Issue Q1

April 2022

Tax & Legal News

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Tax Court Cases

Federal Constitutional Court - 1 BvL 1/13: Tax privilege granted for income from business profits over income from surpluses in 2007 unconstitutional

8 January 2022

In a recent decision, the Federal Constitutional Court held that the favorable tax treatment of income from trade or business, self-employment, agriculture, and forestry (so called ‘profit income’) versus taxable income computed on a cash-basis (“surplus income”) to be unconstitutional. This privileged tax treatment of income from profits, which only applied for 2007, is considered by the court as unequal and thus not justified

MORE INFORMATION

Supreme Tax Court - I R 22/20: Cum-ex deal rejected by Supreme Tax Court for want of beneficial ownership of shares

15 March 2022

In a recently published decision, the Supreme Tax Court dealt with so-called cum-ex share transactions. In its judgment the court rejected a “business concept” that sought to “exploit” uncertainties in the clear economic allocation of shares in such a way that withholding tax once withheld might be credited or refunded by the tax authorities twice or even more times.

MORE INFORMATION

Supreme Tax Court - IX R 8/20: Maintenance of separate work room not required for deduction of home-working costs

24 March 2022

In a case before the Supreme Tax Court the question was raised as to whether home office costs could be accepted as potentially leading to tax deductible expense, even if the work was completed in any room at home. The Supreme Tax Court held that a deduction of home-working expenses does not require that a specific office is maintained for the taxpayer’s employment activity. It is sufficient if the room is used exclusively or almost exclusively for business/professional purposes.

MORE INFORMATION

Official Pronouncements

Further extension of declaration deadlines for the 2020 taxable period by the Fourth Corona Tax Relief Act.

On 31 March 2022, the German Federal Ministry of Finance (MoF) published a circular in relation to the further extension of the tax declaration deadlines for the 2020 period of assessment proposed by the Fourth Corona Tax Assistance Act.

In view of the continuing exceptional situation caused by the Corona pandemic, the declaration deadlines for tax declarations listed in Section 149 (3) of the General Tax Code(GTC) and the interest-free grace periods (Section 233a (2) GTC) for 2020 are to be extended by a further three months by the Fourth Corona Tax Assistance Act. In anticipation of this statutory regulation, the Federal and State Tax Authorities have issued various instructions.

The present MoF circular supplements the MoF circular of 20 July 2021 Accordingly, in anticipation of the statutory regulation, the following applies:

tax returns (under Section 149 (2) GTC) which are submitted for the 2020 assessment period after the expiry of the applicable declaration deadlines but before the Fourth Corona Tax Assistance Act comes into force, will not be subject to a late filing penalty under Section 152 (2) GTC.
tax returns prepared for the 2020 assessment period by members of the tax advisory professions (Section 149 (3) half-sentence 1 GTC) and submitted after 31 May 2022 but before the entry into force of the Fourth Corona Tax Assistance Act, shall not be considered to be late within the meaning of Section 152 (1) GTC- unless the tax authorities have ordered an earlier submission of the tax returns under Section 149 (4) GTC.

Source:
Ministry of Finance circular dated 01 April 2022, (IV A 3 -S 0261/20/10001 :016).

Federal Ministry of Finance publishes Tax Relief Bill 2022

Following the release on 23 February 2022 by the Committee of the Coalition Government of a paper entitled “10 Steps to Relieve our Country”, the Federal Ministry of Finance published the draft Tax Relief 2022 bill on 2 March 2022. On 28 March 2022, the Committees to the Bundesrat published additional proposals.

Draft Bill

The draft bill seeks to enact several of the measures proposed in the“10 Steps to Relieve our Country” paper, namely:

- The lump-sum deduction from employee income will be increased by € 200 to €1,200 applying retroactively from 1 January 2022;
- The personal basic tax-free allowance for 2022 will be increased from € 9,984 to €10,347 applying retroactively from 1 January 2022;
- The increase in the commuter allowance from €0.35 to € 0.38 (for each kilometre travelled over 20 KM) has been brought forward and will now apply retroactively from 1 January 2022. The increase is time limited and will cease in 2026.

  Among the proposals mentioned in the 10-Step paper but not included in the draft bill were:

- A proposal to abolish the renewable energy levy from 1 July 2022; and
- An extension of the short-time working allowance to 30 June 2022.

On **16 March 2022** the Tax Relief Act 2022 was approved at the federal cabinet's meeting.

