German Tax Monthly

Information on the latest tax developments in Germany

October | 2021

Federal Tax Court (I R 77/17): Applying the EU Parent-Subsidiary Directive in the case of a Partnership acting as an Intermediary

With its decision of 18 May 2021, the German Federal Tax Court (BFH) ruled that the requirements of the Parent-Subsidiary Directive are met also when an asset management partnership acts as an intermediary.

In Germany, dividends received by a foreign corporation from a domestic corporation are generally subject to 25% withholding tax. However, according to the Parent-Subsidiary Directive, the recipient of the dividend has a claim to refund of the withholding tax withheld and paid. To obtain a refund, the creditor must file an application with the Federal Central Tax Office (BZSt). Nevertheless, the German refund regulation – which transposes the EU Parent-Subsidiary Directive into national law – also requires that the creditor holds at least a 10% direct interest in the German corporation.

In the case at hand the plaintiff, a co-operative under Dutch law, held a 33.6% share in a German asset management partnership (GbR, civil law partnership). The GbR, in turn, held a 100% share in a German Corporation (AG, stock corporation). In the year at issue, 2014, the AG distributed a dividend to the GbR. The AG withheld 25% withholding tax at the expense of the plaintiff and remitted it to the local tax office. In June 2014 the plaintiff filed an application for the refund of the full amount of withholding tax with the BZSt.

In dispute was whether the plaintiff held a direct interest in the German AG within the meaning of the EU Parent-Subsidiary Directive.

The BFH took the same view as the Cologne Lower Tax Court that there was a direct holding despite the GbR acting as an intermediary.

Even though the asset management partnership is the legal owner of the investment in the German AG under civil law, a tax-based perspective is in fact authoritative for fulfilling the requirements of a direct investment within the meaning of the German refund regulation. Accordingly, an asset management partnership is not subject to

Content

© 2021 KPMG AG Wirtschaftsprüfungsgesellschaft, a corporation under German law and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. Printed in Germany.

income tax. Pursuant to the "transparency principle", the profits generated are directly and solely attributable to the partners who are subject to taxation. The same applies to the partnership's assets, which are proportionally attributable to the partners. Therefore, from an economic point of view, a "look-through" approach is taken with respect to the asset management partnership. This is also true for assessing the required minimum holding of 10%.

Consequently, the prerequisites for fully refunding the withholding tax in Germany are met.

Lower Tax Court of Saarland (1 V 1374/20): Attribution of Profits and Exit in the case of a Permanent Establishment without Personnel

The Lower Tax Court of Saarland passed a ruling on the attribution of assets, attribution of profits and so-called "passive exit" in the case of permanent establishments without personnel (ruling dated 30 March 2021, file ref. 1 V 1374/20). These proceedings only addressed suspending the enforcement of the tax assessment. Such suspension is to be effected when there are serious doubts as to the legality of the tax assessment.

The plaintiff was a German limited partnership that has been operating a wind farm on leased property since 2011. The plaintiff's partner was a Danish partnership. The plaintiff has no own staff either in Germany or in Denmark. Both technical and business management is carried out by two German service companies.

With effect from 1 January 2013, the Authorised OECD Approach (AOA) for attributing profits to a permanent establishment was transposed into German tax law. Accordingly, a permanent establishment is treated as a separate and independent business entity. The significant people function is relevant to the attribution of assets. As a result, the German tax office assumed that all assets and transactions are, contrary to previous practice, not attributable to the plaintiff's German permanent establishment (wind farm), but instead for the first time to the management permanent establishment in Denmark because the sole and, thus, the significant people function of the plaintiff is performed in the management permanent establishment in Denmark. As a result, the plaintiff's entire assets did exit for tax purposes. Furthermore, the current loss from the year under dispute (2013) can no longer be taken into account in Germany.

The Lower Tax Court of Saarland first found that in the case of the wind farm – according to German law as well as pursuant to the tax treaty with Denmark – this involves a German permanent establishment whose income falls under German tax jurisdiction. Furthermore, the wind farm's assets are also to be attributed to this German permanent establishment for the period prior to 2013.

However, in its ruling, the court expressed serious doubts in many respects regarding the legality of the tax office's view:

- There is serious doubt whether the assets of the German permanent establishment following introduction of the AOA with effect from 1 January 2013 are now attributable to the management permanent establishment in Denmark and, as a result, this leads to the realisation of profits through fictitious withdrawal.
- There is also serious doubt as to whether the attribution of assets according to the people function can even be applied at all in the case of permanent establishments without personnel.
- Finally, there is serious doubt as to whether a so-called "passive exit" can occur if Germany's right to tax is excluded or restricted just through government action (i.e. due to transposing the AOA into law with effect from 1 January 2013).

