PKF

# Newsletter

**Key Issue:**
Plans for the reform of tax legislation in the USA

03|21

# Dear Readers,

For Europe, the election of Joe Biden as the new US president means an improvement in trade relations with the USA. At the same time, however, companies on both sides of the Atlantic also have to prepare themselves for changes in taxation. To this end, in the Key Issue section of this edition of the PKF newsletter, you will find a preview of the upcoming **US tax reform**, which is generally characterised by significant tax increases.

In the second report in our Tax section, we present the main features of the draft of the **Act on the Modernisation of Withholding Tax Relief** and the Certification of Capital Gains Tax. The aim here is to introduce procedural simplifications for those with restricted tax liability, but also to provide protection, to the greatest extent possible, against abuses and fraud. Next up, we discuss the tax aspects of contributions that are made in a form other than nominal capital. Taking into account legal requirements and current case-law, the **repayment of capital contributions** is an interesting means of distributing equity free of tax to shareholders.

Subsequently, in a further report, we discuss two recent rulings by the ECJ and the German Federal Fiscal Court that relate to the conditions under which a **holding company** would be able to make an **input tax deduction**. In this connection, the distinction between a pure financial holding company and a functional holding company is important. Two rulings likewise constitute the subject matter of the subsequent report where we answer the question on the extent to which deducting **anticipated work-related costs in the case of a semester abroad** is permitted.

In the Legal section we kick off with a discussion of the **draft Act on the European Interconnection of Transparency Registers**. The planned changes will result in an increase in the number of companies that are required to record their beneficial owners in the transparency register from, currently, approximately 400,000 to around 2.3m (!) - a lot of work for companies and their consultants is inevitable. In the next article after that we take a look at the **problem of contestation under insolvency law**. In the run-up to a looming insolvency, debtors frequently attempt to salvage the available private assets from the clutches of the insolvency administrator, e.g., by transferring the assets to spouses or close relatives. The extent to which this is also possible in cases where **property** has supposedly been **sold** too cheaply was an issue on which the German Federal Court of Justice recently had to provide a ruling.

With our best wishes for an interesting read.

Your Team at PKF

Key Issue

Plans for the reform of tax legislation in the USA

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TAX

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# Plans for the reform of tax legislation in the USA

**Shortly after his inauguration, on 20.1.2021, the new President, Joe Biden, started reversing many of his predecessor's decisions and providing new impetus. The Biden administration is likewise planning to make changes in the area of tax legislation in order to roll back some parts of the big overhaul of the US tax code in 2017 (cf. PKF Newsletter 2/2018).**

## 1. Introduction

Ever since the elections in the US federal state of Georgia, at the beginning of January 2021, Biden's party has had a majority in both chambers of the US Congress and, therefore, the possibility of pushing through tax reform. In the following section we have aimed to give an overview of the reform plans that have already been released. However, you should bear in mind that changes to these plans are still possible and/or even probable as no bills have yet been introduced in Congress.

## 2. Income Tax

The intention is to push up the top tax rate for incomes above USD 400,000 from currently 37% back to 39.6%.

Furthermore, this rate would also apply to long-term capital gains (holding periods of more than one year) if the overall income adds up to more than USD 1m. Up to now, a special tax regime has been applicable to long-term capital gains that provides for a top tax rate of just 20%.

Recipients of income above USD 400,000 would, in future, contribute more to social security (social security tax). Up to now, the income cap for social security tax was USD 142,800 (status date: 2021) with a 12.4% contribution rate that is evenly split between employers and employees. In future, incomes above USD 400,000 would once again be liable to social security tax with no upper limit. Therefore, only recipients of incomes between USD 142,800 and USD 400,000 would be exempt from additional social security contributions.

**Please note:** This would also mean a noticeable increase in personnel costs for employers given that the proportional social security tax contributions (6.2%) for salary payments above USD 400,000 would have to be taken into account.

### 3. Estate and gift taxes

The intention is to raise the top rate of estate tax applicable at the federal level from 40% to 45%. Moreover, the applicable lifetime exemption for 2021 would be reduced from USD 11.58m to USD 3.5m per person. The generous lifetime exemption for estate and gift taxes would therefore be reduced by almost 70% and would, thus, be rolled back to the level that applied when President Obama assumed office in 2009.

