

Tax
Germany

January 2018

Sweeping changes of German transfer pricing rules - January 2018 Update

In December 2016 we provided an overview of the most important adopted and expected changes in German transfer pricing rules. The below gives an update of this overview.

I. Current and future changes

Current and expectable changes of the tax law on transfer pricing are, in particular:

1. Overhaul of the Legislative Decree on the Documentation of Profit Allocation ("Gewinnabgrenzungsaufzeichnungsverordnung"; "GAufzV"): In force. Applies for all fiscal years beginning after December 31, 2016.
 - More specifications of statutory documentation, containing far-reaching extensions of taxpayers' obligations to cooperate.
 - A detailed (German language) critique by [Schnorberger/Haverkamp/ Etzig, BB 2017, 1111](#); as well as [Schnorberger/Haverkamp/ Etzig, BB 2017, 2455](#) is available here.
2. Establishment of a transparency register to record "economic owners" (i.e., individuals or natural persons, resp.) behind privately held companies and registered partnerships. Individuals, who (1) hold more than 25 % of the share capital, directly or indirectly, or (2) control more than 25 % of the voting rights or (3) exercise similar control under any circumstance in a non-listed company, shall be disclosed. Non-compliance may result in administrative penalties: In force since June 26, 2017.
3. Limitation of deductible license fees ("license barrier"; "Lizenzschranke") paid to related entities, where license fees are taxed at a preferentially low rate in the hands of the licensor and the preference regime (e.g. "IP Box") violates the OECD Nexus approach: In force. Applies to license fees (charges in accounts) arising after December 31, 2017.
 - For further details see our Client Alert "[Federal Council approves new law limiting royalty deductions](#)" of July 2017.
4. New taxpayer reporting obligation for investments in non-EU/non-EFTA companies, where controlling or decisive influence is established. Non-EU/non-EFTA companies are partnerships, corporations, associations or assets domiciled or managed outside of the EU and of the European Free Trade Association (Swiss companies are not covered). In general, the report shall be filed with the tax return. A corresponding reporting obligation for banks and certain financial institutions was implemented. These have to report relations to non-EU/non-EFTA companies which they brokered or established, when

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these relations give rise to controlling or decisive influence, be it directly or indirectly. The same applies where such potential influence can only be exercised together with related parties. Applies for reportable relations arisen after December 31, 2017.

5. Abolition of protection of confidential banking information in tax proceedings: In force. Applies to all proceedings pending on or after June 25, 2017, i.e. this applies partly with retroactive effect.
6. Possibility of a collective information request: In force. Applies to all proceedings pending on or after June 25, 2017, i.e. this applies partly with retroactive effect.
7. Listing of grave cases of tax evasion expanded: Using a non-EU/non-EFTA company (e.g. a base company) as a sham to illegally reduce taxes on a continued basis represents grave tax evasion. Grave tax evasion statutorily leads to higher penalties than regular tax fraud cases. Voluntary self-disclosure is precluded: In force. Applies for tax evasions committed after June 25, 2017.
8. Update of the OECD Transfer Pricing Guidelines for Multinational Enterprises: Includes changes based on the OECD BEPS reports on Action Item 10 (Aligning Transfer Pricing Outcomes with Value Creation) and Action Item 13 (Transfer Pricing Documentation and Country-by-Country Reporting). Published on July 10, 2017. According to the OECD, individual changes apply as from their approval by the OECD Council and the Committee on Financial Affairs. In local jurisdictions, application of Guideline updates depends on enforcement practice and on whether tax treaties are interpreted purely historically or dynamically.
9. Update of the OECD Model Tax Convention on Income and on Capital. Includes changes based on the OECD BEPS reports on Action Items 2 (Neutralizing the Effects of Hybrid Mismatch Arrangements), 6 (Preventing the Granting of Treaty Benefits in Inappropriate Circumstances), 7 (Preventing the Artificial Avoidance of Permanent Establishment Status) and 14 (Making Dispute Resolution More Effective). Published on December 18, 2017.
10. New administrative regulations on (licenses for) the use of group names, trademarks and logos: Published on April 7, 2017. Applies in all pending cases.
11. New administrative regulations on Country-by-Country-Reporting requirements: Published on July 11, 2017. Applies in all pending cases.
12. Implementation of the Multilateral Instrument by selective adjustments to double taxation treaties: Expected from 2019 onwards.

Particularly noteworthy are the following points:

- Germany has confirmed its longstanding position on specific activity exemptions from permanent establishments: Preparatory and auxiliary activities listed in double tax treaties are only then exemptions from permanent establishments, if they are truly of preparatory or auxiliary nature in the individual business concerned. In other words, Germany has confirmed its position that the listed activities are no “per se” or “automatic” exemptions from permanent establishment status.

