German Tax Monthly

Information on the latest tax developments in Germany

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Government Draft for an Act to implement the EU Minimum Taxation Directive

The Federal Ministry of Finance (BMF) published the government draft bill for an "Act for the implementation of the EU Directive to ensure a global minimum taxation" (Minimum Tax Directive Implementation Act). The draft is closely based on the so-called Minimum Taxation Directive of the EU (Council Directive (EU) 2022/2523 of 15 December 2022) and takes into account the OECD model regulations and the first Administrative Guidance of the OECD.

In addition, the draft law contains the following so-called "accompanying measures":

- **Royalty deduction limitation rule (§ 4j Income Tax Act):** deviating from the ministerial draft, the royalty deduction limitation rule is not to be completely abolished after all, but merely mitigated by lowering the low tax threshold from 25% to 15% (as of 2024).
- **CFC taxation:** the low tax threshold of the CFC taxation is also to be lowered to 15% as of 2024 (as already provided for in the ministerial draft). However, the trade tax liability of CFC tax amounts is now to be retained.

In line with international accounting standards, a mandatory exemption from the accounting for deferred taxes resulting from the application of the Minimum Tax Act or corresponding foreign tax laws was included in the government draft.

The Act is intended to transpose the EU's minimum taxation directive into national law. The aim is to implement central elements of the international agreements on Pillar 2 (rules on minimum taxation) of the so-called two-pillar solution of the OECD. The relevant rules are to be regulated in Germany in a new tax law, the Minimum Tax Act (MTA).

Business units located in Germany are subject to tax. Prerequisite is that the consolidated financial statements of the ultimate parent company must show annual turnovers of at least 750 million euros in at least two of the four financial years immediately preceding the financial year (turnover limit).

Both internationally and nationally active groups of companies are covered. However, a five-year tax exemption is provided for groups with minor international activities (business units in a maximum of six tax jurisdictions and tangible assets of the foreign business

Content

units of a maximum of 50 million euros). Government units, international organisations, non-profit organisations, pension funds, investment vehicles (as ultimate parent company) and real estate investment vehicles (as ultimate parent company) are exempt.

The tax liability of domestically located business units is independent of the respective legal form - i.e. partnerships can also be subject to the minimum tax - and is added to the income tax or corporation tax liability. The taxation is independent of the taxation of the shareholder or partner (separation principle).

The minimum tax is composed of the Income Inclusion Rule (IIR – in German “primary supplementary tax”), the Undertaxed Payment Rule (UTPR – in German “secondary supplementary tax”) and the Qualified Domestic Minimum Top-up Tax (QDMTT – in German “national supplementary tax”). The UTR is to be applied subsidiarily to the IIR and serves as a catch-all measure, if the low taxation is not already compensated by the application of the IIR.

The calculation of the minimum tax – country-specific calculation of the top-up tax based on a minimum tax rate of 15 percent – is based on GAAP (usually the accounting standard of the parent company) and certain necessary adjustments. Starting point is the so-called “minimum tax net income”, i.e. the result of the commercial balance sheet calculated for the financial year. The minimum tax net income is to be adjusted by certain amounts, including total tax expenditure and dividends.

Accepted accounting standards, according to which the relevant consolidated financial statements are prepared, are defined by the Law as International Financial Reporting Standards (IFRSs or IFRSs adopted by the EU in accordance with Regulation (EC) No. 1606/2002 on the application of international accounting standards) and generally accepted accounting principles of Australia, Brazil, EU/EEA Member States, Hong Kong (People's Republic of China), Japan, Canada, Mexico, New Zealand, India, Republic of Korea, Russia, Switzerland, Singapore, the United Kingdom, the United States of America and the People's Republic of China. The recognized accounting standards also govern the status of a QDMTT.

The draft contains special provisions for the transition year, the transition period and the initial phase. It contains provisions on the use of tax attributes at the time when a group of companies becomes liable to minimum taxation for the first time in relation to a tax jurisdiction (including taking account of recognized deferred taxes when calculating the effective tax rate). This also includes special provisions for intra-group transfers of assets, which, according to the explanatory memorandum, are intended to prevent "step-up models". Transfers after November 30, 2021 will be affected, meaning that companies will have to have data ready for a significantly longer period before the minimum tax rules are applied for the first time.