Furthermore, there are plans to put a stop to frequently used structuring possibilities where individual assets are contributed to business assets and then stakes in the respective company are transferred. To date, up to 40% in estate and/or gift taxes could be saved as it has been possible to apply so-called valuation discounts on business assets.

### 4. Corporate income tax

The intention is to increase corporate tax rates, too. The Federal tax for enterprises that are treated as corporations under US tax law would be increased from the current rate of 21% to 28%. If the other tax charges at the level of the Federal States, - which may vary from Federal State to Federal State -, are taken into consideration then this could potentially result in an overall tax burden for corporations of approximately 36%.

In future, corporations in the USA would have to pay tax on profits that have been generated abroad at a rate of 21% instead of 10.5% currently. This rule would apply to corporations with foreign shareholdings where the corporation holds at least 50% of the shares (so-called controlled foreign corporations, or CFCs for short). Profits from these CFC shareholdings are then already taxed if they arise in the foreign country and not just subsequently when the profits are transferred to the USA as a profit distribution to the parent company. However, this does not include CFC shareholdings in those countries where the effective tax rate is the equivalent of at least 90% of the US Federal tax rate for corporations. In the event of an increase in the US Federal tax rate to 28%, the only CFC shareholdings that would then be excluded would be the ones based in those countries with an effective tax rate of, at least, 25.2%.

**Please note:** Therefore, shareholdings in German corporations whose effective tax rate is normally approximately 32% should thus generally be unaffected by this rule.

Biden, just like his predecessor, would like to create more jobs in the USA and to stop production operations being shifted overseas. To this end, the intention is to create new incentives for companies, such as, e.g., in the form of a 10% “Made in America” tax credit for investing in the revitalisation of production facilities in the USA or providing substantial salary increases for employees who work in production.

By contrast, companies that shift their production operations overseas would be penalised. It is envisaged that this would entail applying a surtax on the profits generated as a result of shifting production facilities overseas (a so-called offshore penalty tax) as well as a prohibition on the tax deduction of the outlay spent on shifting the production operations overseas.

## Conclusion

German corporations with subsidiaries in the USA will essentially be affected by the increase in the tax rates resulting from the planned tax reforms. Nevertheless, further investments in locations and production capacities could be a sensible course of action as the “Made in America” tax credit could, potentially, compensate for the effects of the increase in the tax rate.

StB [German tax consultant] Sabine Rössler

# Withholding capital gains tax – Plans to simplify procedures

**On 20.1.2021, the German Federal Cabinet adopted the draft bill on the Modernisation of Withholding Tax Relief and the Certification of Capital Gains Tax Act *(Gesetz zur Modernisierung der Entlastung von Abzugsteuern und der Bescheinigung von Kapitalertragsteuer, AbzStEntModG)*. The aim of this is to optimally streamline the procedure for providing relief from capital gains tax and withholding tax for taxpayers with restricted tax liability, under Section 50a of the Income Tax Act *(Einkommenssteuergesetz, EStG)*, at the Federal Central Tax Office *(Bundeszentralamt für Steuern, BZSt)* and to provide protection, to the greatest extent possible, against abuses and fraud. Furthermore, ECJ rulings had made it necessary to revise Section 50d(3) EStG in the area of withholding tax relief.**

### 1. Digitalisation of the procedure ...

The BZSt is responsible for, among other things, capital gains tax relief for capital gains recipients based in a foreign country. To this end, data is already being collected at the BZSt on "declarations for exemption from withholding tax" that have been issued. From 2024 onwards, it will basically be mandatory to file applications electronically and to retrieve assessment notices electronically as well as to transmit the data electronically for the tax certificates issued for capital gains.

### ... with a database for capital gains tax

Generally, electronic reporting requirements would expand the withholding procedure for capital gains tax; by centralising the collection of reports at the BZSt the aim is to make it easier to identify arrangements that attempt to circumvent the taxation of dividends. This comes in response to the schemes that became known under the terms cum-ex, cum-cum and cum-fake. The information will be used by the fiscal authority – and in this case, in particular, the special unit set up at the BZSt – for the purpose of analysing and monitoring.

