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Statutes
Cases
Decrees

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Official Pronouncements

FATCA regulations finalised

On May 31, 2013 Germany and the USA signed an agreement setting forth the conditions to be adhered to by German banks wishing to be ranked as FATCA-compliant (Foreign Account Tax Compliance Act) and so avoid penalty withholding taxes on their US source income. FATCA reporting to the (US) IRS is through the (German) Central Tax Office, which is also responsible for supervising adherence to the conditions by banks and other financial institutions operating in Germany. In June of this year, the finance ministry published a discussion draft of its intended regulations to be followed by financial institutions. This draft has now been finalised and republished in the form of a decree. Essentially, banks have a reasonable time to adjust their procedures to meet their FATCA reporting obligations in respect of all accounts held for US taxpayers. The first reporting deadline is July 31, 2016.

Tax information exchange agreements

The finance ministry has issued a decree on the procedures to be followed by tax offices when requesting information from the authorities of another country under a tax information exchange agreement. Requests are to be routed through the Central Tax Office and are to be made on a form designed for that purpose. The decree also discusses German participation in foreign tax audits and foreign participation in German ones, as well as information requests in connection with criminal proceedings.

Purchase of doubtful debts VAT-free

On October 27, 2011, the ECJ held the purchase of doubtful debts (non-performing loans) not to be a business activity and therefore free of VAT (case C-93/10 *GFKL*). The Supreme Tax Court followed this case and the finance ministry has now amended its VAT Implementation decree accordingly. A doubtful debt in this connection is one that has not been serviced for 90 days past the due date for interest or capital repayments (minor deficiencies excluded). A loan is also doubtful in this sense if immediate repayment has been demanded, or where the creditor is entitled to do so. Since the purchase of a doubtful debt is not a business activity, no input tax on the costs of purchase or collection can be deducted. This position contrasts with the purchase of a valuable debt as a collection service, or to relieve the creditor of business risk. In this latter case, the service is subject to VAT, the margin between the purchase price and the redemption value being the gross consideration including VAT.

VAT-free sales with interrupted delivery

VAT-free intra-community or export sales of goods basically presuppose uninterrupted delivery from the seller to the buyer, by, or at the order of, one of the two parties. However, it can happen that the delivery flow is interrupted, such as where the seller carries the goods to the docks where they are loaded onto a ship for carriage to a port in the buyer's home country. The buyer then takes delivery on arrival, taking the goods to their final destination on his own premises. Effectively, the carriage is shared between buyer and seller; thus it is not a single journey. However, the finance ministry has now decreed that a "broken", or interrupted, journey in such circumstances may still be treated as a single transport – with VAT exemption for the transaction as an intra-community supply or export sale – if the final destination is known at the start of the first movement and the legs of the journey are continuous.

By contrast, the ministry takes the view that an interrupted delivery breaks a triangular transaction so that each link in the chain becomes a separate sale with its own VAT consequence. However, it makes an exception in respect of deliveries from other member states through Germany to third countries that are treated as triangular transactions under the law of the state of departure. That position will be followed in Germany if a Germany tax liability would be the consequence of not doing so.

Full input tax deduction on VAT-free sales to NATO forces

The finance ministry has followed a Supreme Tax Court judgment of August 2013 holding that a VAT exemption under a special-case rule takes precedence over the exemption available under a generally applicable provision. Sales to NATO forces stationed in Germany (including sales for the benefit of their members) are exempt under the various NATO and SOF (status of forces) agreements, which rank as special-case rules. Accordingly such sales do not restrict the right of the supplier to deduct input tax, even if, under the generally applicable rules, the sale would have been exempt with curtailment of the supplier's input tax deduction.

Supreme Tax Court Cases

Development aid secondees to Indonesia taxable in Germany

The double tax treaty with Indonesia provides that the salaries of specialists seconded by the German development aid agency to work in Indonesia on German-sponsored development aid programmes remain taxable in Germany unless the work is physically performed in Indonesia and the individual specialist is resident there and is not a German national. The German tax office of a specialist sent to Indonesia on a ten-month assignment as office manager claimed that these treaty provisions meant that his entire salary was taxable in Germany. He responded with the assertion that only 60% of his time hat been spent on projects solely funded by the development aid agency, the remainder being devoted to joint projects with other agencies and to general office admin. In consequence, 40% of his salary was taxable in Indonesia and should be free of German tax.

