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By PwC Deutschland | 05. September 2023

Federal Cabinet approves government draft of the Growth Opportunities Act

At its closed-door meeting in Meseberg on 30.8.2023, the Federal Cabinet adopted the government draft for a law to enhance growth opportunities, investment, and innovation as well as tax simplification and tax fairness (Growth Opportunities Act).

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The government draft that has now been passed differs in parts from the draft bill as of 14 July 2023 (see our **Newsflash** of 18 July 2023). The main adaptations are shown below.

Tax incentives for investments in climate protection

With regard to the planned introduction of a non-profit-dependent investment premium, the present government draft provides favourable changes leading to an expansion of the scope of application.

In contrast to the draft bill of 14 July 2023, the **minimum amount** for the grant of the investment premium under Section 2(3) of the draft Climate Investment Act is to be reduced from the previous EUR 10,000 to **EUR 5,000.**

In addition, the government draft provides for an **extension of the eligibility period** by two years. The investment premium will now be granted for a limited period for investments made by the applicant after 31 December 2023 or (at the earliest) after the publication date of the Growth Opportunities Act and completed before 1 January 2030 (previously 1 January 2028). Investments completed at a later date will only be eligible if partial production costs were incurred or advance payments on acquisition costs were made before 1.1.2030 (previously 1.1.2028) (Section 3 Climate Investment Premium Act - Draft).

Against the background of the extension of the eligibility period, the entitlement to the investment premium in relation to partial production costs incurred or advance payments made on acquisition costs of a privileged investment before 1 January 2030 (previously 1 January 2028) will not begin until 31 December 2029 (previously 31 December 2027) (Section 5 (2) Climate Investment Premium Act - Draft). Similarly, in addition to the proven acquisition and production costs in the eligibility period, partial production costs and advance payments made on acquisition costs incurred before 1 January 2030 (previously 1 January 2028) should also be included in the eligible expenditure (Section 4 (1) Climate Investment Premium Act - Draft).

In total, i.e. taking into account the investment premium together with other state subsidies and aid, **no more than EUR 30 million** in aid may be granted per applicant in connection with a eligible investment project (Sections 4 (4) and (6) Climate Investment Premium Act - Draft). In contrast to the draft bill, the other subsidies and aid to be considered here are no longer include restricted to those for environmental protection.

With regard to the **income tax treatment** of the investment premium, the government draft now provides on the one hand that the acquisition or production costs as reduced by the investment premium are to be decisive not only for the depreciation for wear and tear pursuant to Section 7 ITA, but also for the increased depreciation and for any special depreciation. On the other hand, it is envisaged that the investment premium - insofar as it exceeds the residual book value at the time of its determination - is to be recognised as an increase in profit.

In contrast to the earlier draft bill, a maximum of four and no longer only two applications for investment premiums per applicant may now be submitted to the tax office responsible for the taxation of the applicant. Furthermore, the relevant **minimum assessment base** for the relevant application was reduced from EUR

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50,000 to **EUR 10,000** (Section 5 (1) Climate Investment Act-Draft).

According to the newly inserted Section 10 (2) Climate Investment Premium Act - Draft, **the terms** used in the Climate Investment Premium Act, which have been taken from **income tax law**, are to be interpreted in accordance with the principles applicable to income taxation.

Amendments to the Income Tax Act

Changes to the interest limitation rule

While the draft bill dated 14 July 2023 still provided for very far-reaching changes to the interest limitation rule – going beyond an adjustment to the requirements of the ATAD (Council Directive (EU) 2016/1164 of 12 July 2016) - the government draft now only provides for selective adjustments.

In contrast to the draft bill, the exemption limit of **EUR 3,000,000** is not to be converted into a tax- free allowance but will remain an exemption limit. The other grounds for exclusion from the application of the interest limitation rule under Section 4h (2) ITA (absence of or only proportionate affiliation to a group, equity escape clause) are also to be retained with adjustments. All three exceptions should no longer be applicable in the future insofar as the interest expenses of a year were increased due to an interest carry-forward from previous years. As a result, an interest carry-forward will only be deductible if sufficient EBITDA is available for set off.