The issue of assets (which previously were attributed to a German permanent establishment) possibly exiting as a result of implementing the AOA concerns cases where the permanent establishment existed already before 1 January 2013. The doubts regarding attributing assets in the case of permanent establishments without personnel could also be transferable to other cases, e.g. computer servers or solar parks. The doubts regarding the so-called "passive exit" could equally be transferable to other cases, e.g. concluding a new tax treaty or amending an existing tax treaty, whereby the German right to tax assets is restricted or excluded.

In the proceedings to suspend enforcement, only a summary review is conducted as to whether there also are substantial circumstances that contradict the legality. The tax office has lodged an appeal with the German Federal Tax Court against the ruling (file ref. I B 44/21). The Lower Tax Court of Saarland has not yet reached a decision on the main proceedings.

© 2021KPMG AG Wirtschaftsprüfungsgesellschaft, a corporation under German law and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. Printed in Germany.

Current Status of Implementation of the German Property Tax Reform

The implementation of the German property tax reform is in the final stretch and the federal property tax model as well as the state models that deviate from the standard federal model are now in place. In particular, the date for the revaluation of properties for the purposes of the reformed property tax is drawing ever closer. The first main assessment using the new property tax values is to take place on 1 January 2022. The new property tax values apply for the first time for taxation in 2025.

Background: In April 2018 the German Federal Constitutional Court declared the previous valuation system for property tax unconstitutional and granted the legislator a deadline until the end of 2019 to find a new regulation. The German Property Tax Reform Act was announced on 2 December 2019. The reform specifies taxation based on a value-dependent property tax model in the form of the rental value method and the replacement costs method, but also includes an escape clause for the federal states. According to this escape clause, the federal states can deviate from the federal regulations in favour of other models. As things currently stand, five federal states have made extensive use of this clause. Two federal states are using the federal model with adjusted tax assessment factors and nine federal states are applying the federal model without any changes.

Federal model

According to the amendment to federal law, the value of undeveloped land is determined using the standard land values calculated by expert committees.

In the case of developed land, a standard simplified rental value method is applied as valuation method for residential property, which is tied to the sustainable realisable net income. The value of developed (residential) property consists of the standard land value and the average rental value for the building in question. In the case of detached and semi-detached houses, rental housing and owner-occupied properties, the rental value is typically assumed based on the notional net rent depending on the location of the property to reflect the change in value in recent decades due to rising property prices. At the same time, the tax assessment factor as second factor in the calculation is reduced to counter a rise in total property tax revenue.

The replacement costs method is applied particularly to non-residential properties as it is currently not possible to calculate any average net rents (excl. heating costs) for these properties using available statistical sources. The replacement costs consist of the land value and the building's replacement costs, which are based on the normal production cost.

In the case of agricultural land and forestry, a separate rental value is used which is based on the capitalisation of average earnings in relation to the respective use.

Overview of state models

All of the federal states have already announced whether they intend to follow the federal model or make use of the escape clause.

Berlin, Brandenburg, Bremen, Mecklenburg-Western Pomerania, North Rhine-Westphalia, Rhineland-Palatinate, Saxony-Anhalt, Schleswig-Holstein and Thuringia are applying the federal model. Baden-Württemberg, Bavaria, Hamburg, Hesse and Lower Saxony have developed their own valuation models. Saarland and Saxony are using the federal model with adjusted tax assessment factor. All of the states will be following the rules of the federal model for the valuation of agricultural land and forestry.

In some cases, the state laws have already been passed or are at least in the draft bill stage. While the value-dependent federal model uses the market value, the state models are based on area models that are not dependent on value and which, with the exception of Bavaria, all take into account location-specific factors. The exception is Baden-Württemberg, which uses a model based purely on land value. All of the state models also provide preferential treatment for residential use.

© 2021KPMG AG Wirtschaftsprüfungsgesellschaft, a corporation under German law and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. Printed in Germany.

Imprint

Published by
KPMG AG Wirtschafts-
prüfungsgesellschaft
THE SQUAIRE, Am Flughafen
60549 Frankfurt/Main, Germany

Editorial Team
Prof. Dr. Gerrit Adrian
(Responsible*)
gadrian@kpmg.com

Veronika Aschenbrenner
Julian Fey
Alexander Hahn

Newsletter subscription
https://www.kpmg.de/newsletter/subscribe.aspx

*Responsible according to German Law
(§7 (2) Berliner PresseG)

kpmg.de

kpmg.de/socialmedia.de

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2021 KPMG AG Wirtschaftsprüfungsgesellschaft, a corporation under German law and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved. Printed in Germany.