PKF

Newsletter

Key Issue:
New administrative principles for transfer pricing

10|21

Dear Readers,

We have a presentation of the **new administrative principles for transfer pricing** in the Key Issue section of the October edition of our PKF newsletter. This is because, to a certain extent, the German fiscal authority has gone far beyond OECD requirements here. We have analysed the administrative principles to determine the issues that can be expected to create potential for conflicts with tax auditors. In the second contribution in our Tax section, we continue our series of articles on the **option model** according to which members of **partnerships** will be able to elect to have their companies **taxed as corporations** from the beginning of 2022. In this regard, the main focus in this edition is the treatment of so-called **special assets** where there is a risk either of changes in the size of shareholdings or the realisation of hidden reserves. Next up, we critically examine a tax court ruling where an appraisal of **intra-group allocations** gave rise to the assumption of a **constructive dividend**. The fact that the Hamburg judges failed to accept, for tax purposes, not just an unreasonable share of the allocations but, instead, the entire transaction is problematic as this could have a negative ripple effect on many other intra-group relationships. By contrast, a further ruling that we discuss in our fourth report is encouraging. In this, the judges who rule on fiscal matters disregarded the legal situation and decided that **withholding tax may** also be **credited against trade tax** if it has not been possible to offset the credit against corporation tax. Subsequently, we give a brief overview of how **gifting arrangements** can allow you to achieve **tax advantages** and still provide for the future of the donor. Furthermore, you will be provided with two pieces of advice about how even after the accrual of an inheritance advantages can still be realised.

In the Legal section there is an overview of the **registration requirements** that arise for companies if **packaging** is imported or filled and used on a commercial basis; this thus, by no means, affects merely producers but also retailers.

We continue our series of illustrations of the PKF locations - this time it is Munich. Bavaria's state capital is worth a visit even when there is no Oktoberfest.

With our best wishes for an interesting read.

Your Team at PKF

Victory Gate

Front cover photo: Cathedral of Our Lady and the Town Hall

Key Issue

New administrative principles for transfer pricing

Contents

TAX

Dr. Oliver Treidler

The new administrative principles for transfer pricing – An initial appraisal of the practical impact

The German fiscal authority published new administrative principles for transfer pricing on 14.7.2021; these came into effect immediately and will apply to all assessment periods that are still open. The new administrative principles now refer directly to the OECD Transfer Pricing Guidelines, which are attached to the administrative principles as an appendix, and should ensure dynamic alignment with future developments in the international context.

1. Background

The new administrative principles replace, amongst others, the 1983 administrative principles as well as parts of the 2005 administrative principles procedures that were not updated in December 2020. They also follow on from the transfer pricing updates in the External Tax Relations Act (Außensteuergesetz, AStG) in May 2021 and should ensure that, in Germany, the interpretation and application of the arm's length principle will be harmonised with the post-BEPS Transfer Pricing Guidelines. Moreover, there have also been a number of systemic changes.

The new administrative principles consist of six chapters in total. In the following section we discuss the most important regulations (unless otherwise indicated, the referenced/cited paragraph numbers relate to these).

2. Assessing the arm's length nature of a transaction

Paragraph 1.5 could be regarded as a kind of leitmotif for the administrative principles. According to this paragraph, by applying the arm's length principle the aim is not merely to adjust a transfer price but, instead, also includes the basic idea behind the transaction (i.e., the general conduct of the parties) as well as the terms and conditions of the respective business relationship. While the OECD also focuses on the need to perform an analysis of the general circumstances of the taxpayer and to adequately define the controlled transactions, the German administrative principles appear to overemphasize this aspect. This is also reflected in, among others, paragraph 1.22, according to which, apart from the price, the terms and conditions (e.g., contract period, payment terms, discounts and bonuses) and also adjustment clauses, collateral as well as clauses for amending and terminating contracts could per se be subject to the application of the arm's length principle and trigger a transfer price adjustment.

Please note: This leitmotif - particularly in conjunction with the administrative principles that were amended in December 2020 - could be a harbinger of (more) controversial discussions during future tax audits. Tax auditors could feel compelled to require extensive explanations on the arm's length nature of individual terms and conditions; this would not only increase the compliance burden (and the burden of proof) for taxpayers but would also call into question the holistic approach for the application of the arm's length principle (including outcome-oriented approaches).

3. Economic substance, risk control and the hypothetical arm's length test

Alignment with the OECD Guidelines implies that transfer pricing regulations reflect a view of the arm's length principle that is characterised by economics where the functional and risk analysis is the most important feature.

3.1 Value chain analysis

Paragraph 3.7 stipulates, among other things, that a value chain analysis has to be carried out to provide the basis for determining whether or not the apportionment of profit within a multinational enterprise adequately matches the functional and risk profiles of the individual entities. Here, however, the provision is unclear as to the cases where taxpayers would be expected to perform a value chain analysis that goes beyond a functional and risk analysis in the sense of quantifying the individual value-creating contributions.