### 2. Tougher liability for tax certificates

In the future, issuers of incorrect tax certificates will be held liable for all the information that should be included on a tax certificate. Furthermore, they would also be liable in the event of a faulty transmission of data. The required data will provide important information for uncovering the truth in the case of share transactions that are particularly susceptible to the creation of "constructs" around the dividend record date.

In particular, in the event of incorrect information from the capital gains debtor or by means of a statement from the issuer of the tax certificate to the tax office that the issuer had not got back an incorrect tax certificate, up to now, it had been possible to avoid a liability claim against the issuer of the tax certificate. In future this will cease to apply.

### 3. Section 50d EStG will be updated and "divided up"

The intention is to transfer the current provisions under Section 50d EStG – which relate to relief from capital gains tax or from withholding tax for those with restricted tax liability in the case of royalties, or similar, on the basis of the EStG or a DTA – to a (new) Section 50c EStG. There would be no change in the requirement for tax to be withheld for the above-mentioned income.

Two procedures would be available for capital gains tax relief, namely, exemption in the course of the withholding procedure on the basis of an existing exemption certificate, or a refund of the tax that was withheld on the basis of an exemption notice. Remuneration for a debtor of up to € 5,000 annually (e.g., for royalties under a DTA) may be paid out without, or with a reduced tax deduction. The hitherto applicable recording procedure (Kontrollmeldeverfahren) will be abolished.

A certificate of exemption would, in the future, no longer have a retroactive effect. In the future, a certificate of exemption would only be effective from the date of its issue and, moreover, would be valid for a maximum of 3 years. Only creditors of the capital gains may apply at the BZSt for a certificate of exemption.

If the tax has already been paid then relief could only be claimed through a refunding procedure.

**Please note**

In any case, the debtor has to submit a withholding tax return even if, because of an exemption, no taxes have been withheld and paid.

StB [German tax consultant] Thorsten Haake

# Tax-free repayment of capital contributions from foreign corporations

**A shareholder may generally receive payments free of tax if they originate from the profit distributions of a corporate body and if these payments can be deemed to have been made out of a so-called 'contribution account' for tax purposes (Section 27 Corporation Tax Act [*Körperschaftsteuergesetz, KStG*]). Under specific conditions, this can also apply to corporate bodies that are liable to pay tax in other EU member states. A ruling to this end, issued by a German court, extended the scope of application of this tax exemption also to third country entities. The Federal Fiscal Court *(Bundesfinanzhof, BFH)* confirmed this once again in a recently published ruling and, in doing so, also expressed its opinion on the differences in the possibilities for entities from the EU and from third countries to provide evidence of the repayment of capital contributions.**

## 1. Definition of the basic problem and the rules for corporations resident in Germany

Applying tax privileges at the level of the shareholder to the repayment of nominal capital as well as capital contributions by a corporation is necessary for systematic reasons because the paying in of these amounts did not give rise to any tax-deductible expenses for the shareholder. From the shareholders' point of view, paying in the contribution merely increased the acquisition cost of their shares in the entity. Consequently, the repayment of nominal capital and/or capital contributions has to be offset against the acquisition cost of the shares in the entity, generally, in a way that does not affect the operating result for tax purposes.

An exception applies to nominal capital arising from a capital increase from company funds where retained earnings are used. Such components of nominal capital have to be separately assessed for tax purposes (so-called separate statement). The repayment of nominal capital is treated like a distribution of retained earnings. While the repayment of nominal capital may be immediately treated as tax-exempt, for the repayment of capital contributions in the context of a profit distribution, however, a specific appropriation sequence has to be fol-

lowed; here, the so-called distributable profit has to be appropriated first. Furthermore, the tax-free repayment of capital contributions is restricted to the amount that has been determined in the course of a separate assessment of the contribution account for tax purposes.