Furthermore, the internationally agreed simplifications are included, in particular the transitional CbCR safe harbour (use of country-by-country reports of multinational groups), transitional rules for blended CFC tax regimes, simplifications for insignificant business units as well as the safe harbour regulation for QDMTT, which applies not only to EU member states, but also to third countries.

The central actor in the national taxation procedure is the so-called minimum tax group. Several taxable business units of a group of companies form a minimum tax group. The IIR, UTPR and QDMTT amounts of the business units belonging to the group are attributed to the group parent. All business units as well as joint venture and joint venture subsidiaries are obliged to provide the group parent with the information required to prepare the tax return. The group parent has to file an annual tax return and owes the minimum tax.

In addition, an annual minimum tax report must be submitted to the Federal Central Tax Office (BZSt), inter alia, for purposes of international exchange. The intentional or reckless omission, incomplete or untimely submission of the minimum tax report is an administrative offence, which can be punished with a fine up to 30,000 euros. However, for a transitional period – financial years beginning on or before 31 December 2026 and ending before 1 July 2028 – there shall be no administrative offence if it is proven that appropriate measures have been taken to justify an untimely or not prescribed manner or an incorrect or incomplete transmission.

In principle, the Minimum Tax Act is to be applicable for the first time for financial years beginning after 30 December 2023. The UTPR, on the other hand, will only apply one year later, for the first time for business years beginning after 30 December 2024.

The government draft can now be introduced into the parliamentary procedure. The Bundesrat will then have the opportunity to comment on the draft law. This will be followed by the resolutions of the Bundestag and the Bundesrat.

Ministerial Draft Bill for a Growth Opportunities Act

The Federal Ministry of Finance (BMF) published a ministerial draft bill for an "Act to strengthen growth opportunities, investment and innovation as well as tax simplification and tax fairness" (Growth Opportunities Act).

The draft law contains a large number of amendments in various areas of tax law. These are the main contents at a glance:

Restrictions on the deduction of interest expenses

Reform of the interest limitation rule

- Conversion of the de minimis threshold of three million euros into an allowance
- Introduction of an "anti-fragmentation regulation": The allowance is not granted separately for each business within the meaning of the interest limitation rule (e.g. for each subsidiary). Rather, similar businesses that are under uniform management are considered as one business for purposes of the tax allowance
- Complete repeal of the further exemption regulations (standalone clause and equity escape)
- Extension of the concept of interest (e.g. also economically equivalent expenses and other expenses in connection with the procurement of borrowd capital)

Introduction of an interest rate barrier

- Business expense deduction ban for interest expenses exceeding a legally defined maximum rate
- Applies only to interest expenses due to a business relationship between related parties
- The maximum deductible rate should generally correspond to the BGB base interest rate increased by two percentage points. As of 1 January 2023, this would correspond to 3.62%
- Opportunity of proof: that both the creditor and the top group parent company could only have received the capital at an interest rate above the maximum rate. If the proof is successful, then the interest rate that could have been obtained in the most favourable case shall be deemed to be the maximum rate for the purposes of the interest rate barrier
- In addition, counter-evidence option: interest rate barrier does not apply if the creditor carries out a substantial economic activity in its state of residence

The amendments to the law are to come into force on 1 January 2024

Improvement of the tax loss deduction

Loss carry-back

- Extension to 3 years (for the first time for losses in 2024)
- Permanent increase to 10 million euros (20 million euros in the case of joint assessment), i.e. beyond 2023

Loss carry-forward (unlimited loss offset only up to 1 million euros, above that only on a pro-rata basis)

- Temporary suspension for 2024 to 2027 (i.e. no base amount) - still being agreed by the ministries
- From 2028 onwards: Increase of the base amount to 10 million euros / 20 million euros (previously: 1 million euros / 2 million euros)