With regard to the exemption limit of EUR 3,000,000, the government draft, like the draft bill, provides for the introduction of an anti-fragmentation regulation, according to which the exemption limit is only jointly available to similar businesses that are under uniform management or controlling influence by one person or group of persons.

The get-out clause in cases of an absence of group affiliation will be replaced by a narrower "stand-alone clause", which provides for non-application of the interest limitation where the taxpayer does not have a related party within the meaning of section 1 (2) Foreign Taxes Act and the taxpayer does not have a permanent establishment outside its state of residence. The current requirements for the application of the exclusion rule for corporations as regards shareholder financing in Section 8a (2) CTA will be deleted, as they are no longer necessary due to the new regulation.

According to the government draft, the equity escape for group-affiliated companies is to be retained. In future, a company will be able to claim it as a group company if it is consolidated with one or more other companies according to the accounting standard relevant for the equity escape (as a rule this will be IFRS). Corporations must also comply with the regulations on shareholder financing in Section 8a (3) CTA. On the one hand, these regulations are to be adapted to the requirements of the ATAD by lowering the relevant participation limit to "at least 25%" of the capital from the previous "more than 25%". In addition, the wording is to be adjusted in reaction to a ruling of the Supreme Tax Court of 11 November 2015 (I R 57/13, BStBl. II 2017, 319), according to which remuneration on loans from each of the individual qualified shareholders were not to be summated when calculating whether the 10% limit for harmful shareholder debt financing had

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been reached. The new wording adopts the previous interpretation of the tax authorities so that, when calculating of the 10% limit, the aggregated remuneration on loan capital paid to all qualifying shareholders is relevant.

The widening of the definition of the term “interest” to meet the requirements of the ATAD as provided for in the draft bill remains unchanged in the government bill. This also applies to the exemption from the interest limitation rules for interest expenses or interest income emanating from certain loans used to finance long-term public infrastructure projects and granted from public funds on the basis of general funding conditions. Furthermore, the extension of events triggering a forfeiture of an EBITDA carry-forward or an interest carry-forward on a partial business discontinuation or transfer have also found their way into the government draft.

In contrast to the draft bill, which foresaw the application of the new regulations for the assessment period 2024 onwards, the government bill provides for a first-time application of the amended regulations for financial years which begin on the day of following the passing of the law by the German Bundestag, but which do not end before 1 January 2024.

Interest expense rate restriction

The regulations on the restriction of interest expense rates (Section 4l ITA Draft) already provided for in the draft bill as a further measure to limit the deduction of interest expenses remain essentially unchanged in the government bill.

Subsection 2 was added in the government draft to cover situations where a change in the interest base rate under Section 247 (1) Sentence 2 German Civil Code occurs after the conclusion of an agreement. In such cases, the interest expense deduction will only be restricted following the expiry of one month following the date the change in the interest base rate under Section 247 (1) Sentence 2 German Civil Code takes effect. This relaxation of the rule will only apply where the agreed interest rate only exceeds the maximum rate because of the change in the base rate.

The regulation restricts the deduction of interest expenses on loan agreements between related parties within the meaning of Section 1 (2) Foreign Taxes Act and is restricted to cases in which the creditor does not engage in any substantial economic activity in the state in which it has its registered office or its management or where the state in which the creditor has its registered office or its management is a state which is not obliged to provide administrative assistance within the meaning of Section 4 (2) No. 2 in conjunction with Subsection 4 Sentence 1 of the Act Combatting Tax Avoidance and Unfair Tax Competition. In contrast to the draft bill, the explanatory memorandum to the government bill now adds that the “substantial economic activity” should have a connection to the specific financing transaction. According to the explanatory memorandum, this requires in particular that the creditor either has the ability and authority to actually control the risk of the specific financing transaction or to bear it. The basic prerequisite for this should be that the decision-makers have the necessary experience and competence and have access to adequate information.

In addition, the explanatory memorandum now states that, in the case of a financing relationship affected by

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the regulation, the agreement of an interest rate not exceeding the maximum rate under Section 4l (1) Sentence 2 ITA does not lead to a hidden profit distribution merely because a higher interest rate would have been agreed between the debtor and the creditor had the effects of Section 4l ITA not been taken into account .