**Please note:** A further advantage of repaying nominal capital as well as amounts from the contribution account for tax purposes is that the entity that distributes the profits does not have to withhold any capital gains tax. This is on condition that the entity that distributes the profits promptly provides the shareholder with a tax certificate that correctly indicates the use of funds from a contribution account for tax purposes.

### 2. Repayment of capital contributions from EU corporations

Since the rules for the assessment of the contribution account for tax purposes, in Section 27(1)-(6) KStG, apply solely to corporations in Germany with unlimited tax liability, for many years, there was the problem that foreign corporations were procedurally not able to certify the use of funds from a contribution account for tax purposes. Consequently, shareholders resident in Germany were likewise unable to benefit from the tax-free repayment of capital contributions from foreign corporations. There were concerns here, in particular, in relation to EU law.

Therefore, in 2006, the German SE Introductory Act created a separate assessment procedure for EU corporations (Section 27(8) KStG). The foreign corporation can request a separate assessment of the amount that may be considered as the repayment of capital contributions. The non-extendible deadline for applying for an assessment is however very tight and only runs to the end of the calendar year following the calendar year in which the repayment of capital contributions was made.

In practice, filing an application for an assessment has often proved to be very work-intensive because of the fiscal authority's stringent requirements with respect to documentary evidence. In extreme cases, this can mean that the foreign corporation has to reconcile – as if in a set of shadow accounts – the differences in its presentation of equity and one based on the German principles for tax accounts and going all the way back to 1.1.1977 (the introduction of the corporation tax imputation system in Germany).

While this is not consistent with Section 27(8) KStG, the fiscal authority also wants to include corporations that are resident in the EEA states within the scope of the application of the rules.

### 3. Repayment of capital contributions from corporations in third countries

According to a BFH ruling from 13.7.2016 (case reference: VIII R 47/13), restricting the scope of application of the rules on the repayment of capital contributions to corporations that are resident in Germany and in the other EU member states violates not only the general principle of equal treatment under Article 3, paragraph 1 of Germany's Basic Law, but also the free movement of capital for third countries that is applicable under EU law. Therefore, the BFH granted shareholders of corporations in third countries the possibility to provide proof, on the basis of their own tax assessment procedures, that the profit distribution by the subsidiary is indeed the repayment of capital contributions. In its ruling from 10.4.2019 (case reference: I R 15/16), the BFH then confirmed this decision.

The key advantage of this ruling for shareholders of a non-EU corporations in relation to the application of Section 27(8) KStG is that the ruling is not tied to the very short preclusion period. Although, in specific cases, the degree of practical difficulties with regard to providing proof could be similarly high. Whether or not tax accounts, for example, can be drawn up under analogous application of German law was left open by the BFH.

In a further, recently published, ruling on this issue from 27.10.2020 (case reference: VIII R 18/17), that concerned a subsidiary company in Austria, the BFH established that the concurrent existence of the assessment procedure in accordance with Section 27(8) KStG, on the one hand, and the ruling on the repayment of capital contributions from third countries, on the other hand, does not constitute unconstitutional unequal treatment. However, from the ruling it is also possible to infer that the lack of an individual possibility to provide proof of repayment of capital contributions within the scope of the assessment procedure for the shareholder in cases in the EU could, potentially, constitute an infringement of the free movement of capital.

### Recommendation

The above-mentioned BFH rulings have, so far, not been published in the Federal Tax Gazette (Bundessteuerblatt), which means that they are not generally applied by the fiscal authority. If you already have a situation where the repayment of capital contributions from abroad has been effected or is being planned then, please, do not hesitate to contact us so that the possibilities for applying the latest ruling can be considered.