Climate protection investment premium

- For all taxable enterprises irrespective of legal form, size and activity
- Funding period: Limited to approx. four years; In principle, investments commenced and completed after the date of promulgation of the Act and before 1 January 2028
- Amount of funding: 15% and a maximum of 30 million euros per beneficiary for the entire funding period
- Beneficiary investments: Acquisition and production of new depreciable movable assets of fixed assets as well as measures on existing movable assets of fixed assets; must be in operational use for two years
- Must serve to improve energy efficiency in the company, be included in a savings concept (prepared with the help of an energy consultant or an in-house energy manager) and be able to exceed applicable EU standards
- Acquisition/production costs of at least 10,000 euros per asset
- Application: can generally be submitted at the time of purchase/production until 31 December 2029; Maximum of two applications per eligible person in the entire funding period
- Receipt as a contribution without affecting profit or loss

Improvement of depreciation possibilities and further investment incentives

Improvement of depreciation possibilities

- **Immediate depreciation of low-value assets**: Increase of the limit of acquisition or production costs (from previously 800 euros) to 1,000 euros

- **Collective item method**: Increase of the limit of acquisition or production costs (from previously 1,000 euros) to 5,000 euros; reduction of the liquidation period (from previously five years) to three years
- **Special depreciation** (in the year of acquisition and in the four following years): Increase from currently up to 20% of the investment costs to up to 50%
- First-time application for assets acquired, produced or incorporated into business assets after 31 December 2023

Expansion of research allowance (in principle from 2024)

- Among other things, expansion of the eligible expenses to include the reduction in value of usable movable assets of the fixed assets used in the research and development project benefiting from the subsidy, which are necessary and indispensable for the implementation of the research and development project
- Accordingly increase of the eligible cost share for contract research from 60% to 70%
- Increase of the maximum assessment basis for the research allowance from currently four million euros to twelve million euros

Partnerships

Option for corporate income taxation

- Access for all partnerships (instead of previously only trading partnerships and partnership companies)
- Also for newly established companies and for corporations that have been transformed into partnerships
- Improvements to the fictitious distribution of retained profits
- Entry into force on the day after promulgation of the law

Procedural adjustments to the Act to Modernise the Law on Partnerships

- Continuation of the joint ownership principle in income taxation
- Procedural changes for associations of persons with legal capacity, among others: Fulfilment of tax obligations by the legal representatives; tax declaration obligation should be primarily incumbent on the association of persons, the association of persons should be held liable for late payment surcharges, notification of administrative acts to the association of persons, right of objection/appeal of the association of persons itself

The publication of the ministerial draft bill is the first step in the legislative process. Only after a government draft bill has been introduced into the parliamentary procedure will the Bundesrat have the opportunity to comment on the bill. This is followed by the resolutions of the Bundestag and the Bundesrat. In the course of the legislative procedure significant changes can still be made in the course of the legislative process.

Government Draft for a Future Financing Act

The Federal Ministry of Finance (BMF) has published the government draft bill for a Law on the Financing of future-proofing Investments (Future Financing Act).

The Future Financing Act contains measures in financial market law, company law and tax law that are intended to strengthen the performance of the German capital market and increase the attractiveness of Germany as a financial location for both national and international companies and investors. In particular, start-ups, growth companies and small and medium-sized enterprises (SMEs) as drivers of innovation are to be facilitated in accessing the capital market and raising equity capital.

In the area of tax law, a reform of the tax treatment is to facilitate employee share ownership in particular with effect from 2024.

Tax exemption for the transfer of employee share ownership at a discount

The tax-free maximum amount is to be raised from 1,440 to 5,000 euros. However, in future the tax-free amount is to be linked to a requirement of additionality ("in addition to the salary owed anyway") if the tax-free non-cash benefit exceeds 2,000 euros per calendar year. Deferred compensation thus remains possible to a limited extent.

In addition, an "indirect holding period" of three years is to be introduced for employee share ownerships in order to avoid undesirable windfall effects through immediate sale after transfer of the share by the employee without loss of tax exemption. If the shareholding is sold or transferred free of charge within three years, the initially tax-exempt portion of the salary is to be taxed at the final withholding tax rate of 25 percent.

