tax Authorities (circular of the German Federal Ministry of Finance (BMF) dated 17 December 2002, IV A 6-S 2176-47/02), a provision for these securities-linked direct pension commitments may only be recognized acc. to Sec. 6a EStG if the employer guarantees a minimum benefit. Such a guarantee exists only when the employer has made a contractual commitment of an employer-financed minimum benefit, or, in the case of a deferred compensation scheme, according to the law in the amount of the respective vested pension benefits (i.e. the linked securities). Pension provisions may only be recognized based on the amount of the guaranteed minimum benefit. For employer-financed pension commitments, pension provisions should be recognized in the amount of the discounted value of the guaranteed minimum benefit and after deducting future services. For employee-financed deferred compensation schemes, pension provisions should be recognized in the amount of the discounted value of the linked securities, without deducting future services.

In its decision dated 4 September 2024 (case reference IX R 25/21), the German Federal Tax Court (BFH) had to decide on the securities-linked direct pension commitments to executives/shareholder-managers, which were partly financed by the employer and partly by the employees through deferred compensation. According to the BFH, a pension provision can be recognized according to Sec. 6a EStG even without a guaranteed minimum benefit. Consequently, for the recognition of a pension provision there is no restriction on the amount of the guaranteed minimum benefit. Therefore, for employer-financed securities-linked pension commitments, the pension provision can be recognized on basis of the current value of the linked securities (i.e. in the amount of the discounted value of the linked securities and after deduction of future services) if there is no guaranteed minimum benefit or if the value of the linked securities exceeds the guaranteed minimum benefit.

In its decision, the BFH also confirms its ruling of 28 February 2024 (case reference I R 29/21), which is also in favor of the employing companies. This ruling allows companies to recognize a pension provision for each separable part of a direct pension commitment that fulfills the requirements of Sec. 6a EStG even if other parts of the direct pension commitments do not fulfill the requirements of Sec. 6a EStG.

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Debt waiver by a shareholder of a corporation in return for a debtor warrant

The Federal Tax Court (BFH) had to decide whether the loss from a debt waiver in exchange for a debtor warrant should be accounted for at the time of the waiver and not only when it is certain that the condition subsequent will no longer occur.

In the underlying case, a shareholder of a GmbH waived his loan receivable against the GmbH. The waiver was subject to the condition subsequent that the GmbH was economically and financially able to repay all loans in full from a balance sheet profit or a liquidation surplus ("debtor warrant"). The shareholder claimed the resulting loss as income-related expenses in the waiver year.

In its ruling of 19 November 2024 (case reference VIII R 8/22), the BFH ruled that the loss from the non-recoverable portion of the loan claim is to be taken into account as the income from capital assets at the time of the waiver in accordance with section 20 (2) of the German Income Tax Act (EStG). In doing so, the BFH contradicted the opinion of the tax authorities, according to which the tax consequences of the conditional waiver are to be accounted for only if and as soon as it is established that the condition will no longer be met. Taxpayers subject to income tax should be aware of the BFH decision as it deviates from the established view of the tax authorities.

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European and constitutional doubts regarding the excess profit tax

The EU Energy Crisis Contribution Act, introduced on 16 December 2022, is based on Regulation (EU) 2022/1854, which was enacted in response to the sharply rising energy prices in the EU due to the war in Ukraine. The law imposes a solidarity contribution on unexpectedly high profits of companies operating in the oil, natural gas, coal, and refining sectors for the fiscal years 2022 and 2023. The assessment basis is the portion of the taxable profit that exceeds the average profit of the fiscal years 2018 to 2021, increased by 20%. The tax rate is 33%.

In its decision dated 20 December 2024 (2 V1597/24), the Finance Court of Cologne expresses significant EU law and constitutional doubts regarding the solidarity contribution and suspends the enforcement of the tax regulation in provisional legal protection. The court raises substantial doubts about the legality under EU law, particularly due to the lack of the unanimous decision by the Council of the European Union, which is generally required in tax matters. A preliminary ruling request regarding the legality under EU law is already pending before the European Court of Justice under case number C-358/24. Additionally, annulment actions (T-775/22; T-802/22) concerning the EU regulation are pending before the General Court of the EU.

In addition to compatibility with European law, the court also questions whether the act is in line with German constitutional law. The court raises concerns due to the restriction to only a small number of companies in the energy sector, as well as regarding the excessive overall tax amount of ordinary income taxes combined with the energy crisis contribution.

In this context, the Finance Court of Cologne has serious doubts about the legality of the tax registration in the present case and suspends the enforcement of the energy crisis contribution regulation. An appeal against the decision is pending before the Federal Tax Court under case reference II B 5/25 (AdV). Given the statements of the Finance Court of Cologne, a referral to a European court in the main proceedings is likely.

