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## Recent tax changes in Germany – Impact on Indian investors

One may have heard that the majority of world's tax literature is produced in Germany, but only a small percentage of the changes are of interest to Indian investors in this country. This article covers for the most recent changes and plans, which can be decisive for Indian investors.

As national elections will be held in Germany on 22<sup>nd</sup> September 2013, it can be expected that the next months will not bring too many surprises. All political parties prefer to wait for the post-election period before starting major initiatives. One of the consequences of the upcoming elections is that the Federal Council so far objected the bill for Annual Tax Act 2013, which should have passed Parliament before year-end 2012, but some changes were included in other bills or will most probably follow soon.

In the "bill on the simplification of company taxation and the tax treatment of travel expenses" passed on 1st February 2013, the following changes were included:

- The maximum amount of loss carry back has been increased. Starting with losses that are assessed in 2013, these can be carried back one year up to €1 million for purposes of corporate income tax.
- In transformation of an ECJ decision, not only German, but from now on also all EU/EEA companies with its place of effective management in Germany may function as group companies (*Organgesellschaft*) within a German fiscal unity regime and allocate its domestic taxable income to a controlling parent company (*Organträger*).
- The bill provides for various simplification measures regarding the deductibility of travel expenses by providing, inter alia, a definition of the "principal" workplace and a two-tier scale for lump-sum deductions for work-related expenses for meals.

### Reliefs for micro-corporations

A new act shortly called MicroBilG has been enacted for small companies in Germany. It contains reliefs for preparing and publishing financial data for about 500,000 German small corporations (including start-ups from India) if two of the following three criteria are not exceeded on two consecutive balance-sheet dates: sales revenues €700,000, balance-sheet total €350,000 and average number of employees not more than 10. The new act is applicable for small corporations and limited partnerships with a limited liability company as general partner and will apply to financial years ending on 31<sup>st</sup> December 2012 or later.

### Court decision

The Federal Fiscal Court (BFH) ruled in a decision dated 11<sup>th</sup> October 2012 that treaty law can overrule national German rules for constructive dividends. In the case, a German subsidiary of a foreign corporation paid fees for services provided by its foreign mother company. Although the payments were according to the arm's length principle, the German tax office treated these payments as constructive dividends since no written agreement between the involved parties about providing the services was closed in advance. Verbal agreements and later written agreements with retroactive effect were not accepted by the tax authorities.

In contrary to the tax authorities, the court ruled that German constructive dividend rules are not applicable in this case since the dealing at arm's length-principle in the treaty (here: DTT Germany – Netherlands) creates a barrier effect for special German rules of constructive dividends for affiliated companies. This decision will provide legal security for future intra-group payments in multinational groups without prior written agreements. Nevertheless, close attention must be paid to the kind of payments and to rules in the individual Double Taxation Treaties as they may differ from the OECD model convention. So e.g. retroactive payments of man-

aging shareholders remuneration is normally not protected by DTTs and for interests on intra-group loans and intra-group royalties other rules apply.

### DTT changes

A new income tax treaty between Germany and Mauritius applies since 1<sup>st</sup> January 2013. According to the treaty, the withholding tax rate on dividend payments is reduced to 5% when the recipient directly holds at least 10% of the dividend paying company. In addition, the withholding tax rate on royalty payments is reduced to 10%. Since some investments from India to Germany were structured via Mauritius, this might also have an effect on Indian investors.

### Other planned future changes

In transformation of the new article 7 of the OECD Model Convention into German law, it is planned to introduce shortly new rules for attribution of profits to permanent establishments (P.E.), replacing the "Relevant Business Approach" by the "Functionally Separate Entity Approach". In general, it is planned to treat P.E.s like an independent enterprise for tax purposes, accept so called "dealings" for services between P.E. and the enterprise of which it is a permanent establishment and accept payments for such dealings according to transfer pricing rules. Taking into account the functions performed, assets used and risks assumed by the enterprise through the permanent establishment and through the other parts of the enterprise it will also be necessary to allocate a part of the share capital and of the goods to the P.E. Different to the present situation, it will then be possible to have a loss in the P.E. although the enterprise as a whole has a profit and vice versa. Since these rules will not apply to commercial invoices and commercial balance sheets and looking at the complex transfer pricing rules we know from subsidiaries, from a tax point of view it cannot be recommended to start or continue your business in Germany via a P.E.

