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KPMG INTERNATIONAL

Taxation of Cross-Border Mergers and Acquisitions

Germany

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Germany

Introduction

Germany's 2008 tax reform significantly changed the corporate income tax system by replacing thin capitalization rules with new earnings stripping rules and by further restricting the use of tax loss carry forwards. In 2009 and 2010, these rules were adjusted by the Economic Growth Acceleration Act and the 2010 Tax Act. These changes have important implications for purchasers of German businesses. The following outline of German commercial and tax law is designed to inform foreign investors about their general tax options on the acquisition of a business in Germany.

Unless otherwise stated, the commentary ignores Germany's solidarity surcharge of 5.5 percent on corporate and individual income tax.

Recent developments

Suspension of turn-around exemption

On 26 January 2011, the European Union (EU) Commission ruled that the exemption from the forfeiture of tax losses in the course of a detrimental transfer of shares in turn-around situations constitutes illegal state aid and infringes with EU freedoms providing for the European common market. The German government appealed this ruling before the General Court of the EU. While the proceedings of the German government were dismissed as inadmissible on 18 December 2012 (EGC-Ruling T-205/11) as the period for filing an action had already expired, numerous taxpayers have brought individual actions before the General Court. These cases are still pending.

In view of a potential decision of the EU Commission against the German government and resultant need to collect the granted tax benefits from taxpayers that took advantage of the turn-around exemption, the German tax authorities suspended application of this clause and stayed all appeals against assessments not applying the turn-around exemption since April 2010, subject to the final decision of the Court of Justice of the EU in this regard.

New law on business taxation

The Act on the Modification and Simplification of Business Taxation and of the Tax Law on Travel Expenses was approved by the German legislator on 17 January and 1 February 2013, respectively. The Act provided the following measures (among others):

- simplification and other amendments of the regulations for tax groups for income tax purposes in response to current case law and EU legal requirements
- maximum cap for net operation loss carrybacks increased to 1 million Euros (EUR).

Defective profit transfer/loss absorption

The new provisions relax the formal requirements of the profit transfer under the profit and loss pooling agreement, one of the major requirements for a German tax group. The new rules consider a profit and loss pooling agreement as correctly executed even where the transferred profit or compensated loss is based on an annual financial statement that contains incorrect carrying amounts, provided certain requirements are met (i.e. where the financial statement was approved by the shareholders, where an unqualified auditor's opinion was issued and where the incorrect amount is rectified). The related tax obligation to correct an error only applies where the error is to be corrected in the financial balance sheet. Where a correction is not required under commercial law, the financial statement does not need to be corrected for the purpose of executing the profit and loss pooling agreement.

Wording of the loss absorption

Where a controlled company has the legal form of a limited liability company (GmbH), recognition of a tax group was conditional on concluding an "agreement on the absorption of losses in accordance with Sec. 302 German Stock Corporation Act (GCSA, [*Aktiengesetz* – AktG])".

According to the recently amended law, a dynamic reference, that is, loss absorption with reference to Sec. 302 GSCA in its relevant version as amended from time to time, must be specifically agreed in profit and loss pooling agreements concluded after 25 February 2013.

Further, the Act on the Modification and Simplification of Business Taxation and of the Tax Law on Travel Expenses provided an interim regulation for existing profit and loss pooling agreements that do not include a reference to Sec. 302 GSCA in accordance with prior tax law. In these cases, the tax group is not denied for the assessment periods ending before 1 January 2015. However, the tax group is only accepted where loss absorption has actually occurred and a dynamic reference has been effectively agreed until 31 December 2014. An amendment of existing profit and loss pooling agreements is superfluous, however, where the tax group is terminated prior to 1 January 2015.

Profit and loss pooling agreements concluded before 26 February 2013 that include a correct but undynamic reference to Sec. 302 GSCA do not have to be amended.

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'Dual domestic link' of controlling entity

Until the recent amendment of the provision governing the tax group for income tax purposes, only entities with their seat and place of management in Germany could become a controlled entity in a tax group.