3.2 Arm's length test

With respect to transfer pricing methods, a strong emphasis is placed on the so-called hypothetical arm's

Olympic Tower and
the roof of the Olympic Stadium

length test, i.e., the use of economic valuation methods (such as, e.g., discounted cash flow). According to paragraph 3.12, the hypothetical arm's length test has to be applied instead of traditional transfer pricing methods if the latter do not provide sufficiently reliable results (e.g., due to a lack of an adequate level of comparability). It further states that the hypothetical arm's length test has to be 'generally' applied to transactions that involve (all kinds of and not just the difficult-to-value) intangible assets, business restructurings and transactions for which the profit apportionment method is used but for which no comparables can be identified.

3.3 Risks for taxpayers

From a taxpayer's perspective, the risk is that the fiscal authority, in conjunction with the wide-ranging obligations to disclose and provide internal information (planning data, etc.), could effectively use the hypothetical arm's length test as an instrument for scrutinising any analysis prepared by the taxpayer on the basis of OECD transfer pricing methods.

Please note: In this connection, an interesting side note is that, according to paragraph 3.14, taxpayers are expected to explain all discrepancies, which might be detected, between valuations performed for non-tax purposes and those for transfer pricing purposes.

4. Other transfer pricing issues

The German administrative principles include regulations on some practical issues that reflect certain unnecessary idiosyncrasies. First of all, in the case of price-adjustment clauses, they do not distinguish between intangible and difficult-to-value assets (paragraph 3.52) and, moreover, it would appear that the German fiscal authorities are generally unwilling to make this distinction (cf. comment above on paragraph 3.12). Consequently, in future, all intangible assets could be subjected to a more detailed examination during an audit.

For intra-group services, the new German administrative principles make reference to Chapter VII of the OECD Guidelines. However, something that is missing in this context is a reference to or inclusion of the documenta-

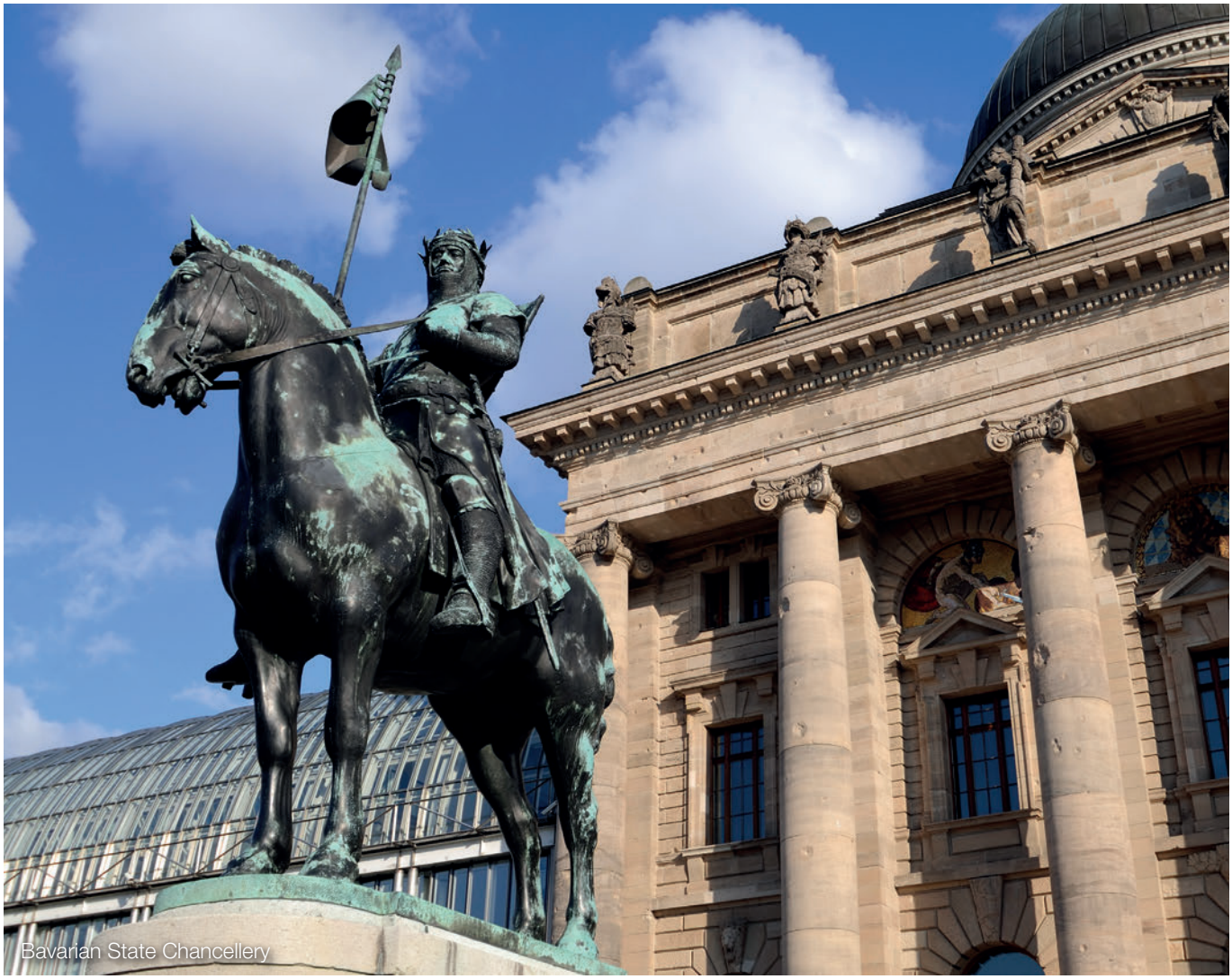
tion related to a ‘simplified approach’ (or the concept of such a simplified approach). Instead of a cross-reference to paragraph 7.64 of the OECD Guidelines, paragraph 3.78 of the German administrative principles stresses the taxpayer’s wide-ranging documentation requirement.