On **28 March 2022** recommendations to the Bundesrat to be adopted at the Bundesrat session on 08 April 2022, the committees to the Bundesrat propose, inter alia:

- Inclusion of measures to mitigate the effects of cold progression;
- an increase in the commuting allowance to 38 cents applying immediately from the 1st kilometre;
- an adjustment of the mileage allowance for business-related travel to current price ratios;
- a reduction in the electricity tax rates set out in the Electricity Tax Act (StromStG) to the minimum level permitted by the EU; and
- a regular review and needs-based adjustment of the income-related expenses lump-sum allowance and the commuting allowance in line with rising energy prices.

Sources:

Ministry of Finance website

Bundesrat: Draft Bill Organised Tax Evasion

The draft bill is being (re-)introduced to combat serious tax evasion executed via organised - "gang"- structures. The current law is limited to organised evasion of VAT and excise duties

The bill had already been introduced in the Bundestag by the Bundesrat on 27 November 2020, but the procedure was discontinued at the end of the legislative period.

According to the original explanatory memorandum to the proposed legislation, organised tax evasion has increased for a wide range of tax types over recent years and has become a major feature of organized white-collar crime. The specific nature of the offence, which regularly goes far beyond "standard" tax evasion, is not currently reflected in the law for all types of taxes.

Section 370 (3) of the German Tax Code increases the prison sentence for serious tax evasion. In this regard Section 370 (3) Sentence 2 No. 5 GTC deals with organized tax evasion by gangs; however, it only applies to organised evasion of VAT or excise taxes. The explanatory memorandum pointed out that organized tax evasion, which can be classified as particularly serious, ceased long ago to be limited to certain types of offences, such as VAT carousels and organized excise tax evasion – such as alcohol and cigarette smuggling. By way of example, the memorandum notes, that cum-ex transactions and related tax arrangements have been systematically planned and carried out by professional market participants such as international investment banks.

There is concern that the highly professional and conspiratorial cooperation of the perpetrator groups makes it difficult to solve the crimes as the arrangements are purposefully concealed through the use of convoluted corporate structures, the relocation of organizational units abroad (often offshore), the involvement of trustees and various other service providers etc.

Accordingly, the present draft bill of the Bundesrat should extend Section 370 (3) Sentence 2 No. 5 GTC to all types of tax.

Source

Legislative proposal of the State of North Rhine-Westphalia, February 16, 2022, BR-Drs. 66/22.

German Federal Ministry of Finance (MoF) published two circulars in relation to the royalty limitation rules

On January 27, 2022, the German Federal Ministry of Finance (MoF) published two circulars in relation to the royalty limitation rules. The first deals with general questions of application of the rules, including, in particular, commentary in relation to “preferential regimes”, an examination of what constitutes conformity to the nexus approach and remarks on the allocation of the burden of proof. In the second circular, the MoF lists which international regimes will fall short of the necessary requirements in the 2018, 2019 and 2020 tax years.

In addition, the second circular also comments for the first time on special cantonal companies in Switzerland. Furthermore, it indicates that US FDII regime continues to be listed as a preferential regime the review of which is still ongoing.

The rules in brief

The royalty limitation rules (Section 4j Income Tax Act), which were introduced in 2017, restrict the deductibility of royalty expenses/licence payments where, the recipient of the income is a related party vis-à-vis the debtor and the income in the hands of the recipient is subject to a special preferential regime. A regime will be considered as preferential, where the tax treatment under it differs from the standard tax treatment and the income is taxed at a rate less 25 %. Where, however, the relevant regime is considered to correspond to OECD Modified Nexus Approach, a full deduction will be possible.

Preferential regimes

A preferential regime is considered to exist where the tax treatment applied differs from the standard treatment. According to the first circular this “difference” is established by comparing the treatment applied to the relevant income to the treatment of other income in the same state. In this regard:

The benchmark for “standard taxation” is the standard tax rate that would be applied to the income of taxpayer with a legal personality comparable to that of the relevant creditor;

It is irrelevant whether the taxpayer must make an application to participate in the regime;

It is not necessary for the regime only to apply to royalty income nor must it be limited to so-called “intellectual property” (IP) regimes such as license boxes, IP boxes or patent boxes.

So-called “tax rulings”, i.e. individual agreements between foreign tax authorities and recipients of royalty payments, can also fall within the royalty limitation rules.

