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By PwC Deutschland | 01 September 2023

Government bill for a law to implement the global minimum taxation adopted

On Wednesday, 16 August 2023, the Federal Cabinet adopted the government's draft bill on the implementation of Council Directive (EU) 2022/2523 to ensure minimum global taxation with other accompanying measures. The draft was officially published on 17 August 2023

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Following the adoption of the Directive on the implementation of a global minimum taxation by the Council of the EU on 15 December 2022, various draft bills have been published by the Federal Ministry of Finance (see our Newsflashes of 21 March 2023 and 12 July 2023). Whilst the government draft issued on 16 August considers both additional points raised in the OECD Guidance of February 2023 and comments received from associations, it does not currently consider the guidance published by the OECD in July.

In earlier drafts consideration was given to abolishing both the royalty deduction limitation rule in Section 4j Income Tax Act (ITA) and charge to trade tax on the CFC add-back, however, the exemption to trade tax on the CFC add-back is no longer included in the draft and the royalty deduction limitation rule is to remain in place in principle. However, the low tax threshold defined in Section 4j ITA to be aligned with the low tax threshold for CFC purposes. It is the current intention to reduce this to 15%.

Material changes compared to earlier drafts:

Changes in the Draft Minimum Taxation Act

i. Sovereign Wealth Funds are not ultimate parent companies.

In line with the OECD Guidance of February 2023, a sovereign wealth fund (SWF) will not be treated as an ultimate parent company according to Section 4 (3) Sentence 2 Draft Minimum Taxation Act. According to Sentence 3, a SWF is a government unit whose main purpose is to manage the assets of the public sector, including related investment activities.

ii. Extension of the definition of “excluded entities”.

Section 5(2) Sentence 2 of the Draft Minimum Taxation Act extends the definition of “excluded entities” in line with the OECD Guidance of February 2023 by including so-called “qualified subsidiaries”. Qualifying subsidiaries are entities whose entire equity is held throughout the financial year by an entity falling under Section 5(1) No. 3 of the Draft Minimum Taxation Act (non-profit organisations). A further prerequisite is that in the financial year the sum of the turnover of the business units of the group of companies, excluding the turnover of excluded units within the meaning of Section 5 (1) No. 3 Draft Minimum Taxation Act as well as Sentence 1, amounts to less than 750 million euros and less than 25 per cent of the turnover reported in the consolidated financial statements.

iii. Treatment of "pushdown accounting”.

Following the OECD model commentary, Section 15 (1) Sentence 2 Draft Minimum Taxation Act now prohibits "pushdown accounting", which usually occurs in the case of acquisitions in the context of a merger. A grandfathering clause is included in Sentence 2 for acquisitions occurring before 1 December 2021 where it has not been possible for the group of companies to determine the minimum tax net profit or loss for the year based on the unadjusted carrying amount of the assets and liabilities acquired in the merger.

iv. Adjustments to Section 16 Draft Minimum Taxation Act- Consideration of the arm's length principle

The government draft takes up the suggestion from the associations to include statements in the wording of

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the law that were previously only found in the explanatory memorandum. Thus, the correction provided for in Section 16 (1) Sentence 1 Draft Minimum Taxation Act is not to be applied in cases of unilateral transfer price adjustments where the nominal tax rate is below the minimum tax rate or where the relevant tax jurisdiction was a low-tax jurisdiction in the two financial years preceding the transfer price adjustment.