The explanatory memorandum establishes the option for the taxpayer to prove that all other things being equal, neither the creditor nor the ultimate parent company would have been able to obtain the loan capital at an interest rate lower than the maximum allowable rate. Thus the refinancing rate of the ultimate parent company or database studies at the level of the ultimate parent company at the time of the conclusion of the financing relationship under investigation may be considered as evidence. Offers from banks or other potential creditors, on the other hand, should not be sufficient. If evidence is provided, the maximum rate should be the most favourable interest rate that the creditor or the ultimate parent company could have obtained.

In contrast the draft bill, which provided for application of the provision from the 2024 assessment period, the government bill provides for the first-time application of the new regulation for interest expenses incurred after 31 December 2023.

Revision of the regulations on the so-called reinvestment allowance

The creation of a "back-taxation-free withdrawal volume" for profits retained but subsequently withdrawn, which was declared in the draft bill as a significant improvement of the rules relating to reduced tax rates for retained profits in Section 34a ITA -, is no longer included in the government draft. The deletion of Section 37 (3) Sentence 5 ITA is also no longer planned, so that it will not be possible to take into account the tax reduction according to Section 34a ITA in the prepayment procedure in future either. Of the originally planned improvements, only the increase of the profit eligible for tax relief by the amount of the trade tax of the business year and by any withdrawals (limited to the amount of the income tax and solidarity surcharge payable on the retained profit) remains.

In contrast, the planned amendments to tighten the rules (e.g. treatment of a subsequent application as a retroactive event; introduction of a - pro rata - back taxation in the case of partial transfers for consideration as well as in the case of gratuitous transfers to corporate income tax subjects; pro rata transfers of the back taxation amount in the case of gratuitous partial transfers to the legal successor) remain unchanged from the draft bill - apart from a few editorial adjustments and changes in wording.

Changes to the tax loss deduction (Section 10d ITA)

As already envisaged in the draft bill, the rules for loss carry-back are to be extended from the 2024 assessment period so that negative income can be carried back to the third period of assessment preceding the year of loss and deducted (within the limits of the minimum taxation) from the amount of total income. In addition, the maximum amounts of EUR 10,000,000 or EUR 20,000,000 (for joint taxpayers) - relevant for the minimum taxation and originally only temporarily increased in the Corona crisis - are now to be retained for the loss carry-back beyond the 2023 period of assessment (Section 10d (1) sentence 1 ITA-Draft).

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In contrast, the temporary abolition of the minimum taxation rule (for the tax years 2024-2027) contained in the draft bill is no longer provided for in the government bill. Instead, the minimum taxation is made somewhat more generous for a limited period by allowing the deduction of a loss carry-forward up to a total amount of income of EUR 1,000,000 without limitation and beyond that up to 80% (previously 60%) of the total amount of income exceeding EUR 1,000,000 (Section 10d (2) Sentence 1 ITA-Draft). The amendment will apply from the 2024 period of assessment and will be withdrawn with effect from the 2028 assessment period of assessment (section 52(18b) sentences 3 and 4 ITA-Draft).

Further changes in the ITA

- According to **Section 6 (1) No. 4 Sentence 2 No. 3 and Sentence 3 No. 3 ITA,** only a quarter of the gross list price is to be taken into account as the taxable benefit for the private use of a purely electric vehicle. The government draft provides for an increase in the maximum list price of purely electric vehicles acquired before 1 January 2031 from the previous EUR 60,000 to **EUR 80,000** for vehicles acquired after 31 December 2023 (Section 52 (12) ITA-Draft).
- In contrast to the draft bill, the government bill provides for a temporary reintroduction of the **declining balance depreciation** for movable fixed assets acquired or manufactured after 30 September 2023 but before 1 January 2025 (Section 7 (2) sentence 1 ITA-Draft), in the amount of 25% but no higher than 2.5 times the straight-line depreciation. This was previously extended by the Fourth Corona Tax Assistance Act.
- The government bill further provides for the introduction of a **declining balance depreciation** of 6% for residential buildings if the construction was started after 30.9.2023 but before 1.10.2029 or the acquisition is based on a mandatory contract concluded with legal effect after 30.9.2023 and before 1.10.2029 (Section 7 (5a) ITA-Draft). If the option of declining-balance depreciation is used, deductions for extraordinary technical or economic wear and tear are not permitted. In contrast to declining-balance depreciation under section 7 (5) ITA, a corresponding application of Section 7 (1) Sentence 4 ITA is mandatory, so that depreciation must be made pro rata temporis in the year of acquisition or production.

