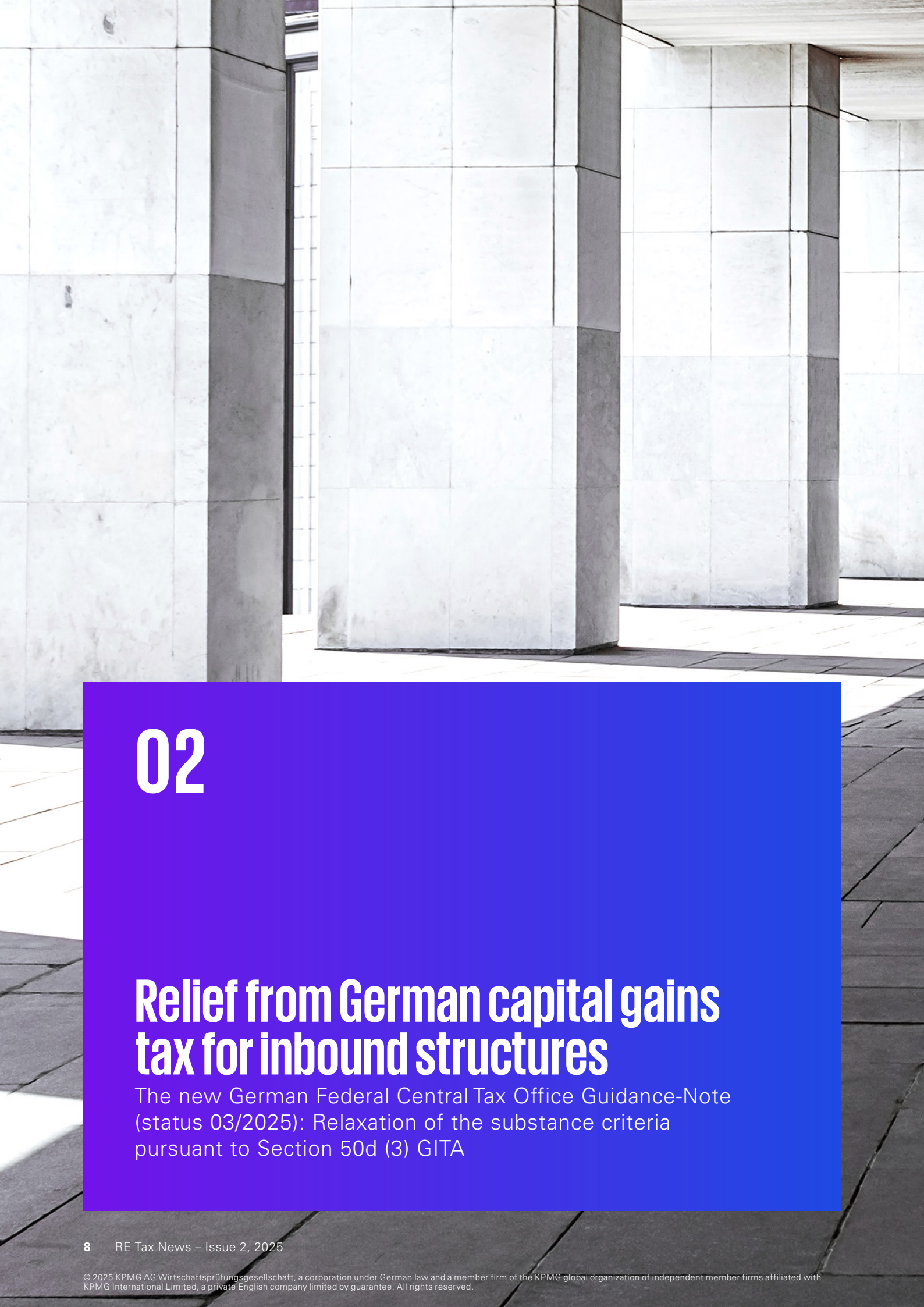

02

Relief from German capital gains tax for inbound structures

The new German Federal Central Tax Office Guidance-Note (status 03/2025): Relaxation of the substance criteria pursuant to Section 50d (3) GITA

In the case of a foreign corporation, the withholding tax relief to which it is entitled - on the basis of a Double Tax Treaty (DTT) or the Parent-Subsidiary Directive (PSD, Section 43b German Income Tax Act hereinafter: GITA) - with regard to dividend payments from Germany is linked to the substance criteria of Section 50d (3) GITA. The wording of Section 50d (3) GITA is subject to interpretation and dispute. This is aggravated by the fact that there is hardly any case law on the current version of the provision and no issued letter from the Federal Ministry of Finance (i.e. BMF-Schreiben). It is therefore all the more pleasing that the current Guidance-Note from the Federal Central Tax Office (as of 03/2025) addresses the interpretation of the substance criteria from the perspective of the tax authorities, who have partially relaxed their view.

