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Tax & Legal News

Statutes
Cases
Decrees

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Official Pronouncements

Correction of VAT overcharge only after repayment

If a supplier overcharges VAT, he is liable to the tax office for the excess although the customer may not deduct more than the correct amount as input tax. With the agreement of the tax office, the supplier may issue a corrected invoice as a basis for recovery of the overpayment. Recovery is conditional upon there being no danger to tax revenue, which basically means the assurance that the customer has not deducted more than the correct amount of input tax. In 2008, the Supreme Tax Court added the further condition that the supplier must have repaid the excess amount to the customer. The finance ministry has now amended its VAT Implementation Decree accordingly.

Following this amendment, recovery of the excess from the tax office depends upon repayment to the customer. The tax office may give its approval for the issue of the corrected invoice before repayment. If, however, the final invoice amount remains unchanged, i.e. the supplier does not repay the overcharge, the VAT is recalculated at the correct amount based on the invoice total. This recalculation will lead to an increase in the deductible input tax for the customer, though only if a corrected invoice showing the new amount is issued.

Staff parties

The Income Tax Act provisions on the benefit in kind for employees attending staff parties, outings and similar functions were revised for 2015. Essentially, the changes recast the previous tax-free limit into a tax-free allowance whilst now taking up all direct costs incurred into the calculation. The finance ministry has now issued a degree setting out its view of the new rules in some detail:

- A staff function in this context presupposes that attendance is open to all employees of the company. However, separate functions may be held for separate units of the organisation (e.g. departments) and for pensioners. Employees from associated companies may also take part, again provided participation is open to all.
- The costs of the function now include all direct costs incurred, but no overhead allocations. Thus, the cost of hiring a room or for music is part of the cost of the function, whereas the costs of the wages department to calculate the benefit in kind – or the heat light and power consumed in a function held on the company premises – are not. The exception is the travelling costs of outside employees to reach the function (e.g. two branches holding a joint function). These are deductible by the employer and exempt for the employee as normal business travel.
- The cost per head is established by participant, but participants are then allocated to their participating employee host. Thus, if a function costs €10,000 and is attended by 75 employees and 25 spouses, the participant cost is €100 per head. Unaccompanied employees have no taxable benefit, as this amount is less than the €110 tax-free allowance. By contrast, each of the accompanied employees taxes a benefit of €90 –

€200 cost less €110 allowance.

- Two staff functions are privileged each year. The employer may tax the benefit in kind at a flat rate of 25%.
- The changes have no direct effect on VAT. Thus the old rule continues: if the cost per employee is no more than €110, it will be deemed as having been incurred in the interests of the employer. If it exceeds that amount, the entire cost will be treated as having been incurred for the private benefit of the employees and no input tax will be deductible.

Supreme Tax Court Cases

Post-dissolution profits and losses from foreign P.E. attributable to foreign country

A GmbH maintained a branch in Belgium up to 2000. In that year, it closed the branch, winding up the tax affairs of the Belgian permanent establishment, after charging a provision for anticipated costs against the Belgian profits. In 2009, part of this provision was released as being no longer required. The tax office maintained that the gain from this release was part of German taxable income, as there was no longer a Belgian branch to which it could be attributed. The GmbH disputed this point of view.

The Supreme Tax Court has now held for the taxpayer. The gain in question followed from the release of a provision originally charged against the Belgian taxable income from the branch. It was therefore attributable to the branch as a post-dissolution event and taxable under the double tax treaty in Belgium as business income. The amount to be deducted from the remaining income to be taxed in Germany was to be calculated under German accounting (tax computation) rules and was thus independent of the treatment in Belgium. However, in regard to this latter point, the court stressed that its present ruling could not be relied upon for years after 2009 (in the meantime fall-back and switch-over provisions have been introduced to make treaty exemption in Germany conditional upon actual taxation in the other state. However, these provisions are of disputed validity).

Supreme Tax Court judgment I R 75/14 (NV) of May 20, 2015 published on October 7

Compensation for loss of office taxable in Switzerland despite mutual agreement to contrary

The German/Swiss double tax treaty taxes compensation paid to former employees for their loss of employment in their country of current residence. They are only taxable in the country of former employment on compensation for benefits, such as accrued bonus or holiday entitlement, already earned. This treaty interpretation, usual in Germany, is not fully followed in Switzerland. Accordingly, the two finance ministries agreed a mutual interpretation of the treaty to the effect that compensation for loss of employment should be taxed in the country of the employment if paid to mitigate the loss of income, and in the country of residence if paid in order to provide for the continued subsistence of the recipient. The agreement was felt to be necessary in the interests of avoiding “white income”. A manager who lost his job in Germany and who then moved to Switzerland to take up a new employment there found himself faced with German taxation on his not inconsiderable compensation for loss of office.