The Supreme Tax Court has now held in favour of the tax office. The salary concerned had been paid entirely from German public funds channelled through the development aid programme. The work assignment was the on-site management of that programme; thus the work had been performed in that connection. That some of the specific projects had been co-financed from other sources had no bearing on the individual's own salary that had not been co-financed. Similarly, the office admin was part of the development aid programme even if it could not be allocated to specific projects. The entire salary was therefore taxable in Germany, assuming the local residence/nationality exception did not apply in the present circumstances.

Supreme Tax Court judgment I R 42/13 of July 7, 2015 published on November 11

Foreign business VAT refund claim form must be complete

Businesses from non-EEA countries may reclaim German VAT borne on their business expenses from the Central Tax Office by filing a refund claim on the appropriate form (or electronically) with the Central Tax Office by June 30 of the following calendar year. The Central Tax Office rejected in October a claim received on June 30 because the form had been incompletely filled out (the confirmation that the services in question had been purchased by the claimant for its business was missing). The Supreme Tax Court has now held that the Central Tax Office was right to reject the claim, as the missing item could not be added after the filing deadline.

Supreme Tax Court judgment V R 9/14 of September 24, 2015 published on

November 11

No VAT avoidance through clash of concept in mail order business

A GmbH arranged for delivery of medicines by its Dutch subsidiary (registered as a chemist – apothecary) to a series of German chemist's shops to be picked up by the end customer against a previously placed customer order. The customer order form gave the customer the choice between delivery to the chemist's shop for a fixed fee (€0.50 per item) or personal pick-up in Holland. The Dutch subsidiary arranged the transport through its GmbH parent, retaining the difference between that company's actual charges and the €0.50 paid by the customer as "commission" for arranging the transport. That subsidiary claimed exemption from VAT in Holland under the mail order exception making mail order deliveries to private consumers taxable in the country of the consumer (unless the total annual supply did not exceed a set limit of – in Germany – €100.000). In Germany, the subsidiary took the position that the business model was not mail order as the transport had been arranged at the specific request of the customer and therefore on his or her behalf as a separate supply. It explained its different conclusions in the two countries on the basis of a slight difference in wording between the mail order provisions of the respective VAT acts. The tax office, though, saw the whole arrangement as mail order from Holland, subject to German VAT.

The Supreme Tax Court has now agreed with the tax office. The customer had no choice as to the means of transport and the personal pick-up option was clearly of only theoretical interest as shown by the minimal use made of it. The actual transport had been arranged by the supplier through its own parent company and its cost had no effect on the standard charge the customer was asked to pay. This standard charge was minor, and could only be justified in economic terms on the basis of bulk shipments in a fully loaded van. The court also pointed out that the language difference claimed was not the only one relevant to the case at issue, citing the English and French versions as further examples. Accordingly, the purpose of the provision must be taken into account, too, and this was to tax large-scale mail order business in the country of the consumer in order to avoid major shifts to countries with low VAT rates. Full exemption from VAT was most certainly not the objective of the provision in the VAT Directive.

Supreme Tax Court judgment XI R 2/13 of May 20, 2015 published on November 4

From Europe

Tax transparency with Liechtenstein

The EU and Liechtenstein signed a tax transparency agreement on October 28, 2015. From 2017 onwards the competent tax authorities of Liechtenstein and the EU member states will automatically exchange information on bank accounts held on behalf of residents of the other state. The information to be exchanged includes the names, addresses, dates of birth and tax identification numbers of accountholders as well as information on account balances. The object is to enable local tax offices to raise the appropriate queries with their own taxpayers. The EU has signed similar agreements with San Marino and Switzerland and initialled one with Andorra. It is still negotiating with Monaco.

For Germany, this EU agreement is a significant advance, replacing, as it does, the previous agreement of September 2, 2009 for the provision of specific taxpayer information on request and augmenting the (similarly, on request) information exchange clause of the double tax treaty with Liechtenstein of November 17, 2011.

ECJ confirms German extended limited tax liability

The Foreign Tax Act provides for continuing liability to German tax for former residents on their German source income if they continue to hold significant economic interests in Germany after their move abroad to a low tax country. This "extended limited tax liability" applies for the ten years following the year of the move by persons with five years of previous residency. Double taxation is avoided by crediting the foreign tax paid against the German liability. A similar rule is included in the double tax treaty with Switzerland, although the period only runs for five years and the treaty explicitly exempts Swiss nationals.

