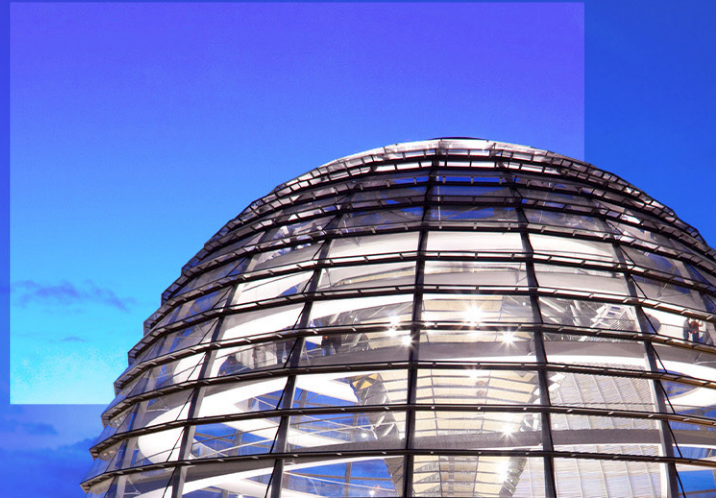


# German Tax Monthly

Information on the latest tax developments  
in Germany

October | 2023



## Government Draft Bill for the Growth Opportunities Act

The Federal Ministry of Finance (BMF) published the government draft bill for the "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:

### 1. Restrictions on the deduction of interest expenses

#### Adjustments to the interest limitation rule

- 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
- Adjustments to the further exemption regulations (stand-alone clause and equity escape) in line with the ATAD requirements
- Extension of the concept of interest (e.g. also economically equivalent expenses and other expenses in connection

with the procurement of borrowed 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

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- Applicable for the first time to interest expenses arising after 31 December 2023.

## 2. 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 increase of the share for 2024 to 2027 from currently 60% to 80%.

## 3. Climate protection investment premium

- For all taxable enterprises irrespective of legal form, size and activity
- Funding period: Limited to approx. six years; In principle, investments commenced and completed after the date of promulgation of the Act and before 1 January 2030
- 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; the assets must be used in the business for two years
  - the assets 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 5,000 euros per asset

- Application: can generally be submitted at the time of purchase/production until 31 December 2031; Maximum of four applications per eligible person in the entire funding period
- Receipt as a contribution without affecting profit or loss.

## 4. Improvement of depreciation possibilities and further investment incentives

### Improvement of depreciation possibilities

- Temporary reintroduction of **declining-balance depreciation** of up to 25%, up to a maximum of 2.5 times straight-line depreciation, for movable fixed assets acquired after 30 September 2023 and before 1 January 2025; introduction of declining-balance depreciation of 6% for residential buildings whose construction is started after 30 September 2023 and before 1 October 2029 or whose acquisition lies within this period
- **Immediate depreciation of low-value assets:** Increase of the limit of acquisition or production costs (from previously 800 euros) to 1,000 euros; from 2024
- **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; from 2024
- **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%; from 2024.

## Expansion of research allowance (in principle from 2024)

- Among other things, expansion of the eligible expenses to include the reduction in value of depreciable 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
- 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.

## 5. 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 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.

### **BFH (I R 48/20): Prohibition of Loss Offsetting in the Case of Retroactive Tax Effect of a Conversion**

In its ruling of 12 April 2023 (I R 48/20), the Federal Tax Court (Bundesfinanzhof, BFH) ruled on various aspects of the prohibition of loss offsetting in the case of retroactive tax effect of a conversion, including the fact that it also applies in cases where there is no intention to abuse the tax system.

