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Official Pronouncements

Bundestag adopted the Act for the Mandatory Reporting of Cross-Border Tax Planning Arrangements

On 12 December 2019, the Bundestag adopted the Act for the Mandatory Reporting of Cross-Border Tax Planning Arrangements. The final approval by the Bundesrat will take place on 20 December 2019

The Resolution of the Bundestag

On 12 December 2019, the Bundestag adopted a law to introduce the mandatory reporting of cross-border tax planning arrangements. The adopted law included the amendments recommended by the Finance Committee. Some other tax regulations have also been amended within the framework of this law. As this is a statute requiring assent, the approval of the Bundesrat is required.

Here is a summary of some of the important amendments to the government bill:

Amendments to the bill on cross-border tax arrangements

In accordance with the recommendations of the Finance Committee of 11 December 2019, the following amendments were made to the government bill:

- The definition of the "tax advantage" has been supplemented and now includes in addition to the granting of tax refunds, also the increase in tax refunds and in addition to the reduction of tax claims also the elimination of tax claims (Section 138d (3) Sentence. 1 General Tax Code "GTC");

- In the original bill no "tax advantage" was considered to exist provided the tax advantage of the cross-border arrangement only had an effect in Germany and provided that the arrangement as a whole was permissible by law. The law adopted by the Bundestag no longer contains this legal regulation. Rather, the Federal Ministry of Finance is authorized, in conjunction with the Federal States, to issue a circular specifying that for certain group categories and under certain criteria no tax advantage will be assumed within the meaning of the Act. Thus, for the group categories listed therein there should be certainty that no reporting obligation exists. However, for tax planning arrangements not included in the circular – for whatever reason – an obligation to report will exist to the extent that the remaining legal prerequisites (Section 138d (3) sentence 3 GTC) are existent.

- Insofar as not yet provided for in the original bill, hallmarks relating to cross-border payments between related parties are restricted to such payments, which can be deducted by the payer as business expenses. In this respect the German provision now complies with the requirements of the Directive (Section 138e (1) No. 3 letters d and e GTC).

- The obligation for an intermediary to report the names of other intermediaries known to him has now been replaced by an option to report (Section 138f (3) S. 2 GTC).

- Where the user of a cross-border arrangement has not been released an intermediary from his legal professional privilege obligations, the obligation of the intermediary to report the arrangement can also be met where the user provides the information which should actually be provided by the intermediary to the Federal Central Tax Office on behalf of the intermediary (Section 138f (6) S. 4 GTC).

- Violations in connection with the obligation to disclose the economic value of cross-border tax arrangements are no longer included in the list of misdemeanours in Section 379 (2) GTC.

- The Federal Ministry of Finance will be obliged to report to the Finance Committee of the Bundestag annually on 1 June on the number of notifications of cross-border tax arrangements and their treatment (Art. 97, Section 33 para. 4 Implementation Act to the GTC).

Further tax changes
The ability to offset losses on income from forward transactions and from the losses on investments held as private assets has been limited:

- Losses from certain forward transactions, e.g. from the expiration of options or losses on the disposal of forward transactions/futures or similar financial instruments can only be set off against profits from similar transactions and with income from so-called option writer transactions up to a maximum amount of €10,000. Unutilised losses can, however, be carried forward to future years and offset according to the same principles (Section 20 (6) Sentence 5 ITA). The new regulation applies to losses arising after 31 December 2020 (Section 52(28) Sentence 23 ITA).

- Losses arising from fully or partially irrecoverable capital receivables, which also include for example shareholder loans, or arising from the write-off or transfer to third parties of worthless assets, or write-offs within the meaning of Section 20 (1) ITA are also subject to a restricted loss utilization. These may only be set off against other income from capital assets up to a maximum amount of € 10,000 and thereafter carried forward to subsequent years, and then offset according to the same principles (Section 20 (6) Sentence 6 ITA). This provision should apply to losses arising after 31 December 2019 (Section 52 (28) sentence 24 ITA).

- The turnover limit for receipts-based taxation is being raised to EUR 600,000 (Section 20 (1) No. 1 VAT Act).