A previously long-term resident German national moved to Switzerland, but continued to work for his German employer, in part from his Swiss home. The German tax office continued to regard him as fully taxable in Germany on his German employment income under the "extended limited tax liability" provision. The taxpayer protested on the grounds that the exemption for Swiss nationals discriminated against him on the grounds of nationality at variance with the non-discrimination provision of the EU/Swiss accord on the free movement of workers.

The ECJ has now pointed out that member states are free to arrange their own direct tax affairs – including treaty relations – provided they do so with respect for the basic EU freedoms. The continued "extended limited tax liability" was not a breach of the EU/Swiss accord as that latter explicitly excluded bilateral tax treaties with member states from its scope. The taxpayer did not suffer any disadvantage from his move to Switzerland, since his overall liability remained the same, the Swiss tax being credited against the German liability. That he would have had an overall lower liability, had he been a Swiss national was irrelevant, given that the purpose of the double tax treaties was to avoid the same income being taxed twice and not to ensure the most favourable tax regime for each taxpayer. Accordingly, there was no breach of any fundamental EU freedom.

The ECJ case reference is C-241/14 *Bukovansky* judgment of November 19, 2015.

Tax information obligation on foreign bank branches justified in overriding interest of fair taxation?

A southern German bank maintained a branch in Austria, where a number of German residents held accounts. The German Inheritance and Gift Tax Act requires banks to inform the relevant tax authorities of the assets held or managed on behalf of deceased account holders. In 2008, the local inheritance tax office requested the bank for account information on all German resident account holders at its Austrian branch who had died since 2001. The German bank objected that it could not supply this information without infringing an Austrian bank secrecy rule making it a criminal offence to pass information on the affairs of an account holder to other than specified recipients without his or her consent. Tax offices were not one of the specified recipients and a deceased individual was no longer able to give consent.

This clash of laws brought the case before the ECJ. The advocate general has suggested that the court take the position that there is no direct clash of laws, given that the German rule is enshrined in a tax act, whereas the Austrian rule is a provision of the Banking Act with no specific mention of taxation. Rather, there is a restriction on the freedom of establishment to be found in the German rule, though this restriction is justified by the need to protect the integrity of the tax system and does not go beyond the minimum necessary to achieve that aim. The advocate general recognises that such a finding does nothing to solve the case at issue – the conflict of laws – and contents himself with the suggestion that the Austrian authorities be duty bound to apply, or disapply, their bank secrecy rule in a spirit of cooperation within the confines of European law. Quite how this could be expressed in an order by a European or German court in a case to which Austria is not a party, he does not say.

The ECJ case reference is C-522/14 *Sparkasse Allgäu* opinion of November 26, 2015.

Input tax on dual use expenses to be split by turnover unless otherwise prescribed for specific circumstances?

The Sixth (and now the VAT) Directive requires the input tax on dual-use costs to be allocated in the ratio of taxable to exempt outputs as measured by their respective turnover, unless another method would lead to more precise results. The German VAT Act, by contrast requires that a turnover based split may only be taken if no other method is possible. A builder of a large house to be rented partly with VAT to other businesses and partly VAT-free as living accommodation split the input tax into recoverable/irrecoverable portions on the basis of the respective turnover. The tax office insisted the split be made by floor space as giving a more accurate (and for the public purse, more favourable) result. Since the argument turns on the compatibility of German law with the VAT Directive, the case came before the ECJ. The advocate general has suggested the court not answer the specific questions raised by the German court, but rather hold that the VAT Directive provision has been incorrectly transposed into German law. He argues that the VAT Directive prescribes a turnover-based split as the general rule only to be departed from in specific circumstances. German law, on the other hand, sees the turnover split as the fall-back position, only to be applied where all else fails. The two concepts stand in direct contrast; thus that of the VAT Directive as the primary law must prevail. Since the German VAT Act makes no mention of specific exceptions, it follows that the authorities can in no circumstances hold a taxpayer to any split other than by turnover.

The ECJ case reference is C-332/14 *Rey* opinion of November 25, 2015.

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