In response to infringement proceedings (No. 2008/4909) initiated by the European Commission, the dual domestic link provisions have been abolished. Instead, a corporation with its place of management in Germany and its registered seat in the EU or European Economic Area (EEA) may become a controlled company in a tax group.

Expanded dual consolidated loss rules

The dual consolidated loss rules have been expanded and should be much more relevant in the future. According to the amended rules, a non-deductible dual consolidated loss arises where a loss of either a controlling or controlled entity can be deducted in another country (including EU/EEA countries) by the controlling entity, the controlled entity or another person. The new rules apply to all open tax years.

New tax regulations for dividends

The German legislator has amended the German dividend taxation for corporate investors in the free float ('*Streubesitzdividenden*') in response to a decision of the Court of Justice of the EU (ECJ-Ruling C-284/09).

According to the new rules, dividends from shareholdings of less than 10 percent of the paying company's share capital received on or after 1 March 2013 are no longer 95 percent tax-exempt; such dividends are subject to corporate income tax at shareholder level. The current tax exemption for capital gains derived from the disposal of shares remains unchanged irrespective of the shareholding held in the company.

Administrative assistance implementing act

The Administrative Assistance Implementing Act was approved by the German Bundestag and Bundesrat on 6 and 7 June 2013, respectively. Among other things, the Act provides for

- measures against so-called real estate transfer tax (RETT) 'Blocker Structures'
- extension of the group exemption for real estate transfer tax purposes
- further limits on the offsetting of losses in case of reorganizations
- extension of the requirement of corresponding taxation of hybrid capital instruments for the application of the German participation exemption.

RETT blocker structures

The transfer of shares in real estate-owning companies can trigger RETT where at least 95 percent of the shares in the company are accumulated or at least 95 percent of the shares are transferred to a new shareholder. By interposing companies according to so-called RETT Blocker Structures, it was possible to avoid RETT on certain transactions, even though more than 95 percent of the shares were directly and indirectly transferred to a new shareholder from an economic point of view.

However, since June 2013, the RETT Blocker Structures do not work for new transactions as the amended Real Estate Transfer Tax Act now considers an 'economic participation'. According to the new provisions, a transaction triggers RETT where a person or company acquires an economic participation of at least 95 percent in a real estate owning company. Such participation equals the sum of direct and indirect participations in the capital or assets of the company. In the case of indirect participations, the participations in the capital or assets must be multiplied on each participation level. The tax authorities issued guidance on the new provisions on 9 October 2013.

Group exemption from RETT

Pursuant to the group exemption for RETT purposes, no RETT is levied in the case of group internal reorganizations, provided certain conditions are met. According to the new regulation, the scope of the group exemption provision includes, in addition to mergers, demergers and carve-outs, contributions as well as other transactions on the basis of the articles of association. The provision applies to transactions implemented after 6 June 2013. The tax authorities issued guidance on the amended group exemption clause on 9 October 2013, which follows a restrictive interpretation of the group exemption provisions. According to this guidance, the group exemption clause applies only to the transfer of real estate, where the real estate is transferred by universal succession.

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Limits on offsetting losses on reorganizations

Where a reorganization is implemented with retroactive effect, the income and net business assets of the transferring corporate entity and the receiving entity generally are determined as if the business assets of the corporate entity had been transferred to the receiving entity at midnight on the date of the reorganization balance sheet.

However, certain restrictions apply with regard to offsetting losses of the transferring entity with income of the receiving entity. These restrictions were expanded regarding the offset of losses of the receiving entity. New rules for reorganizations and contributions implemented after 6 June 2013 no longer permit the receiving entity to offset its losses or interest carried forward against income of the transferring entity generated in the period of retroactivity. Therefore, the income attributed to the receiving entity is fully taxed. The limit on offsetting losses does not apply where the transferring entity and the receiving entity are affiliated companies pursuant to Sec. 271 para. 2 German Commercial Code (*Handelsgesetzbuch* – HGB) before midnight on the date of transfer ('group clause').