Amendments to the Trade Tax Act

Extended property reduction

As in the draft bill, in relation to the extended deduction for real estate under Section 9 No. 1 Sentences 2 et seq. Trade Tax Act, the threshold for harmless ancillary income from the operation of plants for the generation of electricity from renewable energies as well as from the operation of charging stations for electric vehicles and electric bicycles is to be raised from 10% to 20% of the income from the transfer of real property (Section 9 No. 1 Sentence 3 Letter b Trade Tax Act - Draft). The amendment is to be applicable from the 2023 period of assessment.

Trading loss (section 10a Trade Tax Act)

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The temporary suspension of the minimum taxation rule in the assessment periods 2024 - 2027, which was still provided for in the draft bill, is no longer included in the government bill.

Instead, as in the ITA, the provisions on minimum taxation are more generous to the effect that trading income exceeding EUR 1,000,000 is to be reduced by up to 80% (instead of the previous 60%) by unutilised trading losses of preceding assessment periods (Section 10a sentence 2 Trade Tax Act - Draft). The new regulation is to apply - in parallel with the new regulation in the ITA - for a limited period for the assessment periods 2024 - 2027.

Amendments to the Real Estate Transfer Tax Act

In contrast to the draft bill, the government bill now also provides for changes in the Real Estate Transfer Tax Act (RETTA).

With a new Subsection 25, a transitional provision is to be introduced in Section 23 RETTA to ensure that the retention periods for tax-exempt transfers from or to a joint holding *("Gesamthand")* made in the past according to Section 5 (3) Sentence 1, Section 6 (3) Sentence 2 and Section 7 (3) Sentence 1 RETTA are not automatically seen as breached following the extensive abolition of the concept of the joint holding of assets *("Gesamthandvermögen")* by the Act to Modernise the Law on Partnerships with effect from 1 January 2024 onwards. For this purpose, the assets of the company will be used as a point of reference instead of the assets of the joint holding.

An almost identical regulation had been included in the discussion draft for a law amending the Real Estate Transfer Tax Act (cf. our **Blog** of 10 July 2023). It is currently not clear whether the transfer of this transitional provision into the draft of the Growth Opportunity Act means that the introduction of the updated provisions for tax concessions in Sections 5 and 6 RETTA (transfers of real estate from or to companies after 31 December 2023) as provided for in the discussion draft are either no longer being pursued or just being delayed. This also applies to the amendment of the taxation of share deals and the so-called group clause envisaged in the RETTA discussion draft.

Amendments to the Reorganisation Tax Act

Section 15 (2) Sentence 2 et seq. Reorganisation Tax Act ("RTA") - the post-demerger divestment prohibition- is to be amended in response to the Supreme Tax Court ruling I R 39/18 of 11.8.2021.

In addition to the amendments to Section 15 (2) RTA already provided for in the draft bill, the present government bill provides for the introduction of a new Sentence 7, which, according to the explanatory memorandum, is intended to create a group exemption from the post-demerger divestment prohibition corresponding to Paragraph 15.26 of the 2011 Reorganisation Tax Decree. According to this, affiliated companies within the meaning of section 271 (2) of the Commercial Code are not to be considered external parties for the purposes of Section 15 (2) RTA. Intra-group restructurings in connection with or following the demerger would therefore not constitute an event triggering a breach of the prohibition period. In order to prevent avoidance, the second half-sentence of Sentence 7 provides that the indirect sale of a share in a

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corporation involved in the demerger to external parties shall also be detrimental. However, Sentence 7 does not contain a restriction of this provision to disposals that occur after an intra-group restructuring - unlike Paragraph 15.26 of the 2011 Reorganisation Tax Decree.

Pursuant to the application provision in Section 27 (19) RTA-Draft, the amendments provided for in Section 15 (2) RTA-Draft and newly included in the government draft are to be applied for the first time to demergers for which the application for registration in the commercial register - relevant for the effectiveness of the respective transaction - is made after 14 July 2023.

Changes in VAT

In the area of VAT, the introduction of the mandatory electronic invoice for services between entrepreneurs (B2B) is the most relevant change.