StB [German tax consultant] Steffen Zipperling

# Latest news on input tax deduction for a holding company

**A so-called functional holding company or management holding company is deemed to be a business that has to register for VAT if its sole purpose is not merely to acquire interests in other companies, but if it also intervenes, directly or indirectly, in the management of these companies. A functional holding company is generally entitled to make input tax deductions insofar as it intends to use the incoming supplies for its business and for the provision of paid services. These principles for distinguishing, for VAT purposes, between a pure financial holding company and a functional holding company have already been confirmed several times by the ECJ and, in this connection, two recent rulings should be noted.**

### 1. Input tax deduction despite an acquisition ultimately not having been carried out (ECJ from 12.11.2020)

In a case that reached the ECJ, the issue was whether or not a holding company should be allowed to deduct input tax even if the acquisition of a subsidiary that was originally planned is ultimately not carried out. The holding company operated in the telecommunications sector and provided taxable management services to some of its subsidiaries. This was also the plan for a subsidiary that would have been newly acquired. In preparation for the intended acquisition the holding company purchased external consultancy services relating to market research. In order to finance the planned acquisition, the holding

company issued a bond in order to the raise necessary funds. In this connection, the holding company paid a fee to the investment bank that had been commissioned to arrange and execute the bond. However, the acquisition of the subsidiary fell apart and so the capital that had been raised via the bond issue was made available to the parent company as a loan. The holding company claimed an input tax deduction not only in respect of the expenditure for the consultancy services but also the fee paid to the investment bank. In a recent, ruling from 12.11.2020 (case: C-42/19), the ECJ had to decide whether or not this input tax deduction had been rightful and proper.

The ECJ allowed the respective amount of VAT payable for the consultancy services to be deducted as input tax. The decisive factor was that the services received were linked to the acquisition of an associated company for which the holding company had intended to provide management services in return for payment. In principle, the existing entitlement to deduct input tax remains unaffected even for preparations that ultimately were to no avail, insofar as such activities can be attributed to future business activities.

The situation is different in the case of the VAT paid in respect of the fee. Here, the ECJ considered it to be relevant to the issue that, by deviating from its original intention, the capital that had been raised via the bond was used for a tax-exempt activity, namely, extending a loan, free of tax, to the parent company. Consequently, as the fee expenses thus had to be attributed to excluded transactions that are 'harmful' to input tax deductibility, the ECJ refused to allow the respective deduction of the applicable amounts of input tax.

## 2. The Federal Fiscal Court's order for reference with respect to structuring models that enable input tax deduction *(Vorschaltmodellen)*

The Federal Fiscal Court (Bundesfinanzhof, BFH), in its ruling from 23.9.2020 (case reference: XI R 22/18), referred to the ECJ for a preliminary ruling the issue of whether or not a functional holding company should be allowed to deduct input tax even in the constellation of circumstances outlined in the overview below, which are considered to constitute a structuring model that enables input tax deduction (referred to in German as a Vorschaltmodell).

The holding company, as a German limited partner, held stakes in two German limited partnerships for which it provided taxable management services in return for payment; as a functional holding company it was therefore basically engaged in business activities. The limited partnerships acquired plots of land on which they then put up residential buildings with the aim of selling the developed plots (VAT-exempt activity of real estate development). While the other partners made their equity contributions in cash, the holding company contributed its share of the equity by providing architectural services. In order to fulfil its obligation to make an equity contribution, the holding company also purchased services from third parties and sought to deduct the input tax from their invoices. Unlike the tax office, the tax court allowed the input tax deduction. Providing benefits in kind as an equity contribution can also be classed as a business activity.

The BFH however considered it to be doubtful that the incoming supplies that the holding company had passed on to the limited partnership as the partner's equity contribution had been purchased for its business. In particular, the BFH also saw the risk of misuse because, by artificially putting in place a managing holding company, it could be possible to achieve an input tax deduction that would not be compatible with the system and to which neither the subsidiary nor the holding company would otherwise have been entitled.

*Recommendation*

In this respect, until there is a ruling from the ECJ, such structuring models should be avoided. Furthermore, it remains to be seen if the ruling discussed in section 1 could also give rise to a new discussion of the issue of whether the (first-time) input tax deduction has to be based on the planned or on the subsequent actual use of the incoming supplies.