Please note: In other words, in the case of remuneration for services rendered, the allocation of costs is likely to remain an area of potential conflict and high administrative expenses for taxpayers.

One of the, possibly, most interesting developments is the fact that the construct of a so-called ‘hybrid entity’ has apparently been removed from the German transfer pricing rules (at any rate, this seems to be implied in paragraph 3.33). In the past, this classification of a company, which exhibits the features of an entity that performs routine functions as well as of an entrepreneurial entity, sometimes made it difficult to align German transfer pricing rules with international regulations, in particular, when it came to classifying the contracting parties and the use of the transactional net margin method.

Conclusion and recommendation

It is certainly a welcome development that the fiscal authority has aligned its new administrative principles more closely with the international OECD Guidelines and, in the international debate, national perspectives should increasingly fade into the background. Nevertheless, it cannot be denied that, due to the very wide scope of application (in terms of both content as well as time), new areas of discussion will open up. Consequently, all taxpayers with cross-border business relationships would be well advised to re-examine their existing documentation of transfer prices with a view to potential problem areas. However, the real challenges will only become apparent in the course of future tax audits.



Bavarian State Chancellery

WP/StB [German public auditor/ tax consultant] Tanja Schmitz / Benedikt Helling

New option model for partnerships – Part II The effects of the notional change of legal form on special business assets

In Part I, in the PKF newsletter 9/2021, we started our series of detailed explanations of the German Act on the Modernisation of Corporation Tax Law, which was promulgated on 30.6.2021, with a comparison of the various systems of taxation for partnerships and corporations as well as a look at the process of exercising the option; in Part II, in this newsletter, we discuss the consequences of exercising the option through a notional change of legal form with particular reference to the special business assets.

1. The background to the change in taxation

As of 1.1.2022, partnership organisations and professional partnerships (Personenhandelsgesellschaften, a German type of professional corporation) will have the possibility, by way of the option, of using the same tax regulations as corporations. This should eliminate the differences that exist within the framework of German business taxation for the partnerships that exercise the option.

Please note: The Act on the Modernisation of Corporation Tax Law (Gesetz zur Modernisierung der Körperschaftsteuer, KöMoG) was promulgated in the Federal Law Gazette (Part I No. 37, p. 2050) on 30.6.2021, although the Act will, for the most part, come into force on 1.1.2022 it also partially came into force immediately after it was promulgated.

While a transition to corporation tax sounds simple at first, nevertheless, it can indeed entail pitfalls in view of the particularities that apply to the taxation of partnerships under German tax law. In this regard, the special business assets of co-entrepreneurships assume particular importance.

2. Transitioning to taxation in accordance with the German Corporation Tax Act

Exercising the option to be treated as a corporation for tax purposes is handled like a notional change of legal form of a commercial partnership into a corporation, although the Reorganisation Tax Act is directly applicable. For a tax neutral transfer, the change of legal form would have to take place at book value. However, in order to be able to file an application for the book values to be rolled over (or for recognition at intermediate values) all the assets that form part of the business assets that are essential for operations have to be transferred to the enterprise making the acquisition. This rule also applies to assets held as special business assets by individual partners.

3. Business assets that are essential for operations held as special business assets

Special business assets comprise assets owned by the co-entrepreneurs and not by the partnership. Nevertheless, the assets are used for the business operations or for the stake in the company. The special business assets are merely in the possession of the partnership. Such assets frequently include real estate, buildings, licences, patents, investments and possibly stakes in the general partner GmbH [a German limited liability company].

Business assets that are essential for operations but held as special business assets will have to be identified and transferred to the jointly owned assets at the same time as the option is exercised and be materially related to it; this is because merely continuing to make the assets available for use would prevent the roll-over of book values altogether. Consequently, economic ownership has to be transferred on the reference date of the notional change in the legal form.

However, as exercising the option does not involve a reorganisation act under civil law, there are no generally applicable rules for the transfer of economic assets to the assets of a notional corporation. Therefore, appropriate ancillary civil law agreements (such as contribution or transfer agreements) between the co-entrepreneur and the company will be necessary. For such a transfer, legal issues related not only to civil law but also company law will have to clarified thus, for example, how the respective transfer should be structured in relation to the co-shareholders since, normally, there are non-tax-related reasons for the existence of special business assets. Moreover, neither changes in the size of the shareholding nor a gratuitous contribution to the other co-shareholders would be desirable. Transferring special business assets in

return for granting company shares without further provisions regarding the other shareholders would increase the fixed capital account of the transferring shareholder and, thus, the size of the shareholding in the partnership that has exercised the option to the detriment of the other co-shareholders. If no other company shares are granted then the contribution would lead to an increase in the joint specific-purpose reserve account, to which all shareholders are entitled and, thus, a gratuitous contribution.