Wording of Section 50d (3) GITA and relaxations due to the new German Federal Central Tax Office Guidance-Note

The wording of Section 50d (3) sentence 1 GITA is worded negatively and includes an „and link". Accordingly, a foreign corporation is not entitled to relief, to the extent that its shareholders would not be entitled to this claim if they realised the income directly and – to put it simply – where the entity does not carry out any active economic activity of its own. Section 50d (3) sentence 2 GITA also states that section 50d (3) sentence 1 GITA does not apply if the foreign corporation proves that none of the main purposes of its involvement is to obtain a tax advantage or that it is listed on a stock exchange.

For the legal practitioner, it is easier to read § 50d (3) sentence 1 GITA positively, i.e. under which conditions the foreign corporation is entitled to relief.[1] The „and-linkage" then becomes an „or-linkage". The link with section 50d (3) sentence 2 GITA then results in a total of four alternative options for the foreign corporation to prove a claim for relief.[2]

Accordingly, a foreign corporation is entitled to relief from German withholding tax on the basis of a DTT/EU Directive, provided that

- their shareholders would be entitled to this claim in the event of an imaginary direct receipt of income from Germany (so-called "hypothetical relief claim" of the shareholders pursuant to section 50d (3) sentence 1 no. 1 GITA, while also taking into account the requirements of section 50d (3) GITA at their level) or

- the source of income from Germany, i.e. in the case of dividends, the shareholding in the corporation, has a substantial connection with its economic activity (so-called own active economic activity of the foreign corporation as the applicant pursuant to Section 50d (3) sentence 1 no. 2 half-sentence 1 GITA). The mere generation of income, its transfer to shareholders (so-called "passive holding activity"[3]) as well as an activity, insofar as it is carried out with a business operation that is not appropriately set up for the business purpose, is deemed to be a passive holding activity pursuant to Section 50d (3) sentence 1 no. 2 half-sentence 1 GITA. Section 50d (3) sentence 1 no. 2 half-sentence 2 GITA does not qualify as an economic activity, or

- there is significant and regular trading in the main class of shares on a recognised stock exchange (so-called "stock exchange clause" pursuant to section 50d (3) sentence 2 alt. 2 GITA) or

- it succeeds in proving that none of the main purposes of its involvement is to obtain a tax advantage (so-called "proof to the contrary" or "principal purpose test" pursuant to Section 50d (3) sentence 2 alt. 1 GITA, in order to ensure that the provision complies with European law).[4]

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1 *See also the German Federal Central Tax Office Guidance-Note on the interpretation of Section 50d (3) GITA, as of 3/2025.*
2 *See also the German Federal Central Tax Office Guidance-Note on the interpretation of Section 50d (3) GITA, as of 3/2025.*
3 *So-called pure conduit companies within the meaning of ECJ case law, judgements of 26 February 2019 - C-116/16, C-117/16 „T-Danmark and Y-Denmark.*
4 *Cf. RegE to the AbzStEntModG, BT-Drucks. 19/27632 S. 60.*

Relaxation of the "hypothetical relief claim" of the shareholders:

The wording of Section 50d (3) sentence 1 no. 1 GITA „insofar as their shareholders would be entitled to this claim in the event of an imaginary direct receipt of income from Germany" essentially permits the following two interpretations:

Strict interpretation in the sense of the explanatory memorandum („all-or-nothing principle"):[5]

According to the explanatory memorandum, the shareholder must, in deviation from the previously applicable version of the law[6], according to „the same entitlement provision" be entitled to discharge.[7] This is not the case even if the shareholder has the same amount of relief, but the entitlement arises from a different DTT.[8] Furthermore, Section 50d (3) GITA should also be applied at shareholder level, i.e. they must also be actively involved.[9] If, according to these criteria, there is no hypothetical claim for relief on the part of the shareholders, the claim should be denied in full. Only the complete denial of the claim for relief would prevent the incentive to engage in „experimental" tax structuring abuse.[10]

The relaxed interpretation within the meaning of the new Guidance-Note („insofar as interpretation"):[11]

According to the explanations in the new Guidance-Note, it is now only necessary to check whether there is an entitlement to relief on the merits, i.e. irrespective of the legal basis on which this entitlement to relief is based. In future, the entitlement to relief will only be restricted in terms of amount if the parties involved would have a lower entitlement to relief. This applies to both direct and indirect shareholdings. However, Section 50d (3) GITA should continue to be taken into account at the shareholder level insofar as corporations have a stake in the applicant.