With regard to what constitutes low taxation, the amount of tax legally owed tax, will not be relevant but rather the tax actually levied and paid. Any subsequent refund claims will also be taken into account. Furthermore, refunds available to other taxpayers may also be considered in calculating the tax rate. This will be the case where the shareholder of the royalty recipient is entitled to a tax refund following a dividend receipt.

A general low rate of taxation in the creditor’s country of tax residence will not per se lead to the assumption that a preferential regime exists. Rather, the low level of taxation must constitute a deviation from standard taxation;

Where the royalty income is attributed in whole or in part to a person other than the creditor or where tax is (also) levied on another, the total tax burden will be considered.

Nexus conformity

The circular refers to the analyses of international preferential regimes performed by the Forum on Harmful Tax Practices (FHTP) of OECD. These are split into two categories, namely the analysis of IP-Regimes and the analysis of other preferential regimes. Only regimes in the former category will be examined by the FHTP for their nexus conformity. The second circular issued by the MoF in connection with the royalty limitation rules on 6 January 2022 contains the FHTP’s non-exhaustive list of preferential regimes not considered to have adopted the nexus approach in the years of assessment 2018 to 2020.

Where the FHTP has not performed a nexus-conformity analysis, e.g. where the regime is in the category of “other preferential regime” or where the royalty payment forms part of a “tax arrangement,” the question of nexus-conformity will be investigated as part of the normal tax assessment process.

Burden of proof

Finally, the circular comments on the burden of proof. General principles will apply, namely that the tax authorities bear the burden of proof for facts which increase the tax burden whereas the taxpayer bears the burden of proof for facts which reduce it. This means that the tax office must prove the existence of a preferential arrangement or lower taxation, although the use of the FHTP analyses may be sufficient for this purpose.

The taxpayer is not only required to prove that the license expenses are deductible as a business expense and that any preferential regime is nexus-compliant, but also has additional obligations to cooperate and provide evidence under the provisions of the General Tax Code due to the international element.

It is, however, open to the taxpayer to prove that an existing preferential regulation does not apply or to provide evidence for standard taxation, e.g. by means of a foreign tax assessment notice and the calculations on which it is based, a confirmation of the foreign tax authority, etc. Where the FHTP has confirmed that a regime is nexus-compliant, the taxpayer will not be obliged to provide further evidence.

Source;

Questions on the Application of Section 4j ITA - IV C 2 -S 2144-g/20/10002 :007 (5 January 2022)

Rules of Application (non-conforming preferential regimes) - Section 4j ITA - IV C 2 -S 2144-g/20/10002 :005

From Europe

ECJ: Withholding tax on notional interest in case of interest-free loans compatible with EU law

In a Bulgarian case the European Court of Justice (ECJ) held that EU law does not preclude national legislation imposing withholding tax on notional market-based interest (mandated under local tax anti-avoidance rules). Such withholding tax cannot be exempt under the regimes of the IRD (EU Interest – Royalty Directive 2003/49/EC) and the PSD (EU Parent-Subsidiary Directive 2011/96/EU) as there have been no actual payments of interest.

Background

In the case of dispute, a Bulgarian company received an interest-free convertible loan with a 60-year maturity from its EU-based sole shareholder. Under the loan arrangement, the Bulgarian borrower could waive the obligation to repay the loan if at any time after the date of financing the outstanding loan is converted into capital of the Bulgarian subsidiary. Pursuant to the Bulgarian tax regulations interest-free loans and loans deviating from the relevant market conditions are considered tax avoidance by way of an irrebuttable presumption. Hence, the Bulgarian tax authorities assessed 10% withholding tax on a notional market interest that should have been payable to the shareholder.

ECJ decision

The ECJ noted that there was unequal treatment here, which constitutes a restriction on the free movement of capital pursuant to Art. 63 TFEU. However, this infringement is justified in the opinion of the court since retention at source is a legitimate and appropriate means of ensuring the tax treatment of the income of a taxable person established outside the State of taxation and an appropriate measure to prevent tax evasion.

The ECJ went on to say that EU Member States may adopt measures to prevent and combat of tax evasion/tax avoidance, as far as these are proportionate and justifiable in terms of the objectives to be achieved. This includes taxation at source of notional interest on interest-free loans granted by foreign companies or foreign shareholders. As far as the Bulgarian case is concerned the ECJ pointed out that this national legislation must therefore be regarded as capable of safeguarding a balanced allocation between the Member States of the power to impose taxes and ensuring the effective collection of tax in order to prevent tax avoidance.