If a transfer at the same time is not desirable then, alternatively, the special business assets that are essential for operations can be separated, in parallel, 'sidewards' in a (possibly new) sister GmbH & Co. KG [a German limited partnership with a limited liability company as a general partner] deemed to be of a commercial nature. We believe that the transfer can take place at same time as the option is exercised with the roll-over of book values. According to the current case law of the Federal Fiscal Court (Bundesfinanzhof, BFH), the requirement for a mandatory transfer beforehand no longer exists. A transfer where hidden reserves are not realised would give rise to a blocking period.

Recommendation: Since, in this case, the Federal Ministry of Finance (Bundesministerium der Finanzen, BMF) - according to the current draft of a guidance letter of 30.9.2021 - provides for a review to determine if the conditions for the option to be exercised at book values are not present pursuant to Section 20 of the German Reorganisation Tax Act, consideration should be given beforehand to obtaining binding information in this regard. Nevertheless, the BFH and the BMF have accepted this method for comparable cases of gratuitous contribution.

4. Real estate transfer tax changes due to the KöMoG

When the option is exercised, the lack of change in the legal arrangements does indeed mean that this does not give rise to the elements required under the Real Estate Transfer Tax Act (Grunderwerbsteuergesetz, GrEStG) because the same principles apply to a notional change of legal form as do to an actual change of legal form. However, when real estate in special business assets is transferred then particular attention should be paid to the additional changes in the GrEStG due to the KöMoG.

The transfer of domestic (German) land and property in special business assets from a sole owner or from several co-owners to jointly owned assets - which according to Section 1 GrEStG is generally a taxable event - is tax-exempt according to Section 5 GrEStG insofar as the transferor/s hold/s a share of the assets that are jointly owned. A reduction in the size of the stake within 10 years (starting from 1.7.2021) would however result in subsequent taxation accordingly.

In order to clamp down on certain tax structures (crea-

Eine Münchener Institution: Der Biergarten

tion of shelf companies) the lawmakers made additional changes to the GrEStG in the form of prior and subsequent holding periods for partnerships that exercise the option; these amendments made it into the final draft proposal for the KöMoG at the urging of the Finance Committee so that the concessions will not even apply. Through this, despite only partial amendments there will indeed be considerable restrictions as exercising the option will be viewed as a reduction in the shareholding. Therefore, exercising the option for co-entrepreneurships with land and properties that form a part of special business assets that are essential for operations is likely to become, at least, significantly more difficult.

Please note: It will be absolutely necessary to compare tax burdens on a case-by-case basis.

In the alternative solution, where land and properties that are held as special business assets are transferred to a sister GmbH & Co. KG deemed to be of a commercial nature, the tax concessions would still apply so that the real estate transfer tax would not have to be paid insofar as the transferor holds shares in the acquiring company. This would apply as long as, during the 10-year blocking period, this sister GmbH & Co. KG, on its part, does not opt for corporation tax or the transferring shareholder/s, do not reduce their shareholdings.

5. Conclusion and Outlook

In view of the strict conditions with respect to special business assets that are essential for operations in the case of a change of legal form, it will be significantly more difficult for businesses with special business assets that are essential to make use of the option. In the run-up to the draft legislation there was a discussion about keeping these as business assets, unfortunately, this was not included in the final version. It remains to be seen whether or not, in the new legislative period, lawmakers will improve this section of the legislation and thus make it easier for many companies to exercise the option.

In practice, many issues relating to the exercise of the option have generally already arisen. In order to provide advice and information on the disputed issues for the local tax offices that process enquiries as well as for taxpayers and their consultants, the BMF is working on a guidance letter on the application of the option pursuant to Section 1a KStG. The BMF published a draft on 30.9.2021 and asked for comments on this by 20.10.2021. The initial impression of the BMF guidance is that it confirms the numerous considerations of the tax consulting community that has already intensively addressed cases of uncertainty in connection with the option pursuant to Section 1a KStG. We will report back once the final version is available.

Recommendation

At any rate, the effects of the option need to be carefully thought through beforehand; in this case, the requisite preparatory steps will have to be completed by the reference date selected for the exercise of the option. Your PKF partner would be pleased to help you with these complex issues.

StB [German tax consultant] Dr Maximilian Bannes

Constructive dividends in the context of intra-group allocations

When assessing whether or not an amount should be categorised as a constructive dividend, the question that always arises relates to the arm's length comparison. If the payment or allowance does not stand up to such a comparison then this can lead to undesirable consequences, as a recent ruling by the Hamburg tax court (Finanzgericht Hamburg, FG) shows.

1. Issue - Services provided to a subsidiary GmbH [a German limited liability company]

In the case in question, the holding GmbH provided various services to a subsidiary GmbH, within the framework of a service agreement, and the remuneration for this was a flat-rate 6% of the subsidiary's sales; in the view of the court, the amount had thus been assessed at a level that was too low. There was no calculation based on the actual costs that had been incurred. In the period in question, the parent company generated mainly losses.