The Supreme Tax Court has held for the taxpayer. Under the treaty as interpreted by the German courts, compensation for loss of office was taxable in the country of residence of the employee when paid. This treaty had been implemented into German law by act of parliament. A mutual agreement between the two fiscal authorities could not change the treaty or its full legal status. An enabling provision in the Foreign Tax Act allowing the finance ministry to transpose mutual agreements into German law by ordinance requiring the approval of the Bundesrat was not sufficiently precise to provide a legal basis for what effectively amounted to a treaty change. That provision could not therefore be applied here. Rather, the change should be documented by treaty amendment which would then require the full process of enactment if it were to attain legal force.

Supreme Tax Court judgment of I R 79/13 of June 10, 2015 published on September 30

Bribes taxable as other income

An employee in purchasing regularly took bribes from a supplier. Initially, he issued invoices in his wife's name for (non-existent) services rendered and taxed the amounts as business income. However, the fraud came to light and he was dismissed by his employer. He accepted his dismissal and agreed to pay a substantial part of his total bribe receipts over the years to his employer as damages. He also accepted forfeiture of his future pension rights and his unpaid bonus. He claimed an expense deduction in the amount of the damages paid, the forfeit bonus and the capital value of the pension rights lost. This deduction was from employment income and was therefore deductible from taxable income in general. The excess was a loss that could be carried back for one year or forward to all future years until fully offset against positive earnings.

The tax office refused this deduction. Rather, it reclassified the bribe receipts as other income and the compensation to the employer as expenses of earning that other income. That meant that the expenses could only be offset against the other income earned in the year they were incurred (zero), carried back against other income earned in the previous year (minimal) and forward against future other income (no concrete prospects of future receipts).

The Supreme Tax Court sided with the tax office. The bonus and pension forfeitures were not deductible at all, as the income would only have been taxable when paid. The compensation payment to the employer was neither an expense of earning employment income leading to a generally deductible loss, nor was it a repayment of previously taxed income that would similarly have been generally deductible. It was a payment for damages caused by the employee's dishonesty and was thus linked to the fruits of that dishonesty – to the bribe receipts taxed as other income. It could therefore only be set against other income, either now or in the future, as and when other income came to be earned.

Supreme Tax Court judgment IX R 26/14 of June 16, 2015 published on October 14

Local tourism taxes constitutional

Many local authorities levy tourist taxes on hotels and other establishments offering overnight accommodation to tourists. The Supreme Tax Court has now held in two cases that these taxes (in Bremen and in Hamburg) are in accordance with the constitution. In both cases, the tax is levied on the length of stay at fixed rates (€2 per head and night in Bremen; €1 for each €50 of the overnight charge in Hamburg, again per head and night). Again in both cases, there are a number of exemptions, including business travel. In Bremen business travel is demonstrated by addressing the hotel bill to the business or company, and in Hamburg by "appropriate vouchers". An employer's certificate is an example of an appropriate voucher.

Fundamentally, the constitutional complaints were based on two contentions: that the local tax duplicated the federal tax of VAT and that the business travel exemption made actual collection of the tax too uncertain for it to be seen as anything other than arbitrary. The Supreme Tax Court has now rejected both contentions. In the view of the court, the local tax does not duplicate VAT as it is levied at a fixed amount (Bremen) or on a fixed scale (Hamburg) on a specific item – accommodation for tourists – as opposed to a set rate on the total charge for all supplies of any description other than those explicitly exempt. It is also levied as a single-phase tax as opposed to the multi-phase VAT. The claim that collection was uncertain was based on the unsupported assertion that tourists were able to avoid the tax at will by telling the hotel staff that they that they were in town on business. However, the court pointed in both cases to the necessity for documentary evidence and to the rights of the city authorities to make spot checks and take other steps to ensure control.

Supreme Tax Court judgments II R 32/14 (Bremen) and II R 33/14 (Hamburg) of July 15, 2015 published on October 21

Ruling fee based on immediate tax effect

Tax offices may issue binding rulings to taxpayers on the tax treatment of planned measures or transactions against payment of a value-based fee. The value is the tax effect of the ruling, that is, the difference between the tax payable if the tax

office rules as requested by the taxpayer and that payable were the tax office to take the opposite position. No fee is payable if the value is less than €10,000 and the maximum chargeable value is €30 m. The corresponding fee range is €241-€91,456.

The Supreme Tax Court has now held that the tax value of ruling requests is to be based on the immediate tax effects of the ruling only. The ruling at issue was on whether or not a planned corporate reconstruction could be recorded at book value, and thus to defer into the future the taxation on the capital appreciation of the tangible and intangible assets. The applicant made the calculation as required, but deducted the tax effect of the (then) deductible trade tax provision resulting from the release of the hidden reserves. He also deducted the effects of the future tax savings resulting from the higher tax depreciation base of assets revalued to market value. The court though rejected both adjustments, saying that neither the trade tax provision nor future depreciation were the subject of the ruling and were thus not relevant to the calculation of its fee.