# Anticipated work-related costs in the case of a semester abroad

**In the context of higher education, for the purpose of deducting allowable expenses a distinction is made between undergraduate studies and second degrees. The costs for a course of study can generally be taken into consideration as anticipated work-related costs if vocational training has already been completed and the course of study is related to a future occupation. Which costs may be deducted as work-related costs is open to debate here – in particular, in relation to a semester abroad.**

### 1. A semester abroad during a master's degree course

The treatment of grants to students in the context of a semester abroad, in the case of a student who had completed a semester abroad in the USA during her master's degree course in law, was the issue that the Munich tax court had to deal with in its ruling from 16.6.2020 (case reference: 5 K 1936/19). The student, S1, was granted an allowance for her master's degree course, free of tax, by the German Academic Exchange Service (DAAD). Following her semester abroad, S1 worked as a German lawyer. The advanced training costs that S1 offset, against tax, as work-related expenses in connection with the semester abroad in the USA were recognised by the local tax office after deducting the travel subsidy, the tuition fee subsidy as well as the monthly grant allowance payments. The income tax assessment notices as well the notices of ascertainment of losses were accordingly issued for the relevant years, however, S1 applied to have the work-related costs recognised without the deduction of the grant allowance payments.

The student's claim was unsuccessful before the tax court. In principle, the costs in respect of her master's degree course were anticipated work-related costs in relation to her income from employment. However, it was only possible to deduct those costs that actually were a financial burden for the taxpayer. In the opinion of the tax court, it was rightful and proper for the local tax office to deduct the tuition fees that had been assumed as well as the monthly grant allowance. Permission was granted to lodge an appeal and it is pending before the Federal Fiscal Court (case reference: VI R 34/20).

### 2. A semester abroad as a tax-privileged period of working away from home where this has been preceded by vocational training

In a similar case, a student, S2, who had successfully completed her vocational training, took up a course of study at a German university and, as stipulated in the rules and regulations of the study programme, spent one semester studying abroad at a partner university. During the period of this compulsory semester abroad, S2 applied for the extra accommodation costs and additional subsistence expenditure arising from this to be recognised as work-related costs. The student's claim was part of a test case funded by the German Taxpayers' Association.

In view of the fact that the rules and regulations of the study programme stipulated that one semester had to be spent studying abroad and, during this period, the students were nevertheless still enrolled at the German university, the BFH (Bundesfinanzhof, BFH) in its decision from 14.5.2020 (case reference: VI R 3/18) ruled in favour of S2. The semester abroad was a tax-privileged period of working away from home as the German university remained the primary workplace for tax purposes. This was a case of anticipated work-related costs that may be deducted even if two households do not have to be maintained and, thus, opens up the possibility of a loss carry-forward in subsequent calendar years.

**Please note**

It remains the case that the costs of initial vocational training or undergraduate study may not be deducted as work-related costs. The expenditure here can only be taken into account within the scope of a special expense deduction and will, at best, have a tax effect if, in the year when the expenses arise, the student has taxable income.

## LEGAL

RAin [German lawyer] Andrea Köhler / Lena Wagner

# Transformation of the transparency register – Instead of the presumption of notification *(Mitteilungsfiktion)* there will now be new obligations backed up by fines

**In accordance with the EU anti-money laundering directive, the transparency registers of the EU member states have to be interconnected with each other by 10.3.2021. On 10.2.2021, just shortly before this deadline, the Federal Government published a draft Act on the European Interconnection of Transparency Registers and to Implement the EU Directive (EU) 2019/1153 (Transparency Register and Financial Information Act). Businesses and consultants should expect a considerable amount of additional administrative work.**

### 1. Changes are required to the way that obligations to notify are fulfilled

According to Section 20(1) of the Anti-Money Laundering Act *(Geldwäschegesetz, GwG)*, companies that are subject to notification obligations are generally required to have the beneficial owner recorded in the transparency register. Up to now, under Section 20(2) GwG, this obligation to notify was in many cases deemed to have been fulfilled if the information on the beneficial owner was already contained in an electronically accessible register (in particular, the commercial register, the register of cooperatives and the register of associations) *(the so-called presumption of notification, referred to in German as Mitteilungsfiktion)*.

A prerequisite for the forthcoming interconnection of the transparency registers of the individual EU member states is that the respective data records for the beneficial owners have to be available in a standard data format. The Federal Government is therefore planning to amend the Anti-Money Laundering Act (GwG), particularly in relation to the requirements in respect of the transparency register.