Corresponding taxation of hybrid capital instruments

While hybrid capital instruments that are classified as equity in Germany lead to dividend income, the classification as debt in a foreign state allows for a deduction of interest paid on the hybrid capital as expenses for income tax purposes.

Dividend income is generally 95 percent income-tax-exempt in Germany if received by a corporation or 40 percent tax-exempt if received by an individual. Hybrid capital instruments are granted an interest deduction without a corresponding income inclusion. According to new provisions of the German Corporate Income Tax Act and the German Income Tax Act, these tax exemptions do not apply where the 'dividend' received is tax-deductible at the level of the dividend distributing entity, thus preventing an arbitrage by hybrid instruments in the future. The new provisions apply for fiscal years beginning after 31 December 2013.

Provisions for contingent losses ('*angeschaffte Drohverlustrückstellungen*')

Certain liabilities may not be fully recognized on the tax balance sheet, thus resulting in built-in losses for tax purposes. However, the German Federal Tax court has decided that such built-in losses are realized if acquired in an asset acquisition. In response to these decisions, the German legislator introduced new statutory rules that govern the treatment of transferred built-in losses by the seller and the purchaser.

According to these rules, which apply for business years ending after 28 November 2013, the seller may realize the built-in losses subject to certain limitations. Generally, built-in losses that are realized due to the transfer of a liability may not be fully deducted in the year of transfer but must be spread over a period of 15 years, unless the following provisions apply:

- Built-in losses realized on the sale or transfer of an entire business or an entire partnership interest or due to the transfer of pension obligations when an employee changes employers may be deducted in whole in the year of transfer. This treatment also applies to built-in losses realized by certain small and medium-sized businesses irrespective of the underlying cause.
- Built-in losses may be set off against hidden reserves that are realized on the sale or transfer of a self-contained business division.

Regardless of the treatment of any built-in losses realized by the seller, the purchaser must apply the original restrictions on the recognition of liabilities in the tax balance sheet of the business year in which the acquisition takes place. Due to the 'reinstatement' of the original tax accounting restrictions, the purchaser will realize taxable income. However, the purchaser is allowed to recognize 14/15 of the amount of such taxable income as a tax-free reserve, which must be released into taxable income over the next 14 business years.

Asset purchase or share purchase

The form of an acquisition is often motivated by tax or other commercial factors. The buyer's main preference is to get a step-up in the acquired assets along with a corresponding depreciation base to reduce the future effective tax rate. The seller's primary interest is to minimize capital gains tax or, ideally, to obtain a tax exemption. Under the current law, however, share deals are generally more tax-efficient for all types of owners, whether corporates or individuals.

The transfer of ownership interests is legally simpler than the transfer of numerous scattered assets. It is easier to specify the interests or shares being disposed of than to identify individual assets. Contracts and licenses held by the purchased entity remain effective and may not need to be assumed (requiring the other parties' consent) or renegotiated.

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Purchase of assets

In an asset purchase, the purchased assets are accorded a new cost base for the buyer, and the selling entity realizes a gain/loss amounting to the excess/shortfall of the purchase price over the book value of the assets. Generally, the allocation of such step-up/step-down is performed on an asset-by-asset basis. Goodwill generally is calculated as the difference between the purchase price and the sum of the stepped-up market values of the other assets and is capitalized at this value. An asset deal provides the purchaser with the opportunity to buy only those assets actually desired and leave unwanted assets (e.g. environmentally contaminated real estate) and, in many cases, unwanted liabilities behind.

However, under German law, there are some liabilities that cannot be avoided and pass to the buyer in an asset deal except under certain circumstances. For example, liabilities with respect to existing employment contracts (German Civil Code [*Bürgerliches Gesetzbuch* – BGB], section 613a) and several tax liabilities (General Tax Act [*Abgabenordnung* – AO], section 75) cannot be disclaimed. Although certain liabilities are taken over where the acquired commercial business is continued under the same name (German Commercial Code [*Handelsgesetzbuch* – HGB], section 25), such liabilities could be disclaimed under certain conditions.