Deferral model for employee share ownerships provided at a discount

The scope of application of the preferential treatment is to be extended in that in future it will no longer be based on the single SME threshold but on multiplied SME thresholds. The companies must then have fewer than 1,000 employees (instead of the previous 250 employees) and may have an annual turnover of no more than 100 million euros (instead of the previous 50 million euros) or an annual balance sheet total of no more than 86 million euros (instead of the previous 43 million euros).

In this context, the period in which exceeding the threshold is harmless is also to be extended. In the future, the preferential treatment can be claimed if the threshold was not exceeded at the time of the transfer of the share or in one of the six preceding calendar years (7-year period, previously 2-year period). So far, "young" companies whose date of foundation is no more than 12 years ago are eligible. In future, the date of foundation may be up to 20 years before the date of the transfer of the share.

The tax exemption is to be extended to cases where the company shares are not granted by the employer itself, but by the (founding) partners or other group companies.

In future, the final taxation of the non-cash benefit is not to take place after twelve years, but only after 20 years, if the employee has not sold the shareholding or terminated his employment relationship beforehand.

Finally, it should be possible to further postpone taxation for the facts "expiry of 20 years" and "termination of employment relationship " (dry income) if the employer irrevocably declares that he assumes liability for the wage tax (optional liability regulation). In these cases, only the later fact of the actual "transfer or sale" would trigger taxation.

The possibility of a lump-sum taxation (wage tax by employer) with a tax rate of 25 percent for all taxable events (transfer of the share ownership, expiry of (in future) 20 years, termination of employment), which was envisaged in the draft bill, was not included in the government bill.

BFH (I R 44/22): Non-Consideration of "Definitive" Foreign Permanent Establishment Losses even in the Case of a Qualified Reversion Clause

In its decision of 12. April 2023, the German Federal Fiscal Court (BFH) commented in particular on the question of whether reversion clauses contained in double taxation treaties (DTT), which in certain cases permit taxation of EU foreign permanent establishment income in the parent state despite an agreed DTT exemption, relativise the Court of Justice of the European Union (ECJ) case law on definitive losses.

The ECJ only recently clarified in its ruling of 22 September 2022 (C-538/20) that the symmetry theory inherent in the DTT exemption, which assigns sole taxation responsibility to the permanent establishment state in the case of both profits and losses, is not objectionable under EU law. In these cases, the situation between a domestic and a foreign permanent establishment was not comparable because the parent state had no overall tax access to the income of the foreign permanent establishment.

In the case in dispute, the plaintiff, a domestic limited liability company, had established a permanent establishment in Italy in 2004 as part of the expansion of the company. Since this branch office only generated losses in the years 2004-2008, the plaintiff closed the Italian branch office on 31 December 2008 and claimed the losses as definitive losses in Germany in the year in dispute 2008 that could no longer be used for other purposes. The tax office did not take these losses into account in the tax assessment in accordance with the exemption for permanent establishment income agreed in the DTT Italy 1989, whereas the Hamburg Fiscal Court amended the contested assessment as requested.

The appeal filed by the tax office was successful. The BFH first confirms the basic statements of the ECJ with regard to the effect of the symmetry theory under EU law in the context of the exemption of permanent establishment income under treaty law, which it had already adopted in its decision of 22 February 2023 (I R 35/22).

The BFH then examines whether the provision contained in section 16(d) of the Protocol to the DTT Italy 1989 is a so-called genuine reversion clause, which has the effect that in the absence of effective taxation in the source state, the right of taxation reverts to the other contracting state. Due to the requirement of "effective" taxation by the source state, the provision is to be classified as a so-called qualified reversion clause, which requires not merely an abstract tax liability for the exemption, but actual ("effective") taxation by the source state.

The BFH does not follow the plaintiff's argument according to which the reversion of taxation with regard to negative income always occurs if the loss was not actually offset against other (positive) income in the source state. In the case of losses, effective taxation by the other state is to be assumed in any case if the other state includes the losses in the tax assessment basis and enables an offset with positive income of another assessment period. However, it is not necessary that such an offset actually occurs at any time.