2. The FG's view - Payments constitute constructive dividends

In its ruling of 17.3.2021 (case reference: 2 K 172/18),

the Hamburg FG categorised the full amount of the flat-rate payment as a constructive dividend. Payments are deemed to be constructive dividends where (among other things) there is a reduction in the assets of the subsidiary GmbH to the benefit of the holding GmbH by reason of the corporate relationship. Determining if the corporate relationship was the reason for the payment should be done on the basis of an arm's length comparison. Such an arm's length comparison should be evaluated from the perspective of both contractual partners. In the view of the FG, on both sides, a prudent and diligent managing director would not have approved a flat-rate sales-based rule but, instead, would always have called for a specific calculation. Therefore, all the payments by the subsidiary GmbH to the holding constituted a constructive dividend.

3. Critical appraisal and classification

The intention and purpose of the legal concept of a constructive dividend is generally not to recognise, for tax purposes, remuneration that is governed by the law of obligations to the extent that it exceeds an amount that is customary for this service; in addition, the excess amount is treated like a dividend. Therefore, for tax purposes, a constructive dividend creates a situation that would have arisen if customary (elsewhere) prices had been used.

However, a constructive dividend has actually only one direction. The term 'dividend' already establishes that a (non-operational) transfer of assets from the subsidiary to the parent company occurs and not vice versa, as in the relevant years in the case in question. The FG cleverly upended this logic. As the agreement was sales-based this means that, formally, it was non arm's length and therefore, from a tax perspective, effectively did not exist and, as a consequence, all the payments constitute dividends. Contrary to the usual approach, the FG did not make a distinction as to the level at which the payments were arm's length. In this case specifically, only an excess amount would have had to be treated as a dividend. In the case in question, on the basis of the previous approach, a constructive dividend would thus not have arisen because the price had even fallen below the non-arm's length price. The ruling was based solely on 'formal' criteria and took no account of economic considerations and reasons.

If the ruling gains acceptance, then a far-reaching impact can be expected. Ultimately, this would lead to an eruption in the law on constructive dividends and constructive equity contributions. If a parent company, for example, provides services at a discount or makes available loans at a lower rate of interest to its subsidiary then, according to existing law, the amount of difference between the arm's length price/ interest rate would not be deemed to be a constructive equity contribution due to the lack of a contributable pecuniary benefit. By contrast, according to the recent ruling, a constructive dividend would have to be deemed to exist in the amount of the remuneration that was paid.

Recommendation

It remains to be seen whether or not the German Federal Fiscal Court will restrict the view represented by the FG. In the meanwhile, intra-group agreements should be rigorously checked to determine if they stand up to an arm's length comparison and, in particular, sales-based remuneration for services should be adjusted as a precautionary measure.

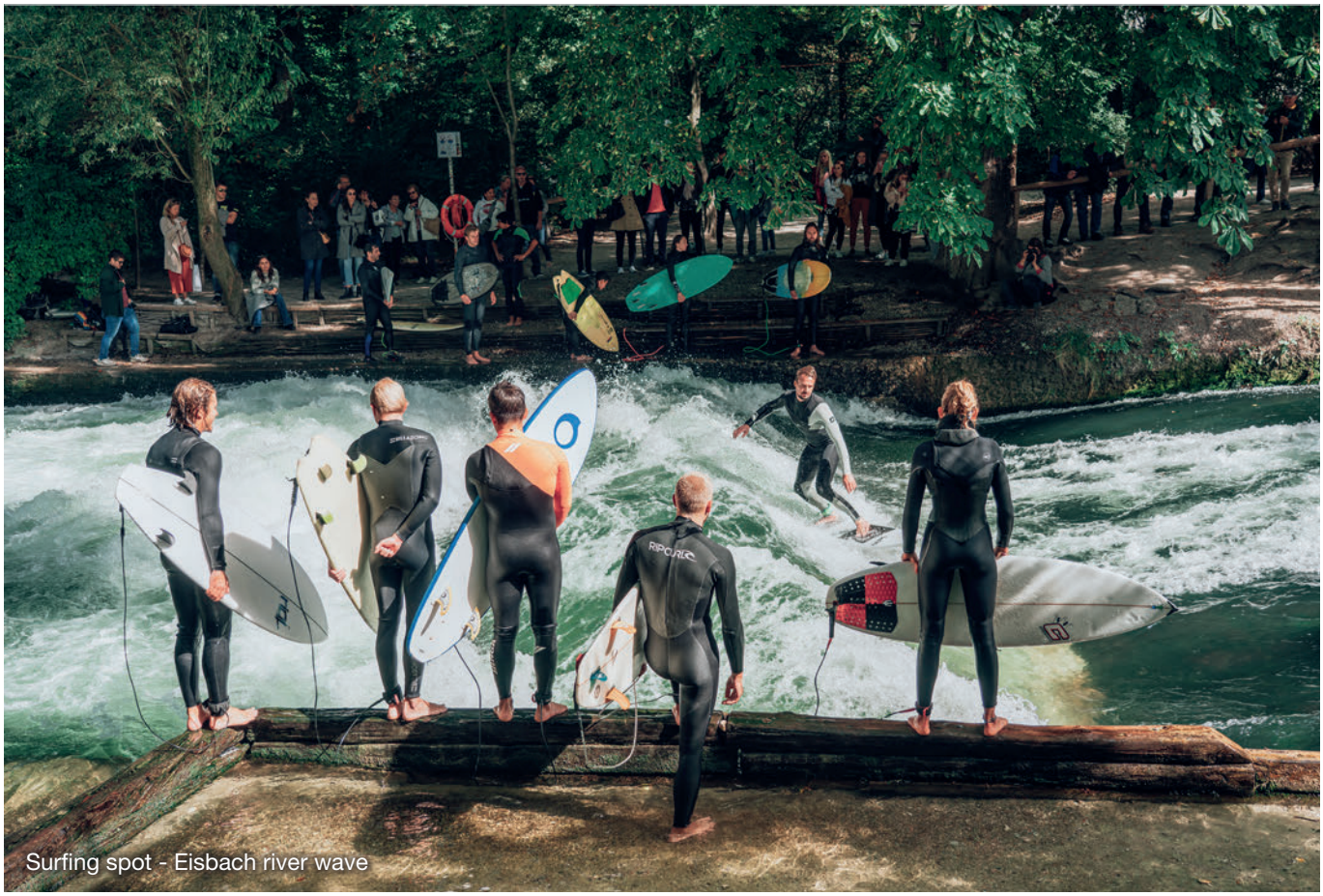
StB [German tax consultant] Holger Wandel

