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German Federal Tax Court (I R 39/18): Carryover of Book Values in the Event of Spin-off

In its judgment of 11 August 2021, the German Federal Tax Court (BFH) ruled that a spin-off fulfils the requirements for a sale only – and therefore carryover of book values is precluded only – if a sale occurs within the five-year period in which the 20% threshold is exceeded.

If the assets of a corporation are transferred to other corporations as a result of split-up or spin-off, the transferred assets must be recognised at fair market value. Alternatively, they can be recognised at their book value upon application if certain conditions are fulfilled. However, the option to use their book value does not apply if as a result of the split-up the requirements for sale to external parties are fulfilled (§ 15 (2) sent. 3 of the German Reorganisation Tax Act [UmwStG]). This can be assumed according to the law if within five years of the transfer date for tax purposes shares in a corporation involved in the split-up are sold that represent more than 20% of the shares in existence prior to the split-up of the corporation taking effect (§ 15 (2) sent. 4 UmwStG).

In the case decided by the BFH, all the ownership interests held in E-GmbH were split off to form the new company L-GmbH in 2008 with retroactive tax effect from 31 December 2007. The objective of restructuring was to sell the shares in L-GmbH to third parties. For this reason, spin-off of the shares in E-GmbH to the company still to be established (L-GmbH) was already agreed in the contract of sale dating back to 2007. The local tax office as well as the Lower Tax Court of Hamburg (judgment 6 K 77/16 of 18 September 2018) were of the opinion that in this case a restriction on sale applies and therefore denied book valuation.

In deviation from the above, the BFH has now decided in the appeal proceedings that tax-neutral carryover of book values is possible in the case at hand. The Court found that the provision of § 15 (2) sent. 3 UmwStG does not represent separate grounds for exclusion, detached from sentence 4: § 15 (2) sent. 3 UmwStG only forms the basis for the

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presumption of sentence 4 and does not constitute independent grounds for exclusion of carryover of book values. It represents one uniform regulation for the prevention of abuse consisting of sentences 3 and 4. The legal requirement that the conditions for sale are created by the spin-off (restriction on sale pursuant to § 15 (2) sent. 3 UmwStG) can therefore only be considered fulfilled when a sale occurs within the five-year period in which the 20% threshold is exceeded (requirements of § 15 (2) sent. 4 UmwStG). In the case under dispute, the requirements of § 15 (2) sent. 4 UmwStG were not fulfilled, as the 20% threshold was not reached. According to the BFH, recourse to sentence 3 of the provision was therefore precluded. Consequently, a spin-off at book value could occur. The BFH thereby ruled contrary to the administrative opinion of the Finance Ministry of Brandenburg in its decree of 16 July 2014 and of the Finance Ministry of Hamburg in its decree of 13 April 2015.

German Federal Ministry of Finance: Guidance on Granting a Research Allowance

With effect from 1 January 2020, a tax incentive for research and development (R&D) was introduced in Germany in the form of a research allowance. The tax incentive is to promote investments in Germany and stimulate research activities, especially by SMEs.

The German Federal Ministry of Finance (BMF) has now commented on the granting of the research allowance (BMF guidance as of 11 November 2021).

Companies of any size and in any sector that are subject to taxation in Germany (non-resident or resident tax liability) can apply for government funding for R&E. Research activities that commenced after 1 January 2020 are eligible for funding. Projects in the areas of basic research, industrial research or experimental development are given preferential treatment. The allowance is generally based on the salaries of the research staff participating in the R&E project and their share of working hours on the project. A tax-exempt research allowance is then paid in the amount of 25 percent of this assessment basis. The allowance is limited to 500,000 euros per financial year (between 1 July 2020 and 30 June 2026: one million euros per financial year). In the case of affiliated companies, this maximum amount is granted only once each financial year.

One special feature is so-called contract research: The research allowance is granted not only to companies that conduct research themselves, but also those that contract a third party to conduct research for them, for example another company, a university or a research institution based in the EU or the EEA. Eligible expenses for contract research amount to 60 percent of the consideration paid to the contractor by the contracting entity. However, in the case of contract research, the contracting entity receives the research allowance, not the company conducting the research. This can have the effect, especially in inbound structures – in which a domestic company is contracted by a non-domestic affiliate to conduct R&D activities – that the corporate group does not receive the research allowance.