Example:

- The applicant is a passive EU corporation that does not carry out any active economic activity of its own pursuant to Section 50d (3) sentence 1 no. 2 half-sentence 1 GITA and is also not itself listed on a stock exchange within the meaning of Section 50d (3) sentence 2 alt. 2 GITA. It holds a 100% interest in a German corporation that distributes dividends.

- Its sole shareholder is an actively operating corporation that is domiciled in a third country and, according to the DTT concluded with Germany, would only be entitled to 5% tax relief if the dividends were received directly from Germany. In turn, only natural persons are involved in the shareholder.

- According to the strict interpretation in the sense of the explanatory memorandum („all-or-nothing principle") described above, Section 50d (3) sentence 1 no. 1 GITA would not be relevant, as the shareholder would not be entitled to relief under the same standard (DTT vs. MTR).

- There would also be a risk that the applicant would not be able to successfully provide evidence to the contrary pursuant to Section 50d (3) sentence 2 Alt. 1 GITA. Due to the difference in the amount of relief, it could be argued that one of the main purposes of its involvement is to obtain a tax advantage.

- There would be a withholding tax deduction with offsetting effect in the full amount (26.375%).

- According to the new relaxed interpretation, the applicant is entitled to 5% relief.

Relaxation of the stock exchange clause:

Pursuant to Section 50d (3) sentence 2 half-sentence 2 GITA, the stock exchange clause requires that the main class of shares in the applicant is traded substantially and regularly on a recognised stock exchange. According to the explanatory memorandum regarding the law[12], the stock exchange listing of a shareholder is only sufficient if the shareholder is entitled to relief under the same provision or is resident in the same country as the applicant.

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5 E.g. Wagner, in: Brandis, Commentary GITA, Status: 174th Supp. vol. November 2024, Section 50d (3) margin no. 74, with further references.
6 § Section 50d (3) GITA in the version of the Recovery Directive Implementation Act of 7 December 2011, BGBl 2011 I p. 2592, introduced with effect from 1 January 2012.
7 Cf. RegE to the AbzStEntModG, BT-Drucks. 19/27632 S. 58.
8 Cf. RegE to the AbzStEntModG, BT-Drucks. 19/27632 S. 59.
9 Cf. RegE to the AbzStEntModG, BT-Drucks. 19/27632 S. 58.
10 Cf. RegE to the AbzStEntModG, BT-Drucks. 19/27632 S. 58.
11 For example, Loschelder, in: Schmidt, GITA, 44th ed. 2025, Section 50d (3) margin no. 22.
12 Cf. RegE to the AbzStEntModG, BT-Drucks. 19/27632 S. 61.

This view is further relaxed by the new German Federal Central Tax Office Guidance-Note. The prerequisite is that all intermediate companies also have an identical or higher claim to relief compared to the applicant and hold a 100% stake. Conversely, an indirect stock exchange listing is not sufficient if there is no continuous 100% shareholding chain or if an intermediate company would have a lower entitlement to relief compared to the applicant.

Example:

- The applicant is a passive EU corporation that does not carry out any active economic activity of its own pursuant to Section 50d (3) sentence 1 no. 2 half-sentence 1 GITA and is also not itself listed on a stock exchange within the meaning of Section 50d (3) sentence 2 alt. 2 GITA. It holds a 100% interest in a German corporation that distributes dividends.

- Its sole shareholder is a listed corporation that is domiciled in a third country and, according to the DTT concluded with Germany, would be entitled to 0% tax relief if the dividends were received directly from Germany. In turn, only natural persons are involved in the shareholder.

- According to the new Guidance-Note, the stock exchange clause applies. The applicant is therefore entitled to full relief.

Facts

- The new Guidance-Note is to be welcomed from a practical point of view, as it partially relaxes the strict and controversial substance requirements of Section 50d (3) GITA with regard to the „hypothetical relief claim of shareholders“ (Section 50d (3) sentence 1 no. 1 GITA) and the „stock exchange clause“ (Section 50d (3) sentence 2 alt. 2 GITA) and in this respect provides more legal certainty.

- The publication of an announcement by the tax authorities as a Guidance-Note, which is only available on the German Federal Central Tax Office's homepage and is typically not published in the Federal Tax Gazette (Bundessteuerblatt), is atypical. The Guidance-Note has been agreed with the Federal Ministry of Finance and is helpful in practice. Nevertheless, the legal quality of a mere Guidance-Note is questionable. An official publication as issued guidance from the Federal Ministry of Finance in the Federal Tax Gazette (Bundessteuerblatt) - as is usually the case - would therefore be welcome in order to document a higher level of binding force in the application of the law.

- It is noticeable that the title of the new Guidance-Note refers to „relief from German withholding tax on capital gains“, which likely means only to dividends. In my opinion, however, nothing else can apply to license payments.

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