Crediting foreign withholding tax against German trade tax

According to previous regulations, it was possible to credit foreign withholding tax only against German income tax and corporation tax, but not against trade tax. However, this approach meant that creditable taxes were frequently lost. This has now been rectified in a recent court ruling - contrary to the language used in German tax laws.

1. Background to surplus tax credits

In the past, particularly after the cut in the rate for corporation tax to 15% due to the 2008 corporation tax reform legislation, in many cases, there have been so-called surplus tax credits. The main factor responsible for these surplus tax credits was that foreign withholding taxes are normally calculated on the basis of gross income, thus before the deduction of related expenses, while the domestic (German) amount that could be offset has to be determined on the basis of net figures. Another reason for surplus tax


Surfing spot - Eisbach river wave

credits is the abolition, as of 2014, of the so-called corporation tax affiliation privilege. Accordingly, free-float dividends are generally subject to corporation tax and trade tax in Germany at the full rates. However, the fiscal authority considers that it is only possible to offset the tax credits for corporation tax purposes.

2. Contrary to the language used in the legislation, the FG has allowed offsetting

In the case in question, the Hesse tax court (Finanzgericht Hessen, FG) had to rule on an issue regarding the German DTA with Canada, with the particularity that, for corporation tax purposes, the German enterprise had generated a negative result, but a positive trading profit for trade tax purposes. Taking the relevant DTA into account, the ruling by the FG, of 26.8.2020 (case reference: 8 K 1860/16), stated that offsetting for trade tax purposes would also have to be possible. In the statement of justification, the crucial point, apart from the special issue mentioned above, was that the FG determined that foreign withholding tax and German trade tax constituted similar types of tax on income within the meaning of Article 2 of the DTA with Canada. This assessment is of far-reaching significance because the definition is normally based on crediting against a tax on income.

The text of the national legislation does not generally provide for any possibility of offsetting in the way that this is enshrined, for example, in the legislation relating to income tax and corporation tax. Nevertheless, in the case in question, use was made of the application of the DTA as superordinate legislation and - regardless of this, that according to German national legislation no offsetting is provided for - offsetting was carried out. Moreover, the FG concluded that crediting the withholding tax against German trade tax has to take place at the level of the trade tax assessment notice.

3. Outlook

The right to determine the extent to which the FG's legal interpretation - that withholding tax, if it is covered in the DTA, may be credited against trade tax - will endure has been reserved for the next highest court, since the FG's ruling is already pending before the Federal Fiscal Court.

Recommendation

In similar cases, it is recommended to lodge an appeal against a tax assessment that is not compatible with this court ruling.


View across Munich to the Alps when the foehn wind is blowing

Gifting and bequeathing – Securing tax advantages through planning

Transferring assets to the next generation early on makes it possible to achieve big tax advantages while still providing for the future of the donor. In the following section we give a brief overview of gifting arrangements that is then supplemented by aspects to be considered in the case of inheritance.

1. Make good use of tax allowances

The burden of inheritance and gift tax can be avoided or reduced through various tax allowances that are newly granted every ten years and, therefore, it is possible to fully utilise them several times. The amount of the tax allowances will depend on the relationship between the donor and the beneficiary. The tax allowance for gifts between spouses is € 500,000 while in the case of gifting to a child this amount is € 400,000. Grandparents are able to hand over € 200,000 to their grandchildren free of tax. The tax allowance for siblings, nephews, nieces and life partners is € 20,000. If and insofar as the assets exceed the tax allowance, then by gifting incrementally over time it would thus be possible to generate a substantial tax saving.

2. Providing pension benefits in the case of succession planning

In the course of succession planning, particularly among small and medium-sized enterprises, businesses are frequently transferred in return for pension benefits. This form of accelerated inheritance has the advantage that the donor obtains financial security via a lifetime annuity.

3. The reservation of usufruct in the case of properties

If properties are gifted to future legal heirs during the donor's lifetime, then this can be done while reserving so-called usufructuary rights; in this way, the donor is able to continue using or renting out the gifted property, although they would still be entitled to the rental income.