According to the BMF, the award of contracts between affiliated companies is not necessarily characterised by an affiliated company conducting the R&D activity on the basis of contractual arrangements usually made between third parties. A fee is not typically always agreed for the services rendered. Instead, the research company usually receives a cost reimbursement plus a percentage profit mark-up, irrespective of the success of the R&D activity. With that in mind, the BMF has established various criteria which, if cumulatively fulfilled between affiliated companies, lead to the assumption of contract research. If not all criteria are fulfilled, in-house research of the "contracting" company must be assumed. In the inbound structures described above, the domestic company could apply for the research allowance in such a case.

A two-stage process is provided for the application and granting of the research allowance: In order to receive the allowance, a certificate must first be applied for stating that it is an eligible R&D project. An application to determine the research allowance is then submitted the tax office. The research activities and time spent must be documented as evidence. The documentation of contract research is evident from the invoices issued and contracts concerned. The research allowance is then deducted from the assessed tax as part of the next tax assessment or paid out in the event of a loss.

Further Extension of the Special Coronavirus Rules for Cross-Border Commuters

At the end of 2021, various consultation agreements between Germany and its neighbouring countries were extended once again.

The coronavirus pandemic presents particular challenges for cross-border commuters who normally commute daily from their country of residence to work in another country. For this reason, the

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German Federal Ministry of Finance [BMF] has concluded temporary consultation agreements with neighbouring countries for cross-border commuters in order to prevent salaries and wages from becoming taxable in the country of residence of the cross-border commuters due to working from home. Accordingly, working days for which salary or wages are received and on which cross-border commuters only work from home because of measures to combat the coronavirus epidemic are considered working days spent in the contracting state in which the employees would normally have carried out their work. The agreements apply to working days from 11 March 2020.

In December 2021, the mutual agreements with Luxembourg, the Netherlands, Austria, Belgium, France and Switzerland were explicitly extended once again. In view of the current pandemic situation, these agreements are to apply until at least the end of March 2022.

The following consultation agreements are currently in place:

- Austria, Switzerland
  The agreements with Austria and Switzerland are applicable until at least 31 March 2022. They are automatically renewed by one month if not terminated. The two agreements also apply to public sector employees and both include an explanation of situations when a home office is considered a permanent establishment.
- Luxembourg
  This consultation agreement is also applicable until at least 31 March 2022 and automatically renewed by one month if not terminated. Likewise, it is also applicable to public sector employees.
- France, the Netherlands
  The agreements with France and the Netherlands are also applicable until at least 31 March 2022 and are automatically renewed by one month if not terminated.
- Belgium
  The agreement with Belgium is applicable until at least 31 March 2022. There is no automatic renewal, however an optional to do so.
- Poland
  There is also a consultation agreement with Poland. It is automatically renewed by one month if not terminated and also applicable to public sector employees.

Entry into Force of the Regulation to apply the Act to Combat Tax Havens

In December 2021, the regulation to apply the Act to Combat Tax Avoidance and Unfair Tax Competition (Steueroasenabwehrverordnung – StAbwV) was promulgated in the German Federal Law Gazette (Bundesgesetzblatt). The regulation has thus entered into force in principle.

The Act to Combat Tax Avoidance and Unfair Tax Competition (Act to Combat Tax Havens – StAbwG) of 25 June 2021 provides administrative and legislative measures that apply in relation to those states and territories that are non-cooperative tax jurisdictions. Tax jurisdictions are non-cooperative pursuant to the StAbwG, if they are on the EU list of non-cooperative countries and territories for tax purposes and specified in the StAbwV. The StAbwV currently lists the following nine non-cooperative tax jurisdictions: American Samoa, Fiji, Guam, Palau, Panama, Samoa, Trinidad and Tobago, US Virgin Islands and Vanuatu.

In addition, the date (24 December 2021) is specified on which the itemised non-cooperative tax jurisdictions were included in the StAbwV. This is relevant for the applicability of defensive measures, because the StAbwG provides for a "phased model" for the timing of certain defensive measures for new countries included. The following applies for the nine above-mentioned tax jurisdictions with the entry into force and inclusion in the StAbwV in the course of 2021:

- From 2022 (the first year after inclusion), tighter CFC rules and withholding tax measures (Sections 9, 10 StAbwG) must be applied.
- From 2024 (the third year after inclusion), measures concerning dividends and sales of ownership interests (Section 11 StAbwG) must be applied in addition.
- From 2025 (the fourth year after inclusion), denial of tax deduction of expenses (Section 8 StAbwG) must be applied in addition.

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