- “Investing Members” within the meaning of Section 8 (2) of the Cooperatives Act will no longer be considered “members” within the meaning of Section 5(1) No. 10 Sentence 1 of the Corporation Tax Act (CTA)and will therefore be entitled to the tax exemption (Section 5(1) No. 10 Sentence 5 CTA).

Ministry of Finance draft bill on the Implementation of the Anti-Tax Avoidance Directive (ATAD Implementation Act) circulated for consultation purposes

On 10 December 2019, the Federal Ministry of Finance (MoF) circulated a draft bill on the Implementation of the Anti-Tax Avoidance Directive (ATAD Implementation Act) to various federations and associations 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 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 pre-empted.

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. As was the case previously, land tax will be calculated in a three-step valuation procedure, which is aimed at determining the “actual” value of real estate for the purposes of land tax.

Tax Court Cases

Inheritance Tax: spousal residence exemption

According to the Supreme Tax Court in its judgment of 11 July 2019 – (II R 38/16), published on 28 November 2019, the inheritance tax exemption on the inheritance a family home by the surviving spouse or civil partner will not apply retroactively where the surviving spouse/partner transfers ownership of the family home to a third party within ten years of acquisition. This will also be the case where the surviving *spouse/partner continues to use the home for residential purposes under the terms of a lifetime interest.*

Background

After the death of her husband, the plaintiff had inherited the jointly occupied family home and had remained in it. One and a half years after the inheritance, she gave the house to her daughter. She retained a lifelong interest to live in the house and did not move out. As a result, the tax office revoked the tax exemption under Section 13 (1) no. 4b of the Inheritance Tax and Gift Tax Act (IHTGA) retroactively because the plaintiff had given away the family home.

Judgment

Subject to the specified conditions, Section 13 (1) No. 4b IHTGA exempts from inheritance tax, the transfer on death of the family home (or a co-ownership in it) to the surviving spouse or life partner. For these purposes the family home is a parcel of built-up land on which the deceased occupied an apartment or a house for his or her own residential purposes up to the time of death. The property must be designated immediately to the heir "for his own use for his own residential purposes". Following any event giving rise to the subsequent taxation, the tax exemption will be revoked retroactively. This will apply where the heir no longer uses the family home for his own residential purposes within a ten-year period following the inheritance; the exemption should not be revoked where it can be shown that there are compelling reasons preventing the heir from "using it for his own residential purposes".

Both the lower court and the Supreme Tax Court confirmed the retroactive revocation of the tax exemption. In the introduction of the tax exemption, the intention of the legislator had been to protect the living space of the family and promote the attainment by families of residential property. Accordingly, only those surviving spouses or life partners, who become the owners of the real estate and actually live there may apply the exemption. If within ten years of the inheritance the heir no longer lives in the property, the exemption is revoked with retroactive effect. The same applies where the heir is no longer the owner of the property. If this rule did not exist, a property could be inherited tax-free and resold a short time later. This would run counter to the stated objective of the promotion of home ownership. If the intention were only to link the exemption to the use of the property with the ten-year period, the provision could have been worded more simply, such as "own-use for residential purposes" or "use for own residential purposes" . The term "own-use for own residential purposes" used in the provision suggests that both the use and the ownership status of the surviving spouse or civil partner would have to be maintained during the ten-year period.

Source:
Supreme Tax Court judgment of 11 July 2019 – (II R 38/16), published on 28 November 2019.

VAT-free sale of endowment policies on the secondary endowment policy market

In its judgment of 5 September 2019 (VR 57/17) published on 5 December 2019, the Supreme Tax Court held that the transfer for consideration of endowment policies on the secondary endowment policy market is exempt from VAT

Background

The appellant was a public limited company which acquired endowment policies taken out by private individuals. The purchase price was above the so-called surrender value, but below the paid-in insurance premiums. Subsequently, the appellant amended the insurance contracts by terminating the supplementary insurances – which were irrelevant for the maturity value – and converting the premium payment plan to an annual payment basis. It then sold its rights to these now modified endowment policies to various funds. In the year in dispute (2007), the appellant treated its turnover on the transfer of the endowment policies as VAT-exempt. The tax office took the view that the sale of endowment policies on the secondary market constituted a single taxable supply. The VAT base of the supply of the service was the purchase price paid by the fund. The court at first instance dismissed the appeal.