4. Property from the decedent's estate (family home) where there is own use

If legal heirs themselves live in a property from the decedent's estate for at least ten years after inheriting it then no

inheritance tax will be incurred. However, the prerequisite for this is that they have to have moved into the property within six months after the accrual of the inheritance. Moreover, during that ten-year period, they are not allowed either to sell, or rent out, or lease out the property. For children, the tax exemption is limited to a living area of 200 sq m.

5. Disclaiming an inheritance

The renunciation of inheritance can be advantageous if the estate is indebted. The same applies even if the estate is worth so much that the personal tax allowances would be significantly exceeded. This is because if, for example, a spouse who has been appointed as the sole heir renounces the inheritance in favour of the children that the couple had together then the inheritance would be split up among (potentially) several people and all the family members who are beneficiaries could then use their tax allowances.

Recommendation: In order not to miss out, the person who renounces their claim can get their children to promise an appropriate financial settlement.

6. Take account of the compulsory portion

Gifts that were arranged in the last ten years prior to the death of the donor are wholly or partially included in the decedent's estate and, thus, increase the amount of the entitlement to a compulsory portion that the disinherited could subsequently claim.

LEGAL

RA [German lawyer] Andy Weichler

Registration requirements in the LUCID Packaging Register for producers and retailers

The amended version of the Packaging Act (Verpackungsgesetz) came into effect on 3.7.2021. In the following section we outline the amendments as well as the requirements that already existed under the Packaging Act. The background to this is that the parties affected by this legislation are still not familiar even with the regulations that already existed and that, in some cases, violations of these are punishable with a fine; moreover, the amendments will now entail additional requirements as well as a tightening of the regulations.

1. Introduction

The Packaging Act has been in force since 1.11.2019 already. It aims to reduce or avert the effects of packaging waste on the environment. To this end, various requirements have been placed on packaging producers. A producer is anyone who places the packaging on to the market on a commercial basis for the first time.

Please note: Therefore, those who fill or use the packaging as such, for the first time, are deemed to be producers. Those who import packaging on a commercial basis are also regarded as producers.

2. Registration requirement

Extensive registration requirements in the packaging register have been placed on the producers of packaging. Producers are generally obliged to register in the LUCID Packaging Register and, depending on the type of packaging, participate in a dual system if their packaging accumulates as waste with final consumers.

Example: This means that, for example, an online retailer that sells a product on a commercial basis and sends it to the customer has to be registered in the Packaging Register. If the retailer fails to comply with this requirement, then there is not only the risk of a fine but also, potentially, a costly warning letter issued by a competitor.

The respective obligations apply not only to shipment packaging, but also to packaging in which the goods leave the production facility for the first time. The registration obligation is therefore very wide-ranging and affects nearly all those who are acting on a commercial basis insofar as this involves goods being packaged.

Furthermore, producers and distributors of so-called packaging that is subject to system participation are likewise obliged to

- participate in a dual system,
- submit packaging data to the Packaging Register and,
- if necessary, file a declaration of completeness.

3. Amendments to the Packaging Act

Since many of those acting on a commercial basis have, in recent years, been ignoring the requirements specified in the Packaging Act, it has now been adjusted via the amendment of 3.7.2021. Following a transition period and starting from 1.7.2022, distributors of transport packaging as well as final distributors of service packaging will also have to be registered in the LUCID Packaging Register.

Please note: This obligation will thus affect, for example, bakery stores that hand out disposable coffee cups or packaging for bread rolls.

Furthermore, final distributors of packaging will have to take appropriate measures to inform final consumers about the ways that the packaging can be returned and the purpose of these. In addition, operators of electronic marketplaces (Ebay, Amazon etc.) will be obliged to check if the retailers operating on their platforms are registered in the LUCID Packaging Register and if these retailers participate in a dual system. Should this not be the case then these retailers would be subject to a marketing prohibition.

Recommendation

By amending the Packaging Act, in particular, lawmakers have effectively placed a requirement on all retailers who package goods to be registered in the LUCID Packaging Register. In many cases, these retailers will also be obliged to participate in a dual system. Therefore, all addressees should, if possible, immediately comply with the requirements listed here, otherwise they could face the risk of penalties and warning letters.

IN BRIEF

Kindergarten fees: Tax-free employer subsidies reduce the special expenses deduction

Many employers subsidise the accommodation and care of their employees' children, who are not obliged to attend school, in kindergartens and similar facilities. In the sections below we discuss the extent to which this benefit is cut back because special expenses deductions have to be reduced.

In their tax returns, parents are able to deduct two thirds of their childcare costs, up to a maximum of € 4,000, per child and year as special expenses. It is irrelevant whether the child is cared for in a play group, goes to a kindergarten or an afternoon childcare centre. However, the childcare costs may only be deducted if the child is a member of the parental household and is not yet 14 years of age. Moreover, the parents have to obtain an invoice for the childcare costs (or a fee notification) and the payment of the childcare costs has to have been cashless.