From a purchaser's tax perspective, the acquisition of a partnership interest is treated as a pro rata acquisition of the partnership's assets. Consequently, the buyer can step-up the basis in their pro rata share of partnership assets acquired to equal the full purchase price.

Purchase price

Where assets are purchased, the buyer should attempt to persuade the seller to agree to a detailed allocation of the purchase price to the assets. Such an allocation is not binding for tax purposes but provides a useful starting point. Non-competition agreements in connection with asset purchases are generally viewed as part of goodwill and do not constitute independent assets, unless a separate price is determined and allocated in the purchase agreement.

Goodwill

The acquired tangible and intangible assets, including goodwill, are to be capitalized at their fair market values. For tax purposes, goodwill is amortized over a 15-year period.

Depreciation

All other assets are depreciable over their useful lives. The tax authorities have published depreciation tables listing the relevant periods for almost any type of asset.

Contingent losses

The acquisition of liabilities that are not recognized in full in the tax balance sheet of the seller due to certain restrictions for tax accounting purposes results in a post-acquisition profit of the purchaser in the business year of the acquisition as the purchaser must apply the original accounting restrictions. The resulting profit may be spread over a period of 15 years, which may avoid taxation of the post-acquisition profit to some extent where the contingent tax loss is correspondingly realized in the same periods.

Tax attributes

Tax losses, interest, earnings before interest, taxes, depreciation and amortization (EBITDA) carried forward and other attributes are not transferred in an asset deal. They remain with the seller or are eliminated.

Value added tax

Asset purchases of a business or a division (branch of activity) are generally not subject to German value added tax (VAT) law [UStG], section 1 par. 1a). Purchases of shares in a corporation or interests in a partnership are tax-exempt under UStG, section 4 par. 8 (f).

Transfer taxes

There is no stamp duty in Germany. However, the acquisition of property in an asset purchase is subject to RETT on the purchase price allocated to the property. The RETT is between 3.5 and 6.5 percent (depending on the German state in which the real estate is located). If an asset deal triggers RETT the purchaser and seller are generally liable for the RETT. Typically, an asset purchase agreement allocates the RETT as transaction costs to the purchaser.

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RETT is also triggered when at least 95 percent of the shares in a company or partnership owning real estate located in Germany are transferred, directly or indirectly. This also applies where less than 95 percent are transferred but, after the transfer, at least 95 percent of the entity are directly or indirectly owned by one taxpayer or a consolidated tax group. Further, a transaction triggers RETT where a person or company acquires an economic participation of at least 95 percent in a real estate owning company. Such participation equals the sum of direct and indirect participations in the capital or assets of the company. In the case of indirect participations, the participations in the capital or assets must be multiplied on each participation level.

For partnerships, any direct or indirect share transfers within a five-year period are added together for this 95 percent test. Where RETT is triggered by the acquisition of shares in a company or partnership, the RETT is based on a special valuation of the real estate for tax purposes, which amounts to roughly 70 percent to 80 percent of the fair market value. However, the standard assessed value is expected to increase for real estate in the near future. The purchaser or direct or indirect owner of at least 95 percent in a real estate owning corporation is liable for RETT.

There is an exemption of RETT for certain reorganizations within a group, including mergers, de-mergers (split-up, spin-off, carve-out) and certain other transfers of property. Similar reorganizations under the law of another EU or EEA Member State are also privileged. According to the recently amended group exemption clause, contributions and other transactions on the basis of the articles of association also may be exempt from RETT. However, according to a guidance issued by the tax authorities, the group exemption applies only to the transfer of real estate where the transaction allows for universal succession of the receiving entity in the position of the transferring entity.

Further, the group exemption only applies where a company and a controlled company are involved in the reorganization. A company is deemed controlled where the controlling company holds (directly or indirectly) an interest of at least 95 percent within a period of 5 years preceding and 5 years following the reorganization.

Purchase of shares

A share deal does not offer the buyer a step-up of the assets (capitalization of assets at fair market value) of the purchased company to increase the depreciation base. The scope for achieving such a step-up by post-acquisition restructuring is limited. VAT and RETT implications are discussed earlier in this chapter.