For businesses with a total turnover of up to EUR 800,000 in the previous calendar year, the transitional regulation, according to which paper invoices or - subject to the consent of the recipient - invoices in any electronic format can be used instead of the e-invoice, has been extended by a further year in comparison to the draft bill, i.e. until 31 December 2026 (Section 27 (39) no. 2 VAT Act -Draft).

Furthermore, in a new Section 14 (6) Sentence 2 VAT Act -Draft, the government draft authorises the Federal Ministry of Finance to issue ordinances. This should enable the Federal Ministry of Finance, with the consent of the Bundesrat, to issue more detailed provisions on the design of the structured electronic format of an electronic invoice by ordinance in order to simplify the taxation procedure. According to the explanatory memorandum to the government draft, this is intended to enable potential amendments to the VAT Directive regarding the requirements for electronic invoices and adaptations to the CEN format EN 16931 to be implemented at short notice, as well as changes to the future reporting system.

Amendments to the Research Grants Act

With regard to the Research Grants Act, the government draft contains the following changes compared to the draft bill:

Section 3 (3) Sentences 2 and 3 Research Grants Act – Draft: In order to make the research allowance more attractive to sole proprietors, the eligible value of own contributions worked is to be increased from currently EUR 40 per hour to EUR 70 per hour. A corresponding increase to the maximum hourly rate for eligible expenses in relation to co-entrepreneur activity agreements is also to be made.

Section 3 (3a) Research Grants Act - Draft The expansion of eligible expenses already provided for in the draft bill is to apply only to depreciable movable fixed assets acquired or produced after 31 December 2023. For this purpose, the asset must only be necessary for the research project and no longer indispensable.

Section 4 (1) Sentence 2 Research Grants Act - Draft The research allowance for certain small and medium-sized enterprises within the meaning of the General Block Exemption Regulation is to be increased from 25% to 35%.

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Introduction of a notification requirement on domestic tax arrangements (Section 138l et seq. General Tax Code)

Various changes to the provisions on the reporting obligations regarding domestic tax arrangements have been included in the government bill, some of which are substantive and some of which are editorial.

Particularly noteworthy are the changes to the factual reporting obligation in Section 138l General Tax Code-Draft. For domestic tax arrangements, a reporting obligation will arise, inter alia, where an arrangement meets either one of the so-called user-related criteria or one of the so-called arrangement-related criteria (Section 138l (5) General Tax Code General Tax Code-Draft). Unlike the draft bill, the fact that the user belongs to a group within the meaning of section 18 of the German Stock Corporation Act is no longer sufficient of itself to meet the user-related criterion. The government draft now provides that the group must exceed certain thresholds in terms of total turnover, income, or revenue, whereby only the positive contributions of the individual group companies are taken into account (Section 138l (5) Sentence 1 No. 1 Letter b General Tax Code Draft). Furthermore, changes are planned to the structuring-related criterion vis-à-vis acquisitions made by reason of death or through the gift of an asset (section 138l (5) Sentence 1 No. 2 Letter a General Tax Code Draft). According to the government draft, estate liabilities within the meaning of Section 10 (5) Inheritance Tax Act or the debts and burdens economically related to a gift are to be deducted in the valuation of the transferred assets pursuant to Section 12 Inheritance Tax Act for the purpose of determining whether the intended threshold of EUR 4,000,000 has been exceeded.

The application regulation in Art. 97 Section 33 (7) General Tax Code Introduction Act has been completely reworded. The regulations on the reporting obligations for domestic arrangements are to be applied in all cases in which the decisive event pursuant to section 138n (1) Sentence 2 General Tax Code Draft occurred after a reference date to be determined by the Federal Ministry of Finance at least one year in advance and to be published in the Federal Law Gazette Part I. The intended time span of at least one year between the date of publication of the application provision in the Federal Law Gazette and the first date of application is intended to give all parties involved sufficient time to set up the IT infrastructure required to apply the provisions. If the Federal Ministry of Finance does not make use of its authorisation, the regulations are to be applied at the latest four years after the end of the calendar year in which the new regulation comes into force.

Schlagwörter

Climate Change, RETT, Reorganisation Tax Act, interest limitation