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Withholding tax on dividends under scrutiny of EU law

The European Court of Justice (ECJ) has recently addressed the significant matter of withholding tax (WHT) refunds for non-resident dividend recipients in two notable cases. The principles established in these rulings are also relevant for German WHT.

WHT refund for non-resident dividend recipients in a loss-making position
The ECJ's decision dated 19 December 2024 addresses the refund of WHT in situations where the dividend recipient incurs losses in their country of residence (C-601/23, Credit Suisse Securities (Europe) Ltd.). A company based in the United Kingdom received a dividend from a Spanish company in 2017, which was subject to WHT in Spain. A full refund of the WHT under the double taxation agreement between Spain and the UK was not possible.

The ECJ ruled that it violates the free movement of capital (Article 63 TFEU) if WHT refunds are provided solely to residents in a loss-making situation, while non-residents in a similar foreign loss-making position are denied such refunds.

In a mere domestic case, dividends in Spain are also subject to WHT, which is considered an advance payment on corporate tax. However, domestic Spanish dividend recipients can reclaim these advance payments if they incur losses. In contrast, non-resident dividend recipients (i.e., a UK company) are unable to reclaim the WHT due to its residency in the loss year, resulting in a definitive tax burden. The ECJ found this to be an unjustified interference with the freedom of capital movement.

However, the refund of the WHT does not mean that Spain waives its right to tax; it is our understanding of the ECJ decision that the dividends will be taxed ("recapture") once the non-resident generates profits in subsequent years. This decision aligns with a previous ECJ ruling (Sofina, C-575/17), which also deemed the immediate imposition of a final WHT as contrary to EU law when the foreign dividend recipient demonstrably incurs losses.

Generally, the principles of this ruling are also applicable to German WHT. In Germany, WHT on dividends, royalties and interest for non-resident recipients also has a final effect if a full relief under a double tax treaty or European directive (in particular parent-subsidiary directive) is not granted. In those cases, non-resident taxpayers may have an additional option to claim a full refund of WHT if they incur losses in their country of residence.

WHT on a gross basis without expense deduction for non-resident taxpayers contrary to EU law
In another ruling dated 7 November 2024 (XX, C-782/22), the ECJ found that a gross taxation of dividends paid to non-resident insurance companies can violate EU law. This can be the case if WHT is due on the gross amount of dividends paid to non-resident insurers, whereas a resident insurance company can credit this WHT and would thus only be taxed on its net income. The case brought before the court does not concern an entirely new issue. In several other decisions (e.g., College Pension Plan of British Columbia, C-641/17), the ECJ decided that final WHT on a gross basis can violate EU law. In Germany, domestic dividend income is taxed on a net basis, while foreign shareholders are subject to WHT on the gross basis. Therefore, it may be necessary, on a case-by case basis, to consider directly linked business expenses in the context of German WHT.

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Transfer pricing: Checklist for reporting obligations

With the Fourth Bureaucracy Relief Act (Viertes Bürokratie-entlastungsgesetz, BEG IV), published on 29 October 2024, further changes to the German transfer pricing documentation regulations were implemented. Already at the end of 2022 procedural changes were implemented with the DAC7 Implementation Act (DAC 7 Umsetzungsgesetz), whereby the submission deadlines for Local File and Master File were shortened from 60 to 30 days and would not start upon the tax auditor's request, but automatically within 30 days of the announcement of the tax audit.

The new regulations on transfer pricing documentation, which now came into force with the Fourth Bureaucracy Relief Act, introduced a potential relief for taxpayers regarding the previously shortened submission deadline for the Local File, but also introduced a new requirement to additionally prepare and submit a separate Transaction Matrix. From 1 January 2025, the taxpayer must submit the Transaction Matrix, together with the Master File and the documentation of extraordinary transactions, to the tax authority within 30 days of the official tax audit announcement. The Local File only has to be submitted during the tax audit when explicitly requested and within 30 days upon the tax inspector's request.

The Transaction Matrix must contain the following datapoints:
- Information on the subject and nature of the transactions
- The parties involved in the transactions, indicating (service) provider and (service) recipient
- The volume and remuneration of the transactions
- The transactions' contractual basis
- The transfer pricing method applied
- The tax jurisdictions involved
- Information on whether transactions are not subject to the standard tax treatment in the relevant tax jurisdiction

Failure to submit the Transaction Matrix on time may be subject to penalties of at least EUR 5,000 (additional sanctions may apply for non-compliance with the general documentation requirements, such as penalties for late submission or non-usability).