As a result of the financial crises, the German Government decided in February 2012 to apply changes on banks. Firstly, recovery and insolvency procedures of banks shall be simplified. Secondly, the now existing universal banking system shall be transformed

## Cooperation

into a separate banking system with a separation of risk oriented investment banking and retail banking until July 2015. Thirdly, bank and insurance company officers violating their obligations shall be prosecuted with fines and up to five years imprisonment.

European Commission proposes tougher anti-money laundering rules. It is suggested to include all cash payments of €7,500 or more in the scope of anti-money laundering regulations. The new proposals establish that individual staff should be fined up to €5 million and firms, such as banks, should be fined 10% of their turnover if they flout anti-money-laundering rules. It also rules that casinos, including online casinos, should process checks on transactions of €2,000 or more.

Other proposed sanctions include withdrawal of bank licenses if a bank is involved, banning of executives from holding board seats as well as public naming and shaming. The Commission has also published a draft regulation governing the information that must accompany fund transfers.

11 Eurozone countries, which account for about 90% of Eurozone GDP (including Austria, Belgium, Estonia, France, Germany, Greece, Italy, Portugal, Slovenia, Slovak Republic and Spain) prepare to launch a financial transactions tax (FTT). After a council decision dated 22<sup>nd</sup> January 2013, the European Commission will now draft legislation enacting a tax.

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a German CPA and certified tax advisor and chairman of the "International Taxation Practice Group" of Geneva Group International, the world's largest multidisciplinary alliance that includes law firms, accounting firms and management consulting firms offering professional services.

### 'Water 'n Waste' Delegation to Germany

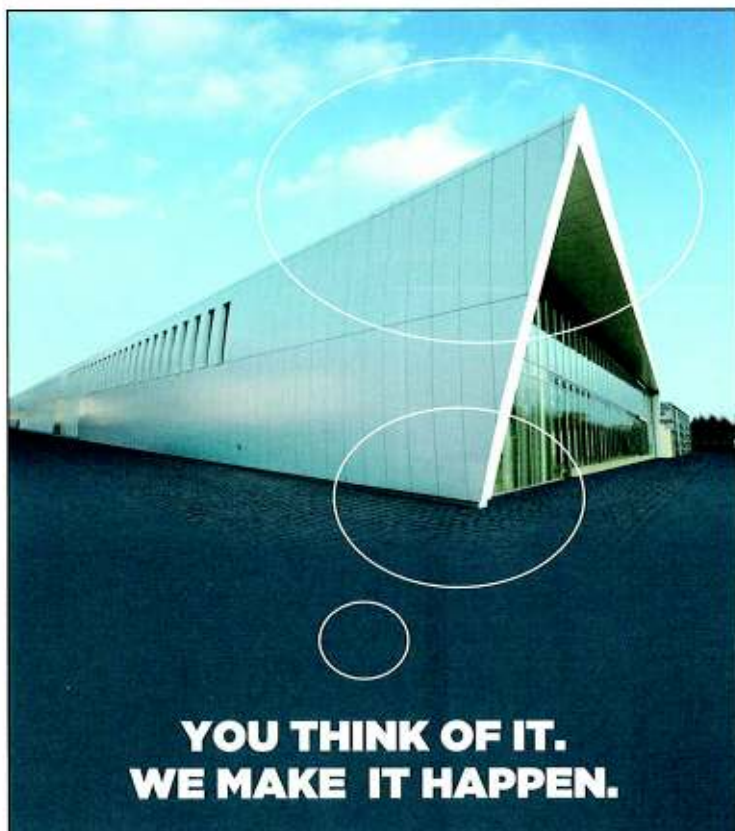
13<sup>th</sup> to 17<sup>th</sup> May 2013

Update yourself on best sustainable practices in areas such as Recycling, Water Treatment and Restoration of rivers and water bodies by participating in the above delegation.



**Key highlights:** •Restoration of the rivers Rhine and Lippe; •Visit to research institutions involved in developing commercially viable technologies; •Visits to municipal and industrial waste water treatment plants; •Visit to a waste segregation and recycling plant with solutions for new use of waste; •Small hydro power solutions for rivers and other water bodies; •Water treatment for industrial purposes and for drinking water quality; •Visit to an engineering company that can implement these solutions.

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