### 2. Changes to the rules on the transparency register

### 2.1 Elimination of any presumption of notification

The draft Act provides for the removal of this presumption of notification. As a consequence, all the companies that are subject to the notification obligation, from now on, will be obliged to notify the transparency registry of their beneficial owners. Therefore, when the draft Act comes into effect, there will be a sudden increase in the number of

companies that are required to record their beneficial owners in the transparency register from, currently, approximately 400,000 to around 2.3m.

### 2.2 A comprehensive register instead of a 'backstop' register

As a result of the removal of the presumption of notification it will no longer be possible to make reference to other registers. In fact, the current format of the transparency register will be transformed from that of a so-called backstop register into a 'complete' register (comprehensive register) that contains data records with a standard structure.

### 3. Staggered introduction of notification obligations as well as penalties for breaches

The Act is due to come into force on 1.8.2021. The companies that have hitherto benefited from the presumption of notification will be required to provide information on the beneficial owners – depending on the legal form – during staggered transitional periods:

» for an AG [*a German public limited company*], an SE [*a European public limited company*], a KGaA [*a partnerships limited by shares*] by 31.3.2022,
» for a GmbH [*a German limited company*], cooperatives and partnerships by 30.6.2022 as well as
» in all other cases by 31.12.2022.

You should bear in mind that breaches of the obligation to notify, in the form of incomplete, incorrect or late notifications, could lead to the imposition of considerable fines. This threat of fines is expected to lead to a swift transformation of the transparency register into a comprehensive register.

### Conclusion

The planned changes will result in a substantial amount of additional work. The companies will be responsible for the completeness and accuracy of the information and it will have to be kept up to date at all times.

RA/StB [German lawyer/tax consultant] Frank Moormann

# Insolvency – Contesting the sale of a property below value

**In the run-up to a looming insolvency, debtors frequently attempt to salvage the available private assets from the clutches of the insolvency administrator, e.g., by transferring assets to spouses or close relatives. If this happens within a period of four years prior to filing for insolvency proceedings by way of gifting then, according to Section 134 of the Insolvency Code (Insolvenzordnung, InsO), the transfer may be contested. The extent to which this is also possible where assets have supposedly been sold too cheaply was an issue on which the Federal Court of Justice *(Bundesgerichtshof, BGH)* recently had to provide a ruling.**

### 1. Issue – Sale price below value

In the case that was decided by the BGH, a father who subsequently became an insolvent debtor had sold a single-family home to his (student) son. A purchase price of € 395k had been agreed. This amount was the "roughly estimated market value" that had been ascertained by an expert consultant shortly before the sale. The purchase price was secured by assuming bank debts (€ 214k) and creating a lifelong residential right in rem for the benefit of the father (€ 181k).

The insolvency administrator was however of the opinion that the property was worth at least € 600k and, therefore, officially announced that he would contest its transfer.

### 2. Basic principle – The burden of proof lies with the insolvency administrator

First of all, the court confirmed the basic principle that contesting is not an option if both parties are satisfied, in good faith, of the equivalence of their gains even if this subsequently turns out to have been false. Therefore, an insolvency administrator carries the burden of presentation and of proof not only for the imbalance in respect of the gains, but the administrator also has to prove that there had been no objective circumstances that allowed the assumption of equivalence.

**Please note:** In this respect, the first two courts made reference to the expert consultant's report and, thus, dismissed the contestation of the gift.

### 3. Easing of the burden of proof where there are indications of disguising as a gift

For the BGH however this was too short-sighted and in its ruling, from 22.10.2020 (case reference: IX ZR 208/18), it referred the case back to the appeal court for a renegotiation and a decision. In the opinion of the BGH, circumstances had indeed been brought forward that contradicted the notion that the parties had assumed that there was parity in terms of value. The lower courts did not sufficiently appreciate this.