As a result, in the view of the BFH, in cases in which - as in the case at issue - the conditions of the reversion clause are not met, Germany's "symmetrical" waiver of taxation under the treaty remains in place and consequently, according to the standards of the ECJ, there is no comparability with purely domestic cases.

BFH (XI R 45/19): Interest Expenses within the Meaning of the Interest Limitation Rule

In its judgment of 22 March 2023, the German Federal Tax Court (BFH) decided that the interest limitation rule (section 4h Income Tax Law) only apply to payments that are remuneration for the temporary provision of borrowed capital.

According to German tax law, expenses caused by the operating activities of a taxpayer are tax-deductible and generally reduce the tax assessment base (objective net principle). In the case of interest expenses, however, the interest ceiling rules must be observed pursuant to which the deduction of interest as business expenses is limited under certain circumstances. According to the statutory provision, interest expenses in this context are payments for loan capital that have reduced the relevant profit.

In the case at issue, the plaintiff (a limited liability company (GmbH)) took out a loan in 2011 in the form of a syndicated loan with a total of five banks. The lead manager was C-Bank. According to the contractual agreements, a so-called “Arrangement Fee” equal to 4.25% of the agreed loan amount was to be paid to C-Bank, in addition to an annual “Agency and Security Agency Fee”.

The matter in dispute was whether these fees relating to the syndicated loan are to be viewed as interest expenses within the meaning of the interest limitation rule. In the view of the German tax authorities, interest expenses include all costs in connection with the granting of the loan, provided that they are paid to the lender. By contrast, the plaintiff did not consider these fees to be payment for loan capital. The Lower Tax Court of Münster (10 K 2859/15 K as of 12 April 2019) had ruled at first instance, that an “Arrangement Fee” is not an interest expense within the meaning of the interest limitation rule, whilst an “Agency and Security Agency Fee” does fall within the area of application of the interest limitation rule.

The BFH confirmed this view: A fee that does not remunerate the possibility to use borrowed capital but another service of the lender is not an interest expense within the meaning of section 4h Income Tax Law. A so-called "Arrangement Fee", which is used to remunerate separate services of a lead manager that go beyond the provision of capital and which is calculated on the basis of the contractually agreed (and not the actually utilised) loan amount, is not subject to the deduction restriction of the interest limitation rule.

The "arrangement fee" paid in the case at issue was a one-off fee for the arrangement activities of the lead manager up to the conclusion of the loan agreement (including the preparation of a financing concept and an information memorandum, organisation and documentation of the signing). The fee was to be paid for the fact that C-Bank, as lead manager, brokered and arranged the syndicated loan with several other banks. In addition, a - pro rata - reimbursement in the event of premature termination of the loan relationship was not agreed.

The lower tax court’s decision partly conflicts with the view of the tax authorities (guidance by the German Federal Ministry of Finance dated 4 July 2008, item 15), according to which all fees are interest expenses to the extent they are payable to the lender.

It should be noted that the ministerial draft bill for a Growth Opportunities Act provides for changes to the interest limitation rule and to expand the definition of interest. Accordingly, in the future, e.g. economically equivalent expenses and other expenses in connection with the procurement of borrowed capital are also to fall under the definition.

BMF Draft on the Application of the German Foreign Transactions Tax Act

On 20 July 2023, the Federal Ministry of Finance (BMF) published a draft of a BMF guidance on the principles for the application of the Foreign Transactions Tax Act (FTTA, in particular on CFC taxation (FTTA Application Decree)).

The new application decree is intended to adapt the existing BMF guidance of 14 May 2004 on the principles for applying the FTTA to the current legal situation. The Act on the Implementation of the Anti-Tax Avoidance Directive (ATAD Implementation Act of 25 June 2021) in particular has resulted in extensive changes to CFC taxation:

- Change of the control criterion and introduction of a shareholder-related approach,
- Abolition of the concept of downstream intermediary companies (transferable CFC taxation),
- Revision of the catalogue of active income,
- Revision and extension of the motive test for certain passive income to third countries.