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- Germany has opted out of generally deeming commissionaires permanent establishments of the principal companies. Germany may, however, include such deeming clauses in bilateral double tax treaties (as agreed in the Australian double tax treaty in 2015 with effect as from October 11, 2016) and
 - Germany indicated its commitment to introduce dispute resolution procedures with guaranteed settlements via arbitration.
13. New tax planning reporting: EU Commission draft directive to obligate tax intermediaries (in general tax advisors) or taxpayers to report cross border tax plans and to obligate EU member states to exchange reported information: According to the draft directive, implementation into domestic law shall apply as from January 1, 2019.
- The Upper House of Parliament (Bundesrat) publicly supported the project on September 22, 2017.
 - The EU Commission emphasized its view that the reporting obligation will not violate EU fundamental freedoms nor the principle of non-discrimination. The EU Commission rejects anonymous reports by tax advisors. If professional secrecy rules bar tax intermediaries from reporting, taxpayers themselves shall have to report.
14. Mandatory dispute resolution in cases of double taxation within the EU to implement the EU Tax Dispute Resolution Directive. The directive entered into force on November 3, 2017. It shall be adopted into domestic law by June 30, 2019. The mandatory dispute resolution rules apply to any double taxation of profits arising as from January 1, 2018.
- The new dispute resolution mechanisms shall be based on the EU Arbitration Convention and extend its scope beyond transfer pricing disputes.
 - The directive is of particular interest in cases where it is in dispute whether a permanent establishment is present or not.
15. Possible changes of German CFC rules to implement the EU Anti-Tax Avoidance Directive ("ATAD I Directive"): Expected the new German Federal Government is formed.
16. Adoption of the EU directive amendment on hybrid mismatches with third countries ("ATAD II directive") and introduction of a comprehensive set of provisions on the tax treatment of hybrid financing and hybrid structures: Expected new German Federal Government is formed.
17. Amendment of the EU Accounting Directive introducing the obligation to publish corporate income tax information for certain companies and branches ("Public Country-by-Country Reporting"): The EU Commission's draft from April 12, 2016 is pending and currently under revision by the European Parliament. A first statement by the Committee on Development was published on April 28, 2017.
18. Administrative regulations on profit allocation to permanent establishments without personnel (server, pipelines, wind turbines etc.): Under consideration.

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The following table provides an overview of all regulations in question, their content and time of application:

	Law or Rule affected	Content	Date of Application
1.	GAufzV	Overhaul of the ordinance GAufzV to match to the recently revised statute on transfer pricing documentation, sec. 90 (3) AO	Fiscal years starting after December 31, 2016
2.	sec. 18 ff. GwG	Transparency register	Since June 26, 2017
3.	sec. 4j EStG	(Partial) limitation of the deduction of royalties ("license barrier")	Expenses incurred after December 31, 2017
4.	sec. 138 (2) - (5), sec. 138b AO	Expansion of reporting obligations in case of shareholdings in non-EU/non-EFTA member state entities.	Investment takes place December 31, 2017
5.	sec. 30a AO	(Partial) repeal of bank secrecy	June 25, 2017
6.	sec. 93 (1a) AO	Collective information requests	June 25, 2017
7.	sec. 370 (3) AO	Use of non-EU/non-EFTA entities (base companies) as grave tax evasion	June 25, 2017
8.	OECD Transfer Pricing Guidelines	Update of the OECD Transfer Pricing Guidelines	Published on July 10, 2017
9.	OECD-Model Tax Convention	Update of the OECD Model Tax Convention	Published on December 18, 2017
10.	BMF Circular - IV B 5 - S 1341/16/10003	Administrative regulations on fees for the use of group name and trademark	Published April 7, 2017, applies to all pending cases
11.	BMF Circular - IV B 5 - S 1300/16/10010: 002	Administrative regulations on the particularities of Country-by-Country reporting	Published on July 11, 2017, applies to all pending cases
12.	Multilateral Instrument	Implementation of OECD BEPS recommendations as notified in the multilateral instrument through bilateral tax treaties	Anticipated for 2019; depending on the conclusion of bilateral agreement with the respective treaty partner
13.	EU Administrative Cooperation Directive-Draft	Obligation for intermediaries or taxpayers to report tax schemes; EU member states exchange information on reported tax schemes	Will apply starting January 1, 2019, according to the directive draft and subject to implementation into domestic law

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	Law or Rule affected	Content	Date of Application
14.	EU Tax Dispute Resolution Directive	Obligatory dispute resolution for disputes on double taxation within the EU	Starting July 1, 2019 applying to double taxation arising on or after January 1, 2018
15.	sec. 7 ff. AStG-Draft	Changing German CFC Rules to adopt ATAD I Directive	Unknown
16.	BEPS-Implementation Law II	Additional set of statutory BEPS implementation rules, for example on hybrid financing	Unknown
17.	EU-Accounting-Directive-Draft	Public-Country-by-Country Reporting	Unknown
18.	BMF Circular	Administrative regulations on profit allocation to permanent establishments without personnel	Under consideration