» The transaction was one between two close relatives; moreover, the buyer (son), as a student, had no income of his own.
» Shortly before the transfer, tax investigators had searched the father's premises and had taken business records.
» The expert consultant had only surveyed the property one day prior to the notarisation of the transfer; when the property was being transferred the expert's report was not even available in written form and, furthermore, the value that had been determined was described as "roughly estimated".
» Finally, there was no detailed valuation of the agreed residential right but, instead, an all-inclusive amount was applied.

## Recommendation

To avoid giving the impression of a disguised gift and in order to structure an asset transfer so that it will be as non-voidable as possible, in the run up to the transaction, a proper expert opinion on the fair market value should be obtained from a publicly appointed expert consultant.

# Internet sales – Threshold for classification as a business

**Occasional private sales on the internet will usually have no tax consequences. If the internet sales continue to grow, however, there is a risk that the threshold level between what constitutes tax-exempt private sales and taxable commercial selling will be breached.**

The Federal Fiscal Court *(Bundesfinanzhof, BFH)* has set out the criteria for differentiating between private sales and commercial selling in its ruling from 17.6.2020 (case reference: X R 26/18). The ruling was prompted by a Ms F who, from 2009 to 2013, had bought up items from household clearances and had listed them for sale on eBay with a minimum bidding price of € 1. In the course of a tax investigation, it was discovered that with around 260 – 1,057 auctions every year she had generated annual sales of between € 40,000 and € 95,000. Ms F took legal action against the income tax and trade tax assessment notices that were issued after she was classified as a commercial seller; in doing so, she pointed out that she was not in the business of selling because she had neither a business plan nor previous experience in retailing and only occasionally purchased items from household clearances. Her priorities were the thrill of the auction and enjoying the haggling.

However, the BFH did not share Ms F's view and ruled that classifying her activities as commercial selling was appropriate. The lower court had taken into consideration not just the period of time and the volume of sales as well as the amount of revenues, but had also based its argument on the methodical purchasing and selling. The woman had systematically bought up her goods at household clearances and had then sold them on eBay, therefore, it had to be to presumed that there had been a structured approach.

Moreover "enjoying the haggling" is not a suitable criterion for distinguishing private sales activities from commercial selling. Furthermore, the BFH expressly pointed out that for a presumption of commercial selling the person doing the selling does not have to perfectly match the ideal profile for a trade professional.

**Recommendation**: Therefore, online sellers who meet the criteria for being classified as a business should declare their sales and profits to the tax authority early on. Otherwise, commercial sellers will be at risk of having to make considerable additional tax payments and interest payments as well as, potentially, facing legal proceedings in respect of tax evasion.

# Flat-rate tax on non-cash benefits – The costs for the external setting of a business event have to be included

**Business-related benefits for employees that are provided by employers in addition to the remuneration that would in any case be due may be taxed on the payroll at a flat rate of 30%. In this case, employers assume the payment of the flat-rate tax while employees do not have to declare the benefit in their income tax returns.**

The Federal Fiscal Court *(Bundesfinanzhof, BFH)*, in its ruling from 7.7.2020 (case reference: VI R 4/19), took a closer look at this flat-rate taxation. In the case in question, the employer had used flat-rate taxation years ago to pay tax on benefits arising in connection with a business function. The local tax office had additionally included the costs for the external setting for the event in the assessment base for the payroll tax (e.g., rent for the hall, technical equipment, portable toilet cabins). After the employer's challenge before the tax court was dismissed, the BFH ruled in favour of the local tax office because, according to the wording of the German Income Tax Act, the taxation has to be applied to all "the taxpayer's expenses, including VAT". Therefore, this includes the costs for the external setting of the event. In the opinion of the BFH judges, with respect to the inclusion of costs, it does not matter whether the employer's expenditure produces a specific benefit for the employee.

**Please note:** The BFH merely excluded the costs for advertising materials from the assessment base for the flat-rate tax, since the purpose of such expenditure was not the event itself but, instead, in-house advertising or promoting the public image for the employer.

## AND FINALLY...

*"Imagine a world in which every single person on the planet is given free access to the sum of all human knowledge. That's what we're doing."*

**Jimmy Wales,** born 7.8.1966 in Alabama/USA, US American internet entrepreneur, co-founder of the online encyclopaedia Wikipedia.

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