Supreme Tax Court judgment IV R 13/12 of April 22, 2015 published on October 14

From Europe

CCCTB revisited – have your say

In March 2011, the European Commission, after years of discussion, proposed a directive to the European Council on a common consolidated corporate tax basis as an option for companies deriving business income from establishments or subsidiaries in more than one member state. At the time, the Commission hailed this initiative as a great step forward, although many saw the draft as little more than a suggested set of primitive accounting rules. Since then, the Council has taken no action and the project now has to be seen as a failure. There are a number of reasons for the Council's (member states') lack of interest, including the lack of any reference to rules allowing or disallowing expense deductions for other than accounting reasons (e.g. funding requirements for pension provisions, restrictions on business entertaining and the investment incentive elements of tax depreciation rules), the inability to properly debate the merits or demerits of allowing taxpaying companies the option between a set of basic accounting standards and the detailed rules of individual member states, and the consolidation aspects of the scheme which would allow not only a complete cross-border loss offset, but also elimination of intra-group profits and losses. The Commission, itself, sees the reason for the lack of council interest in the "sheer scale" of the project, though this view may be fanciful.

The Commission has now decided to restart its project and has called for comments from all interested members of the public, from business, from government and from the world of academe. Go to this link and have your say between now and January 8, 2016.
http://ec.europa.eu/taxation_customs/common/consultations/tax/relaunch_ccctb_en.htm

European Council agrees on automatic information exchange on tax rulings

At its ECOFIN meeting in Luxembourg on October 6, 2015 the European Council reached "political agreement" (agreement in principle) on a draft amendment to Council Directive No. 2011/16/EU on administrative cooperation between member states on tax affairs. This amendment foresees the automatic exchange of information every six months on tax rulings issued with cross-border impact with all other member states. Advance pricing agreements (APA) are also covered. The draft amendment is to be finalised this year after hearing the opinion of the European Parliament and is to be transposed into the national law of member states for entry into force on January 1, 2017. Rulings issued during the previous five years are also to be communicated (those of 2012/13 only if they were still in effect on January 1, 2014) in 2017. The tax authority of any member state receiving information on a ruling may ask the issuing authority for further details. The Commission is to set up a central database on cross-border rulings for monitoring purposes.

Dealing in "bitcoin" exempt from VAT as a currency exchange

A Swedish currency dealer wished to offer a virtual currency exchange service of buying and selling "bitcoin" for Swedish Kroner at the daily rate of exchange together with a margin. He maintained that this service should be VAT-free as a currency exchange or as a transaction in negotiable instruments, but the tax authorities saw it as taxable as any other service, "bitcoin" not being an actual currency.

The ECJ has now held that "bitcoin" is to be regarded as a currency for the purposes of the VAT Directive. There is disparity between the different language versions of the directive, so no one version should be taken literally. However, the only purpose of "bitcoin" and other virtual currencies is to be used as a means of payment to those willing to accept them. They are therefore to be equated with actual currencies. Dealing in them for an actual currency is exempt from VAT as a currency exchange.

The ECJ case reference is C-264/14 *Hedqvist* judgment of October 22, 2015.

German restrictions on tax consultancy excessive?

A former German tax consultant (he lost his professional qualification in 2000) resident in Belgium together with a professionally unqualified associate resident in Germany set up a tax consulting company under English law operating through Dutch and Belgian branches. The two partners claimed to be offering consulting services from Holland, an unregulated environment, on German tax issues for German clients. A German tax office refused to accept tax returns prepared with their assistance and they claimed this refusal to be an unjustified restriction on their freedom to provide services from one member state to clients in another. This service provision was legitimate in Holland and could not be restricted by German professional rules.

Despite considerable uncertainties on the facts of the case, including, in particular, the place and method of operating, the responsible advocate general has suggested the court hold in favour of the service providers. His view is based on the contention that although the German restrictions serve a legitimate purpose, they go beyond the extent necessary to achieve their object. In particular, they insist upon management of consultancy practices regularly operating in Germany by holders of German professional qualifications and upon prior registration by the holders of foreign qualifications wishing to operate occasionally in Germany. There is thus little or no scope for those who do not meet the formal German requirements to demonstrate their competence in other ways. However, the advocate general also points to the number of organisations and individuals permitted to offer tax advice despite lack of professional qualifications. The list includes trade associations, actuaries, employers, carriers, patent lawyers and foreign banks. However, the advocate general does not mention that those on this list are not permitted to offer general tax consultancy, but are only able to apply the rules for those taxes (such as employee withholding taxes) with which they are directly concerned. Possibly, this omission could be seen as weakening his argument.

The ECJ case reference is C-342/14 *X Steuerberatungsgesellschaft* opinion of October 1, 2015.

From PwC

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