

Tax & Legal Newsflash

MoF draft bill on the Implementation of the Anti-Tax Avoidance Directive (ATAD Implementation Act) provided to federations for comment

On 10 December 2019, the Federal Ministry of Finance (MoF) provided various federations and associations with a draft bill on the Implementation of the Anti-Tax Avoidance Directive (ATAD Implementation Act) for comment. The decision of the Cabinet has already been scheduled for 18 December 2019.

Implementation of the European Anti-Tax Avoidance Directive

Following the adoption of EU Directive 2016/1164 of 12 July 2016 (ATAD), as amended by EU Directive 2017/952 (ATAD II) of 29 May 2017, on 10 December 2019, the MoF provided the draft implementation bill to various federations and associations for their comments.

Other EU Member States have also submitted draft bills for the implementation of the Directive in recent months, and in some cases the laws have already been passed.

The present draft bill is intended to implement the ATAD's regulations on exit taxation and hybrid structures as well as on the reform of Controlled Foreign Companies (CFC) rules. In addition, there are to be adjustments to the transfer pricing rules in Section 1 of the Foreign Taxes Act (FTA).

Exit taxation

According to Article 5 ATAD, Member States are obliged to tax (on application in instalments) undisclosed reserves in cases of cross-border transfers of assets, the relocation of businesses or the exit from a jurisdiction of a corporation. Furthermore, where assets are transferred cross-border or a corporation relocates, the "receiving" Member State is obliged to recognise the exit tax value established by the other Member State as the starting value of the assets for tax purposes insofar as this reflects the market value. The draft bill provides for the implementation of Article 5 ATAD in the Income Tax Act (ITA) and the Corporation Tax Act (CTA) (including adjustments to Sections 4, 4g and 6 ITA Draft, and Sections 36 (5) and 12 CTA Draft). Moreover, the draft bill should standardise the deferment concept as well as "bolstering" Germany's right to tax.

The draft bill also includes adjustments and, in particular, a tightening of provisions for the exit taxation of individuals in EU cases within the framework of Section 6 FTA (Draft).

Reform of CFC rules

As part of the implementation of ATAD (Articles 7 and 8), the draft bill provides for a reform of the already existing German CFC rules. The implementation relates to



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Section 7 FTA et seq. The following measures should be highlighted:

A core element is the modification of the control criterion resulting in a shift away from domestic control to a shareholder-based approach, taking into account related parties.

In addition, in the case of multi-level company structures, loss consolidation no longer takes place at the level of the top foreign company within the framework of the CFC rules.

In the case of profit distributions, a deduction will be introduced to avoid double taxation.

However, the draft bill does not provide for a reduction of the rate deemed to constitute a low tax rate. Thus, this remains at the 25% level. The justification given for this is that the consensus at OECD level on the introduction of a global minimum taxation should not be preempted.

The catalogue of active income will be retained. There are some changes as well as some tightening of certain rules (e.g. in relation to dividends and conversions).

Hybrid structures and tax residency mismatches

Articles 9 and 9b ATAD oblige Member States, inter alia, to refuse the deduction of operating expenditure for certain expenses in connection with hybrid arrangements where the income corresponding to the expenses is not taxed by the creditor or these expenses can also be deducted in another state without the expenses being offset by income that is taxed in both states.

In addition, the deduction of operating expenses must also be refused in the case of so-called imported mismatches. These arise where deductible expenses and the corresponding income lead to a tax mismatch in other states which states do not eliminate this mismatch and as a consequence this mismatch is "imported" into Germany via one or more transactions.

The implementation of the rules will essentially be executed through the introduction of a new Section 4k ITA (Draft), which is supported by further provisions in the Sections 3 No. 40d Sentence 2, 50d (9) No. 3 ITA(Draft) and Section 8b (1) Sentence 3 CTA (Draft). The rules represent the ATAD minimum standard.

Further measures

Furthermore, far-reaching adjustments and in some cases a considerable toughening of arm's length principles (Sections 1, 1a, 1b FTA-Draft) and the creation of a legal basis for advanced pricing agreements (Section 89a General Tax Code -Draft) are planned.

Within those changes a proposed regulation limiting the deduction of interest expense is foreseen, if certain legally defined requirements to prove the arm's length settlement of the underlying loans are not met. The provision is applicable from 1 January 2020 onwards.

Next steps

The federations and associations now have until 13 December 2019 to comment. The cabinet decision is scheduled for 18 December 2019. However, the legislative process will not be completed until next year; notwithstanding this, the regulations will in principle be applicable from 1 January 2020.

As this is a statute requiring assent, the approval of the Bundesrat is required in addition to a decision in the Bundestag.

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