First selected notes on the draft regarding CFC taxation

- **Shareholder-related approach:**
  Pursuant to the law, control of the foreign company also exists if the taxpayer is directly or indirectly entitled to more than half of the profits or liquidation proceeds of the intermediate company. In the opinion of the BMF, a shareholder position is not required for this. The concrete contractual agreement is decisive, so that hybrid financial instruments (e.g. profitsharing rights, participating loans or silent partnerships) can also convey such a claim.
- **Closeness through concerted conduct:**
  Pursuant to the law, concerted behaviour between partners of a partnership is rebuttably presumed. In practice, this has considerable consequences, since in principle any participation in a fund in the legal form of a partnership could lead to "control" of any intermediate companies.
  Proof to the contrary should be possible in particular if the common purpose of the investors is exhausted in an asset situation where the investment object is not concretely determined and as long as investors do not know each other and only have information rights. In this context, blind pool funds are mentioned in particular.
- **Active/passive catalogue:**
  The draft explicitly clarifies that disposals of assets also belong to the income, insofar as they were used for the activity.
  According to the BMF, individual activities with a significant economic impact are not to be grouped together but are to be subsumed separately under the catalogue, even if they have an economic connection with other activities (modification of the previously applicable so-called functional approach).
- **Motive test**:
  According to the draft, the motive test is not to be applied to third-country companies, except in the case of non-controlled investment companies. The motive test is excluded insofar as the essential economic activity is predominantly provided by third parties. This should include, in particular, business management and management contracts.
- **Procedural obligations:**
  Pursuant to the law, each taxpayer with a direct or indirect interest in the foreign company must submit a tax declaration. In practice, the question often arises as to whether this also applies if the result is that there is no CFC taxation (e.g. because of the exemption limits). It is also questionable who is obliged to declare in the case of participation via a partnership. According to the draft decree, there is a duty to declare even if the result is that there is no additional taxation. The partnership itself does not have to make a declaration.
- **Tightened CFC taxation:**
  For the first time, the draft also contains statements on the tightened CFC taxation (concerns foreign companies, that are resident in a non-cooperative tax jurisdiction), according to which not only passive income, but all low-taxed income of an intermediate company is subject to (tightened) CFC taxation.

Outlook

Until 4 September 2023, the associations can comment on the draft. The publication of a final version of the application decree is therefore not expected before October 2023.

It should also be noted that there are planned legal changes to CFC taxation. In the draft bill for a Minimum Tax Directive Implementation Act, it is planned as an "accompanying" measure to lower the low tax threshold from the current 25 percent to 15 percent as of 2024, which should significantly reduce the factual scope of application of CFC taxation. According to the explanatory memorandum, this serves to achieve synchronisation with the global effective minimum taxation.

However, the new application decree does not yet refer to the draft bill for a Minimum Tax Directive Implementation Act and continues to focus on a low tax threshold of 25 percent.

BMF Draft Guidance on Anti-Hybrids Rules

The Federal Ministry of Finance (BMF) has published a draft of a BMF guidance on the prohibition of deduction of expenses in the case of taxation mismatches due to hybrid mismatch arrangements (anti-hybrids rules).

Hybrid mismatch arrangements can result in a tax deduction in both states (double deduction - DD) or a deduction in one state with simultaneous non-taxation in the other state (deduction/non-inclusion - D/NI).

The anti-hybrids rules are applicable for the first time to expenses incurred after 31 December 2019. Expenses that were already legally incurred before 1 January 2020 are only deemed to have been incurred after 31 December 2019 if they are based on a continuing obligation and could have been avoided without significant disadvantages as of that date.

If there is no continuing obligation, the anti-hybrids rules are not to be applied even if expenses are incurred after 31 December 2019. In this context, the (clarifying) statements according to which deductions for depreciation are not based on a continuing obligation, and this is also to apply to interest carry forwards within the meaning of the interest limitation rule that only have a tax effect from 1 January 2020 (carryforward of exceeding borrowing costs) and therefore anti-hybrids rules are not to be applied in either case are particularly important for practice.