Besides this tax relief, the German Income Tax Act provides for employers being able to subsidise or completely finance, free of tax, the accommodation and care of their employees' children, who are not obliged to attend school, in kindergartens and similar facilities. This is on condition that these benefits are provided in addition to remuneration that would in any case be due. The Federal Fiscal Court (Bundesfinanzhof, BFH), in its decision of 14.4.2021 (case reference: III R 30/20) critically examined the extent to which employer subsidies may be deducted as special expenses. According to this, kindergarten costs that have been assumed by employers free of tax should not, in addition, be deductible as special costs. In the case in question, the married claimants had paid kindergarten fees of € 926 and had received a tax-free kindergarten subsidy from the employer in the amount of € 600. Contrary to the view of the claimants - according to which two-thirds of the full amount of € 926 should be deducted as a special expense - the local tax office reduced the full amount by the subsidy of € 600 and only allowed the remaining amount, namely € 326, to be used as the basis for deducting two-thirds as special expenses.

The BFH accepted the calculation by the local tax office and declared that, when determining special expenses, it was only possible to include those expenses that had given rise to an actual and definite economic burden. In the case in question, the tax-free employer subsidy for a specific use resulted in a reduction in the economic burden of the parents by a corresponding amount. Conse-

quently, the special expenses have to be reduced by the amount of the tax-free employer subsidy that, in the view of the judges, also applies in equal measure for married and unmarried parents.

Please note: In a tax return, only 'pure' childcare costs will be accepted as special expenses. Costs for a child's meals, tuition and sports activities, for example, are not subject to any tax relief.

Trade tax exemption – A question of proportionality

Companies that exclusively manage their own real estate are able to file an application to make a reduction to their trading profits so that, potentially, no trade tax is incurred. The requirements for this are however very high and there are only a few activities (such as the management and use of own capital assets) that enable exemptions. The extent to which performing an 'inadmissible' activity will exclude the entire exemption was recently decided.

In the case that got to the tax court, the cooperative making the claim had dealt exclusively, in the period from 2014 to 2016, with the letting of property - both residential properties as well as commercial space - and, therefore, had filed applications to reduce their trading profits. A commercial tenant had leased a retail store where she generated profits below the trade tax exemption threshold. In 2014, this tenant also wanted to rent a residential property for which, however, members of the cooperative were given priority. That is why, in December 2014, the tenant purchased a cooperative share (< 0.1%) and, subsequently, moved into a residential property. After a tax audit, the local tax office was of the view that a reduction in the cooperative's trading profits had to be ruled out. The legal action brought against this decision before Düsseldorf's tax court (Finanzgericht Düsseldorf, FG) was successful, as the cooperative had satisfied the requirements for a reduction in trading profits. The FG, in its ruling of 22.4.2021 (case reference: 9 K 2652/19), did indeed confirm that the real estate was partially used for the commercial operations of a cooperative member; however, this shareholding was of minor importance since this member held less than 1% in the cooperative and the tenant herself was not burdened with trade tax. Moreover, this was an isolated case and ruling out the beneficial reduction would not be proportionate and, therefore, unreasonable.

Please note: You should keep in mind the Federal Fiscal Court case law according to which this relief may not be denied if the shareholder that uses the real estate that has been made available generates income that is not subject to trade tax.

Developed real estate – New guideline on the apportionment of the purchase price

When purchasing a rental property, it is generally advantageous for landlords if the local tax office allocates as high a share of the purchase price as possible to the building because only this portion of the costs is factored into the assessment basis used to calculate the depreciation for the building. In contrast to this, the share of the total purchase price that is apportioned to land with an indefinite useful life may not be depreciated and, thus, not have the effect of reducing the tax liability.

In this context, on 1.5.2021, in response to a Federal Fiscal court ruling, the Federal Ministry of Finance published an updated guideline on the apportionment of the purchase price in the case of developed real estate. The situation that gave rise to this publication was that the previous guideline did not reflect actual property values and did not take into account factors related to location and regionalisation.

The new apportionment of the purchase price frequently results in a more favourable and higher building value for the landlord. Although, in cases where lower building values were recognised in the past, these can no longer be adjusted for assessment years where the notices are already final and unappealable. However, in tax assessment cases that are open, the new apportionment of the purchase price may be used as a basis and may also create new depreciation potential for future assessments.

Please note: The fiscal authority would generally recognise a verifiable apportionment of the purchase price that is made in a purchase agreement if it is not illusory and does not constitute an abusive tax scheme. With the new guideline it will be possible to refute suggestions that an agreement appears to be a sham or that a particular arrangement is seemingly abusive.

AND FINALLY...

10 pieces of advice from Niklas Östberg

1. *Speed beats perfection almost every time.*
2. *Most decisions are of a "revolving door" nature. Don't waste time over-analysing.*
3. *Being yourself is always better than a bad copy of someone else.*
4. *Focus on gradual improvements rather than step change.*
5. *It's never too late to enter a market with better customer experience, see Zoom versus Skype or Google Meet.*
6. *Hire people with heart. Heart really matters. It's not just about talent.*
7. *Getting one thing right can compensate for being wrong ten times.*
8. *It is almost always better to let teams try, fail and learn from this than stop them from trying.*
9. *Have the courage to follow your heart and intuition.*
10. *Stay down to earth. Your success is driven by luck, coincidence and many amazing people around you.*

Niklas Östberg, born in 1980 in Sweden, co-founder and CEO of Delivery Hero.

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EUREF-Campus 10/11 | 10829 Berlin | Tel. +49 30 306 907-0 | www.pkf.de

Please send any enquiries and comments to: pkf-nachrichten@pkf.de