On the question whether the Bulgarian legislation goes beyond what is necessary to achieve those objectives, Viva Telecom Bulgaria claimed that the duration of the recovery procedure provided for in the statutes is excessive, since a possible refund of excess withholding tax paid by a resident company on the gross amount of notional interest relating to an interest-free loan granted by a non-resident company may occur only after three years have elapsed. However, subject to the checks to be carried out by the referring court, it is apparent to the ECJ from the explanations provided by the defendant that such refund is made, as a general rule, within a period of 30 days from the date on which the application was made and that it is only in exceptional cases that the procedure may last up to three years. In light of the duration of the general recovery procedure taking up to 30 days, the Bulgarian legislation does not appear to go beyond what is necessary to attain the objectives that it pursues.

Source:

The ECJ case reference is C-257/20 Viva Telecom Bulgaria judgment of 24 February 2022. – The complete ECJ-decision to be found here.

Documentation requirements for refund of withholding tax on portfolio dividends of foreign shareholders in breach of EU law?

in his Opinion of 20 January 2022, the Advocate General (AG) suggests to the European Court of Justice (ECJ) that Germany's requirements for withholding tax claims filed by non-resident corporate taxpayers with seat or place of management in the EU or EEA are too strict in two respects and thus in violation of Article 63 TFEU on the free movement of capital.

In his Opinion of 20 January 2022, the Advocate General (AG) suggests to the European Court of Justice (ECJ) that Germany's requirements for withholding tax claims filed by non-resident corporate taxpayers with seat or place of management in the EU or EEA are too strict in two respects and thus in violation of Article 63 TFEU on the free movement of capital.

In response to the ECJ decision in the case Commission vs. Germany (C-284/09), the German legislator in 2013 introduced a law according to which non-resident corporate income taxpayers, whose shareholding in the distributing German company is too small to benefit from the Parent-Subsidiary Directive (i.e., below 10%) can claim a withholding tax reduction to 0% if the requirements of the new procedural rules are met.

In summary, the AG confirms the doubts raised in a referral by the Regional Tax Court of Cologne as to the compatibility of the German provisions with EU law and sees an infringement of Article 63 TFEU on the free movement of capital, since said documentation is not required from a company domiciled in Germany for the purpose of reimbursement of capital gains tax in the case of the same amount of shareholding. This difference in treatment can only be justified if it either concerns situations which are not objectively comparable or if it is justified by an overriding reason in the general interest. However, this could not reasonably be assumed to be the case here.

Two conditions of the 2013 law are questionable in the case at hand, in which a UK company, owning 5.26% of the shares in a German company, received dividends in the years 2006-2008 from the latter company and now claims a withholding tax reduction from 15% (tax treaty level) to 0%.

First, as regards the requirement that the German withholding tax was neither credited against taxes levied by the residence state of the shareholder or its direct or indirect shareholder(s), nor deducted as expense by any of the said companies, the AG is of the view that it restricts the free movement of capital (Article 63 TFEU).

This is because in a purely domestic situation no such requirement existed. In 2006-2008, the dividend was tax exempt at the level of the German shareholder who, in addition, got a credit for the withholding tax. According to the AG, the restriction cannot be justified by the balanced allocation of taxing rights between Member States or the need to avoid that withholding tax be taken into account twice. Germany must refund the withholding tax unless the tax treaty ensures that it is fully credited in the residence state of the shareholder.

Secondly, non-resident taxpayers must provide a certificate issued by the authorities of their residence state which proves that no credit or deduction was granted at the level of any direct or indirect shareholder. AG Collins considers this requirement to be disproportionate because it can be “practically impossible” to meet.

Source:

ECJ case reference C-572/20, ACC Silicones – Opinion of 20 January 2022.

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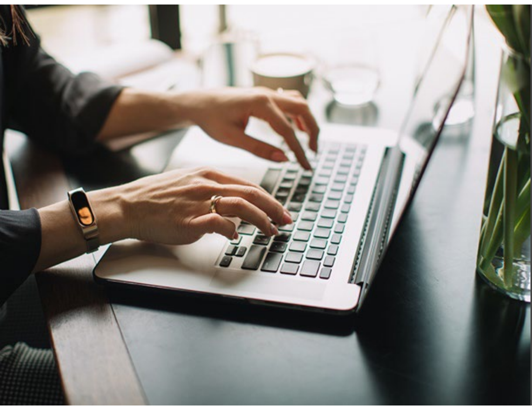

News in brief

tax & legal blog

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