The changes are to be applied from 1 January 2025 also for all open unaudited tax years. The new submission deadlines are mandatory in all cases in which the tax audit notification has been or will be announced after 1 January 2025.

Taxpayers in Germany should therefore deal with the transfer pricing documentation requirements in a timely manner. The following checklist provides an initial overview of key questions that taxpayers should ask themselves after 1 January 2025:
- Is a Master File available?
- Were there any extraordinary business transactions, e.g. a restructuring? If so, has documentation been prepared?
- Is a Transaction Matrix available or can it be generated promptly?

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Key insights on Germany tightening the taxation of 401(k) plans and similar foreign pension schemes

Benefits from old-age pension schemes, direct insurance policies and pension funds are generally subject to taxation on a deferred basis. This means that in general the contributions are tax-privileged during the accumulation phase and that subsequent payouts are taxable in full. The regulation specifically lists the preferential treatments during the accrual period that lead to full taxation of the payout.

If, on the other hand, the benefits stem from contributions that have not received preferential treatment due to one of the listed provisions, only the difference between the benefit and the contributions is considered for taxation.

These principles also apply to benefits from foreign old-age pension schemes, direct insurance policies and pension funds. Before 2025, however, the payout was not taxable in full if the taxpayer was not liable to tax in Germany during the accumulation phase. In the past, this omission could lead to a considerable tax advantage.

The German Federal Tax Court (BFH) ruled on 28 October 2020 (X R 29/18) that for a pension plan under US law ("401(k) plan") only the difference between the capital payment and the contributions could be considered for income tax purposes as the contributions were not tax-privileged in Germany – even though a comparable privilege had been granted in the US during the accumulation phase. According to the BFH, Sec. 22 No. 5 Sentence 2 German Income Tax Act (EStG) provides a conclusive list of the tax exemptions and privileges that lead to the benefits being considered in full. The court rejected the view of the tax authorities that the full amount should also be taken into account for taxation in the case of similar privileges in another country during the accumulation phase.

As a result, recipients of such benefits were sometimes in a better tax position because, despite the amounts being tax-privileged abroad during the accumulation phase, income tax was levied only on the income portion at the time of payout in Germany.

The German government responded to the BFH decision by tightening the rules concerning deferred taxation of benefits received from foreign old-age pension schemes, direct insurance policies or pension funds as part of the German Annual Tax Act 2024. From 1 January 2025 they are also taken into account in full for tax purposes if they are based on contributions for which a tax exemption or preferential treatment (comparable to the German regulations) was granted in another country. If a payout from such plans is considered while being subject to unlimited taxation in Germany, the tax implications should be thoroughly checked well in advance.

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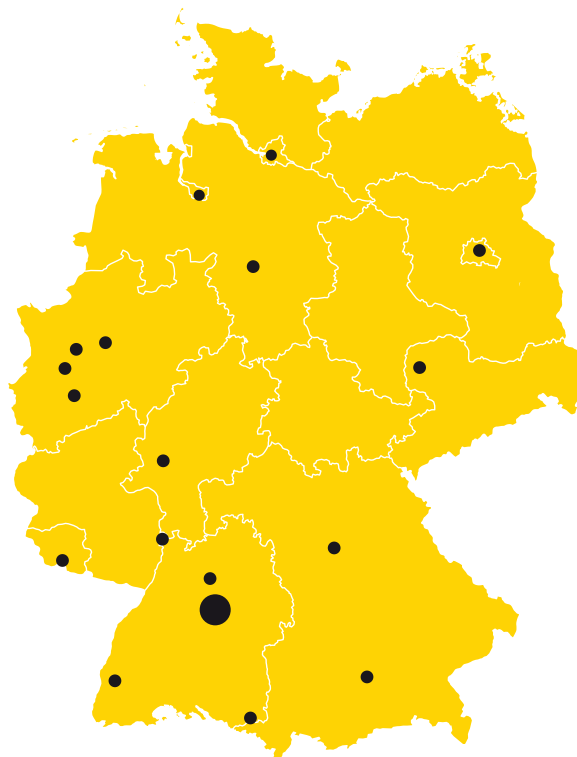

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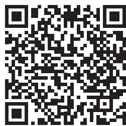

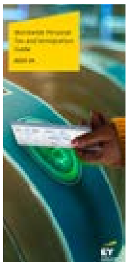

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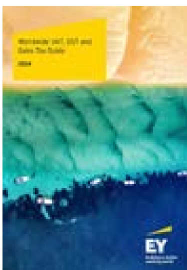

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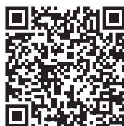

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