Section 16 (2) Sentence 1 Draft Minimum Taxation Act orders a corresponding application of Section 16 (1) Draft Minimum Taxation Act for business transactions between business units located in the same tax jurisdiction if these are to be considered separately for the purpose of determining the effective tax rate (i.e. no jurisdictional blending).

v. Corresponding classification of financial instruments

Again, following the OECD Guidance of February 2023, Section 17 of the Draft Minimum Taxation Act obliges a uniform treatment of financial instruments at the level of both the issuer and the holder. Where the classification of the financial instrument differs from each other, the issuer's classification of the instrument is also binding for the holder.

vi. Deduction of Dividends

In Section 20(2) Sentence 2 Draft Minimum Taxation Act, now provides that in the case of compound financial instruments, the deduction is only made in relation to the part of the dividend or other profit distribution that is attributable to the equity component of the instrument.

vii. Gains or losses from the application of the revaluation method to tangible fixed assets

In Section 22 Draft Minimum Taxation Act, the word "annually" is replaced by "regularly". In this way, the government draft takes up the objection of practitioners that a revaluation of property, plant and equipment is generally not carried out on an annual basis for companies reporting in accordance with IFRS (e.g., in the case of high inflation), but rather only every three to five years.

viii. Adjustment item for pension costs

The provision of Section 25 Draft Minimum Taxation Act now uses the term “pension unit”, which is defined in Section 7 (27) Draft Minimum Taxation Act, in both sentence 1 and sentence 2.

According to this, a pension unit exists on the one hand if it is a public insurance and pension institution within the meaning of Section 5 (1) No. 8 Corporation Tax Act. On the other hand, the term “pension unit” will also apply to an entity that is established and operated to administer or provide retirement benefits and supplementary or ancillary benefits exclusively or almost exclusively to individuals who are subject to state regulation as such or whose benefits are secured or otherwise protected by national regulations and are financed by a pool of assets held through a trust institution or a trustee to ensure the fulfilment of the corresponding pension obligations in the event of the insolvency of the group of companies.

In addition, the term "pension unit" also includes the term "pension services unit" as defined in Section 7 (26) Draft Minimum Taxation Act. This exists where financial resources are invested for the benefit of a

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pension unit or auxiliary and where ancillary activities to the regulated activities of a pension unit are carried out, provided that the service unit belongs to the same group of companies.

ix. Tax allowances

Section 27 of the Draft Minimum Taxation Act contains some clarification on the treatment of tax allowances in its Subsection 1. Recognised tax allowances may not be included in the amount of adjusted tax. Unrecognised tax allowances may not be treated as income and must be included in the amount of adjusted tax. Paragraph 2 has been amended to include a sentence stating that unrecognised tax allowances are tax credits that are not recognised tax allowances but are payable in whole or in part.

x. Tax declaration obligation

The newly inserted Section 91 (1) Sentence 7 Draft Minimum Taxation Act obliges all business units as well as joint venture and joint venture subsidiaries to provide the business unit required to file a tax return with the information required to prepare the tax return.

xi. Transitional regulation for subordinate international activities

According to the new Section 80(1) Sentence 2 Draft Minimum Taxation Act, the transitional regulation does not apply to the primary supplementary tax amount, insofar as this is based on a tax increase attributable to a foreign business entity.

Changes in the Commercial Code in the context of the Draft Minimum Taxation Act

Following a regulation change in the context of IFRS according to which the effects of the global minimum taxation on deferred taxes are to be disregarded, the government draft now also provides for an adjustment of Section 274 of the Commercial Code. Thus, when determining deferred taxes, differences are to be disregarded that result either from the German minimum tax rules or a foreign minimum tax rules which implement the requirements of the EU directive or the OECD model regulations.

Furthermore, the new No. 30a of Section 285 of the Commercial Code states that information on the actual tax expense or taxable income resulting from the German and foreign Draft Minimum Taxation Act for the financial year must be referred to in the notes. In addition, an explanation of any effects of the application of the German Draft Minimum Taxation Act and foreign Draft Minimum Taxation Acton on the corporation is to be included. The same applies to the notes to the consolidated financial statements in Section 314 of the Commercial Code in a new No. 22a.

The new provisions in Sections 285 and 314 are to be applied to financial years ending after 30 December 2023, so that a note could already have to be included for annual and consolidated financial statements prepared as at 31 December 2023.

Keywords

EU-Directive, OECD, Pillar Two, minimum taxation