Judgment

In contrast, the Supreme Tax Court set aside the judgment of the tax court and upheld the appeal. In its view the supplies constituted VAT exempt supplies with receivables under Section 4 No. 8 letter. c of the VAT Act.

By the sale of its rights to and obligations from the modified endowment policies, the appellant was supplying a single service. The transfer of the (future) claim (i.e. the maturity benefit) was to be regarded as the main service because buyers on the secondary endowment policy market (the funds) were only interested in the savings component of the policy.

The decision of the Supreme Tax Court has a considerable effect on the business model purchase/sale of "second-hand" endowment policies. The charge to VAT proposed by the tax authorities and the tax court would have nullified the whole business model.

Source:
Supreme Tax Court judgment of 5 September 2019 – V R 57/17 – published on 5 December 2019.

News in brief	
Proof of VAT-exempt intra-Community supplies	For the purposes of establishing whether an VAT-exempt intra-Community supply had been made, where other evidence exists establishing that the motor vehicles had been sent to their destination in the other EU country, the assumption of the absence of documentary evidence could not contradict such other evidence. The proof of the customer's entrepreneurial status resulting from the VAT ID number cannot be refuted by the mere assumption of a letterbox address. https://blogs.pwc.de/german-tax-and-legal-news/2019/12/10/proof-of-vat-exempt-intra-community-supplies/
Referral to European Court of Justice: VAT exemption for the development and brokerage of insurance products	Does an insurance broker, who makes- in addition to his brokerage activities -a brokered insurance product available to an insurance company, provide VAT-exempt services? The Supreme Tax Court considered this doubtful and decided on 5 September 2019 (V R 58/17), to refer the question to the Court of Justice of the European Union (ECJ) for a preliminary ruling. https://blogs.pwc.de/german-tax-and-legal-news/2019/12/12/referral-to-european-court-of-justice-vat-exemption-for-the-development-and-brokerage-of-insurance-products/
Bundesrat approves the Act on the Tax Promotion of Research and Development (Research Subsidy Act).	On 29 November 2019, the Bundesrat approved the Act on the Tax Promotion of Research and Development (Research Subsidy Act). The statute will come into force on 1 January 2020 initially for a 6-month period. https://blogs.pwc.de/german-tax-and-legal-news/2019/12/02/bundesrat-approves-the-act-on-the-tax-promotion-of-research-and-development-research-subsidy-act/
New Finance Ministry circular on standards for the proper keeping and storage of books, records and	On 28 November 2019 the Federal Ministry of Finance (MoF) issued a revised circular on standards for the proper keeping and storage of books, records and documents in electronic form and for data access (here "GoBD") – (IV A 4 – S 0316/19/10003 :001 (2019/0962810)

documents in electronic form and for data access	https://blogs.pwc.de/german-tax-and-legal-news/2019/12/04/new-finance-ministry-circular-on-standards-for-the-proper-keeping-and-storage-of-books-records-and-documents-in-electronic-form-and-for-data-access/
Waiver of exit tax upon return to Germany	According to Section 6 (1) of the Foreign Taxes Act (FTA), where a taxpayer's unlimited tax liability ceases through the taxpayer giving up his German residence/habitual abode, any material shareholdings held in his private property will be deemed as disposed of even without a sale and any capital gain on the deemed disposal will be taxable under Section 17 (1) of the Income Tax Act (ITA). Section 6 (3) FTA provides for this so-called exit tax to be subsequently waived in certain circumstances. The Münster Tax Court held that in addition to the (objective) re-establishment of the unlimited tax liability (i.e. the re-establishment of the German residence/habitual abode), it was also necessary for the taxpayer to provide credible evidence that the will to return existed (subjectively) upon departure. https://blogs.pwc.de/german-tax-and-legal-news/2019/12/04/waiver-of-exit-tax-upon-return-to-germany/

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