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Germany

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Important court decisions regarding cross-border taxation were issued in Germany in 2011, and the German Tax Administration announced public rulings that will significantly affect business taxation.

Tax Legislation

Three main legislative tax initiatives took place in 2011.

The 2011 Tax Simplification Bill eliminates some formal requirements. The bill contains many minor measures, such as increasing the lump sum for employees' tax expenses, establishing a de minimis threshold regarding fees for tax rulings, and easing the requirements for the electronic submission of tax data.

Second, the Bundestag approved a bill that would implement the EU mutual assistance directive into German domestic law, and final approval by the Bundesrat passed on November 25. The bill would also suspend the reorganization clause under the change of control rule, impose deemed gift treatment for corporations under the Inheritance and Gift Tax Act, and amend the German anti-treaty and anti-directive-shopping rule, which will be relaxed in response to an infringement procedure the European Commission initiated against Germany in March 2010.

Third, Thuringia, Brandenburg, North Rhine-Westphalia, and Baden-Wuerttemberg increased their real estate transfer tax rates from 3.5 percent to 5 percent.

Tax Court Decisions

Cross-Border Taxation

In two February 9 decisions (I R 54/10 and I R 55/10), the Federal Tax Court acknowledged a tax group for trade tax purposes with a foreign-based parent. The court held that the requirement of a German-based parent under domestic tax law violated nondiscrimination rules under the income tax treaty.

Regarding the taxation of foreign private equity funds, in an August 24 decision (I R 46/10), the Federal Tax Court said it doubted whether the criteria developed by the German tax authorities for the treatment of private equity funds as being engaged in asset management were consistent with applicable law. The decision also elaborated on the domestic permanent establishment criteria, in particular whether a subcontractor's facilities may be considered a PE.

Other German Tax Court Decisions

The Federal Tax Court addressed the deduction of expenses for German income tax purposes in several decisions, including costs regarding the establishment of funds as nondeductible items.

Local tax court cases were decided regarding the change of ownership rules under the German Corporate Income Tax Act, which could lead to a forfeiture of losses in a change in ownership of more than 50 percent. The Hamburg Tax Court held that these rules may violate constitutional law and submitted the case to the German Federal Constitutional Court (April 4, 2 K 33/10). The Dresden Tax Court held that German constitutional law is not violated by the rules (March 16, 2 K 1869/10, now pending at the Federal Tax Court).

Dividends Within the EU/EEA

In *Commission v. Germany* (C-284/09), the European Court of Justice held that Germany failed to fulfill its obligations under article 56 of the EC Treaty (free movement of capital) because it charges a withholding tax on dividends paid to a company registered in another member state or a member of the European Economic Area, but no tax applies in a comparable domestic situation.

Public Rulings

The tax administration issued a long-awaited ruling on reorganizations under the Reorganization Tax Act. The ruling, published in November, covers the entire 2006 Reorganization Tax Act and contains a new, EU-law-based definition of a separate line of business, which is often required for a tax-neutral reorganization. The ruling also addresses tax groups (requirement of financial integration into a reorganized parent), cross-border downstream mergers regarding foreign-based shareholders, and applying for tax-neutral treatment of a reorganization.

A ruling published March 28 allows for the formation of a tax group between a German parent company and its subsidiary that has its registered seat in an EU or EEA member state but its place of management in Germany. The ruling is a response to an infringement procedure initiated by the European Commission.

In November a tax administration working group published its analysis on whether the German tax group taxation system and the loss offsetting rules should be amended. ◆

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