Background: According to German Reorganization Tax Law, reorganizations and contributions can be carried out with tax retroactivity of up to 8 months. The period of this retroactive effect is the "tax retroactive period". The retroactive effect has the consequence that the income and assets of the transferring company are already attributable to the acquiring company at the end of the tax transfer date. In the case of retroactivity, a special prohibition on offsetting losses applies when a "profit company" is converted to a "loss company" (Sec. 2 (4) 3 Reorganization Tax Law): positive income of the transferring company generated in the retroactive period cannot be offset against losses of the acquiring company. This means that the profits earned by the

transferring company in the retroactive period are subject to taxation even if the acquiring company, to which the income of the transferring company is already attributed, otherwise incurred losses in the assessment period of the conversion.

In the case decided, a business was transferred by way of a spin-off to a corporation newly established as a result of the spin-off. Under civil law, the spin-off took place in July 2017 with retroactive effect for tax purposes as of 1 January 2017. The spun-off business generated profits until July 2017, while the acquiring corporation generated losses overall in 2017. It was questionable whether and to what extent the loss offset prohibition applied.

The BFH ruling is the first decision with comprehensive explanations on the scope of application of the loss offset prohibition, which was newly introduced in 2013. The BFH establishes the following principles in this regard:

1. The prohibition of loss offsetting is also applicable in cases where there is no intention to abuse the tax system.
2. The rule applies not only to income tax and corporate income tax, but also to trade tax.
3. The ban on offsetting applies to the entire fiscal year. I.e. the prohibition of offsetting is not limited to losses from the retroactive period, the profits of the transferring company can also not be offset against losses of the acquiring company, which were incurred only after the registration in the commercial register (i.e. after the end of the tax retroactive period - here: July 2017) and until the end of the financial year (31 December

2017). Since in the case decided upon the acquiring company was only newly established as a result of the spin-off (in July 2017), this affects its entire losses.

4. An interim tax balance sheet is regularly required to determine the profits of the transferring company from the retroactive period, otherwise the profit must be estimated.

### **Federal Constitutional Court (2 BvL 22/17): Tax Valuation of Pension Provisions**

On 28 July 2023, the Federal Constitutional Court declared a submission by the Lower Tax Court of Cologne inadmissible. The submission procedure concerns the question of whether the application of an interest rate of 6% for the calculation of pension provisions provided for in the Income Tax Act is compatible with the general principle of equality of the German Constitution.

In the tax balance sheet pension provisions may only be recorded at the going concern value of the pension obligation. When determining the going concern value, a flat interest rate of 6% must be used, in deviation of the provision applicable under commercial law.

In the case under review the plaintiff had retirement benefit obligations under the company pension scheme. The pension provisions as recorded in the commercial balance sheet were higher than the amount reported in the tax balance sheet. The difference resulted from the interest rate of 3.89% (in 2015) which had to be used for measuring pension provisions in the commercial balance sheet.

The Lower Tax Court of Cologne had opined that the determination for tax purposes of an interest rate of 6% for the measurement of pension provisions infringes the

general principle of equality as it results in unequal treatment regarding the realization principle that applies in all other accounting rules. In addition, the provision was in breach of the prohibition of arbitrary action. According to the Lower Tax Court the interest rate of 6% has not been compatible with reality for years, and the period of 33 years (1982 to 2015) which has elapsed since the legislator last reviewed the standardization was no longer acceptable from a constitutional law perspective.

The submission of the Lower Tax Court of Cologne has now been declared inadmissible because, according to the Federal Constitutional Court, it does not meet the requirements for demonstrating a violation of Article 3 para. 1 of the German Constitution.

As far as can be seen, no BFH case is pending that directly relates to the question of the constitutionality of the interest rate for pension provisions. However, the Lower Tax Court of Münster ruled for the years in dispute 2010-2012, among other things, that an unconstitutionality could not be assumed (10 K 4131/15 F of 18 March 2021; appeal pending before the Federal Tax Court under file no. XI R 25/21).

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## Imprint

Published by

KPMG AG  
Wirtschaftsprüfungsgesellschaft  
THE SQUAIRE / Am Flughafen  
60549 Frankfurt

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