The scope of application is generally limited to (contractual) arrangements between related persons or between a company and its permanent establishment. If there is a structured arrangement, however, the anti-hybrids rules are also applicable to situations between third parties.

The law provides for a prohibition of deduction for expenses which, due to the use of a hybrid financial instrument ("divergent tax qualification"), lead to a non-taxation or low taxation of the corresponding income abroad (deduction/non-inclusion mismatch) because of the different classification of the financial instrument on the part of the remuneration debtor and the remuneration recipient as equity or debt or in the case of hybrid transfers ("divergent allocation"). Of practical relevance is the clarifying statement on the "causality" of the hybrid element for the prohibition of deduction of operating expenses, according to which the anti-hybrids rules are not to be applied if, in addition to the qualification or attribution mismatch, other causes outside the scope of the anti-hybrids rules arise for a non-taxation or low taxation of the income corresponding to the expenses (e.g. personal tax exemption of the creditor). “Non-taxation" is said to exist insofar as the income corresponding to the expenses is not included in a tax assessment basis (including CFC taxation). Taxation at a tax rate of zero percent, the factual tax exemption of the income corresponding to the expenses as well as the (proportional) waiver of the levying of a foreign tax is defined as non-taxation. “Lower taxation" is said to exist if the income is subject to a lower effective tax burden abroad than that which would result if the capital assets were qualified or attributed in accordance with German law.

Furthermore, the law provides for a prohibition of deduction for expenses in the case of deviating tax treatment of a taxpayer (legal entity) and for fictitious expenses in the case of deviating tax assessment of debt relationships to be assumed between a company and its permanent establishment, insofar as deduction/non-inclusion incongruities arise from this. According to the draft guidance, the concept of expenses includes expenses of all kinds and is not limited to payments, but includes all income changes across periods. In particular, expenses of taxpayers who are regarded as non-transparent for tax purposes in Germany and who are regarded as transparent entities abroad (hybrid entities), which can also be the case if they are included in a foreign group taxation system, are covered by the provision. The draft guidance also explicitly mentions the "check-the-box procedure" that frequently occurs in practice with US inbound structures. According to the draft guidance, a "causality" between the non-taxation and the hybridity is also required for this taxation mismatch.

In addition, the law provides for a prohibition of deduction for expenses insofar as the income corresponding to the expenses is not subject to actual taxation in any country due to their tax allocation or attribution deviating from German law (deduction/non-inclusion mismatch). The draft guidance clarifies that this covers in particular expenses to so-called reverse hybrid entities. As a rule, these are fiscally transparent in their country of domicile, while they are considered non-transparent for tax purposes in the country of their (indirect) shareholders.

The law neutralises taxation mismatches resulting from the double deduction of expenses (double deduction mismatches). Expenses which are in principle deductible abroad, but which are not actually deductible, e.g. because of the application of other deduction prohibitions, are not to be considered as taken into account abroad. On the other hand, the increase of a loss that is in principle compensable for tax purposes or the consideration of expenses in the context of CFC taxation should also be (harmful) consideration within the meaning of the regulation. With a view to the application of foreign group taxation systems, the draft states that, irrespective of the technique used - i.e. offsetting of income or full consolidation - expenses may be taken into account twice.

A further prohibition of deduction concerns taxation mismatches in which Germany is not directly involved, but which are shifted to Germany via one or more transactions (so-called imported mismatches). The regulation is to be applied subordinate to the other deduction prohibitions. The draft guidance states that in the case of multi-level business relationships, there must be a chain of relationships between the German taxpayer and the legal entity bearing the harmful expenses, but not a uniform economic connection between the respective expenses. The economic reason for the expenses does not have to be maintained throughout the entire supply chain, e.g. interest expenses on the one hand and licence expenses on the other. According to the draft guidance, the examination of the regulation on imported mismatches is extensive.

The taxpayer is subject to increased obligations to cooperate and provide evidence for foreign matters. Documents from the accounting of the legal entities involved, information from the foreign tax authorities (on the individual case) as well as the submission of foreign tax assessment notices, tax rulings or confirmations of the (non-)exercise of a foreign option may be required.

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