Germany: Changes to tax group regime proposed

The German government published a draft law on 19 September 2012 that includes measures to improve certain aspects of the tax group (Organschaft) rules. To qualify under the tax group regime, a parent company must hold the majority of the voting rights in a subsidiary from the beginning of the subsidiary’s fiscal year. In addition, the members of the group must conclude a profit and loss pooling agreement (PLPA) for at least five calendar years. Both corporations and partnerships can act as the parent of a tax group, but only a corporation can be a member of a group.

The main proposals are as follows:

• In response to the infringement proceedings initiated by the European Commission, the subsidiary would no longer need to have both its registered seat and place of management in Germany – a German place of management would be sufficient. (Since it is practically impossible to conclude a PLPA with a subsidiary that is subject to foreign corporate law, it is expected that, even under the revised rules, it still would be problematic to include dual resident companies with a German place of management in a German tax group (which would create new issues relating to potential conflicts with the EU freedom of establishment).)

• Following a decision of the Federal Tax Court, it appeared to be possible to transfer the income of a German subsidiary to a foreign parent in a situation that was comparable to a German tax group (the case concerned years before 2002 where a formal PLPA was not required for a trade tax group) and thereby entirely avoid taxation of such income in Germany. To avoid further discussions on the relevance of the decision under current law, it is proposed to require that the subsidiary be held through a German taxable presence or entity and that the income attributed to the tax group parent be taxed in Germany.

• A tax group would be accepted for tax purposes even if the profit transferred was not computed correctly provided the error was corrected in subsequent financial statements as soon as the error was detected. Currently, there is a presumption that a PLPA was not properly executed if the underlying financial statements of a subsidiary in a tax group turn out to be incorrect and, therefore, an incorrect profit transfer/loss compensation is made.

• Existing rules require that the loss assumption clause in a PLPA be identical to the wording in section 302 of the Stock Corporation Act (SCA) even where the subsidiary is a limited liability company (GmbH) and not a stock corporation. According to the proposal, a PLPA with a GmbH would be required to specifically refer to section 302 SCA as current from time to time. PLPAs that do not contain such a reference would have to be amended by 31 December 2014.

• Negative income of both the parent and subsidiary could be offset only if it was not taken into account for tax purposes outside of Germany. The tax group rules currently restrict the use of losses at the level of the parent company of the tax group only in situations in which the losses are taken into account abroad for the parent of the tax group under a concept that is similar to the German tax grouping rules. Because these rules have been of limited practical relevance, they would be replaced by broader rules, under which losses of the tax group parent and/or the subsidiary could not be deducted if they also were tax deductible in another country at the level of the parent of the tax group, the subsidiary or another related party. Based on this broad wording of the law, the rules could exceed what was intended by the legislator and could affect situations in which expenses are included both in Germany and abroad due to qualification conflicts. Future developments concerning these proposed rules will need to be monitored carefully. It is questionable whether the existing dual consolidated loss rule and the proposed extension are in line with EU law.

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