II. Changes implemented in German tax law

Since our December 2016 overview, the following measures have been implemented:

1. Scope of documentation obligations has been extended by the first BEPS Implementation Act: For fiscal years beginning after December 31, 2016. With the amendment of sec. 90 (3) AO, the following changes have been introduced, in particular:
 - The time when transfer prices are being set must be documented.
 - The documentation of the arm's length nature of transfer prices, namely the systematic documentation of comparable data, are a mandatory part of any transfer price documentation.
 - Domestic subsidiaries with EUR 100 million or more in revenue are obligated to document their group's worldwide business activities and overall transfer price policy (master file). This is in line with OECD/G20 recommendations in the final report on action item 13.
 - [For further details see our Baker McKenzie European Transfer Pricing Handbook 2017.](#)
2. Country-by-Country reporting for domestic groups with at least EUR 750 million in revenue: Applies for fiscal years starting after December 31, 2015.
3. Country-by-Country reporting for domestic subsidiaries of foreign groups with at least EUR 750 million in revenue: Applies for fiscal years starting after December 31, 2016.

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Foreign enterprises will have the opportunity to do surrogate filing for fiscal years starting after December 31, 2015.

4. Additional regulations to the EU ATAD I directive regarding hybrid mismatches (EU ATAD II Directive) came into force on June 27, 2017. The directive shall be adopted into domestic law before December 31, 2019 and applies as of January 1, 2020. Regulations regarding reverse hybrid structures apply starting in January 1, 2022.
5. Authorization of the German Federal Ministry of Finance to issue a legislative decree that denies the German tax exemption of foreign income or part of such foreign income, in lieu of a foreign tax credit: Applies starting January 1, 2017.
 - Extension: Now also individual parts of income untaxed abroad may be deemed subject to German taxation, for example tax-free foreign investment allowance (Sec. 50d (9) EStG): Applies for fiscal years starting after December 31, 2016. Note, that the constitutionality of sec. 50d (9) (3) EStG in the version of the annual tax act 2007 is currently under review at the German Federal Constitutional Court.
6. EU-wide, automatic exchange of information on tax rulings and advance pricing agreements (APAs): Applies starting January 1, 2017.
 - Note: Information provided in an application for an APA relating to an affiliate in a non-EU member state, e.g. US, is subject to automatic information exchange with other EU member states.
7. Trade tax on add-backs relating to foreign subsidiaries and foreign permanent establishments: In force since January 1, 2017 and applies for fiscal years beginning after December 31, 2016.
8. Neutralization of double dips for special business expenses in partnerships: In force starting January 1, 2017 and applies for fiscal year 2017 and following.
 - Example: Interest paid by a foreign partner of a German partnership on a loan granted to the partnership is no longer deductible in Germany if the foreign partner can deduct the interest as business expenses in his state of residence.
9. Final version of the ordinance on profit allocation to permanent establishments: Published on December 22, 2016. Applies in all pending cases.

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The following table provides an overview of all regulations in question, their content and date of application:

	Law or Rule Affected	Content	Date of Application
1.	sec. 90 (3) Fiscal Code (AO)	Extension of transfer price documentation obligations	Fiscal years starting after December 31, 2016
2.	sec. 138a (1), (2), (6) and (7) AO	Introduction of CbCR for domestic groups with revenue of at least EUR 750 million	Fiscal years starting after December 31, 2015
3.	sec. 138a (3 - 5) AO	Introduction of CbCR for domestic subsidiaries of foreign groups with revenue of at least EUR 750 million	In general: fiscal years starting after December 31, 2016 Surrogate filing: fiscal years starting after December 31, 2015
4.	EU - ATAD I Directive	Additional regulations on hybrid financing and hybrid structures	Starting January 1, 2020, starting in part January 1, 2022
5.	sec. 2 (3) AO	Switch over based on mere ordinance	Starting January 1, 2017
6.	sec. 2 ff. EU Administrative Assistance Act	Automatic exchange of information on tax rulings and advance pricing agreements	Starting January 1, 2017
7.	sec. 7 GewStG	Trade tax on passive income of foreign subsidiaries and permanent establishment CFC amounts	Starting January 1, 2017
8.	sec. 4i EStG	Neutralization of double dips for special business expenses in partnerships	Starting January 1, 2017
9.	Permanent Establishments	Publication of ordinance on profit allocation to permanent establishments	Starting December 22, 2016, applies in all pending cases

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