Legal form of businesses

When buying a business, it is necessary to understand the legal form in which it is conducted. Most business activity in Germany is carried out through one of the following:

- sole proprietorship (*Einzelunternehmen*)
- general partnership (*offene Handelsgesellschaft* – oHG)
- limited partnership (*Kommanditgesellschaft* – KG)
- limited partnership with corporate general partner (GmbH and Co. KG)
- limited liability company (*Gesellschaft mit beschränkter Haftung* – GmbH)
- Entrepreneurial company with limited liability *(Unternehmergesellschaft (haftungsbeschränkt)* – UG*)*
- stock corporation (*Aktiengesellschaft* – AG).

The federal German law governs these enterprises. A corporation (AG, GmbH, UG) is subject to corporate income tax (since 2008, 15 percent), solidarity surcharge (5.5 percent of the corporate tax), trade tax (approximately 14 percent), and VAT (19 percent standard rate). A partnership (oHG, KG, GmbH and Co. KG) is transparent for corporate income tax purposes (i.e. partnership income is attributed to and taxed in the hands of the partners) but not for trade tax purposes. An election to treat a partnership as a corporation is not possible for German tax purposes.

Of these legal forms, the GmbH and Co. KG, GmbH, UG and AG allow a limitation of the owners' liability to the agreed capital contribution. In the case of the GmbH and Co. KG, this applies, strictly speaking, only to the limited partners. The general partner, the GmbH, does not need to make any capital contribution or be entitled to any share of profits. The management of the GmbH and Co. KG usually rests with its general partner, the GmbH, but this is not mandatory.

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Limited liability company: *Gesellschaft mit beschränkter Haftung* (GmbH)

The GmbH is the most common form of business association. It is a corporate entity with its own legal identity, has one or more shareholders, and has a share capital of at least EUR25,000. Shares in GmbHs are not certified. The purchase and transfer of shares in an existing GmbH requires an agreement, which must be recorded in the presence of a qualified notary. The management of a GmbH rests with one or more managing directors appointed by the shareholders. The managing directors are subject to close supervision and control by the shareholders and are generally obliged to respect instructions given to them at the shareholders' meeting. Where a GmbH has at least 500 employees, a supervisory board must be established according to provisions applicable to AGs. The shareholders control the distribution of net earnings.

Entrepreneurial company with limited liability: *Unternehmergesellschaft (haftungsbeschränkt)* (UG)

The legal form of the UG was established by the German Act to Modernize the Law Governing Limited Liability Companies and to Combat Abuses (*Gesetz zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen* [MoMiG]), dated 1 November 2008.

The UG is not an independent legal form but a subtype of the limited liability company. It may be formed with a share capital of EUR1 to EUR24,999, but is subject to specific statutory restrictions (e.g. contributions in kind may not be performed by an entrepreneurial company).

The UG generally is treated like a GmbH for tax purposes. By increasing the capital to at least EUR25,000, an UG can become a GmbH.

Stock corporation: *Aktiengesellschaft* (AG)

The AG is also a corporate entity with its own legal identity. The minimum share capital is EUR50,000. The management structure invariably consists of a management board and a supervisory board.

The management board is in charge of the management and representation of the AG. The members of the management board are appointed and removed by the supervisory board. The supervisory board only monitors the management board and represents the AG in relation to the management board. The articles of association may stipulate that specific actions of the management board require the prior approval of the supervisory board.

The supervisory board must consist of at least three members or a higher number divisible by three. The shareholders elect the members. Where the AG has more than 500 employees, one-third of the members of the supervisory board must be elected by the employees. Generally, the shares in AGs are certified.

In contrast to the GmbH, AG shares need not be transferred in notarized form and can be traded on the stock exchanges. The shareholders control the distribution of at least 50 percent of net earnings.

General partnership (oHG), limited partnership (KG), limited partnership with corporate general partner (GmbH & Co. KG)

In an oHG, no minimum capital is required and all partners are fully liable for the partnership's debts. In contrast, in a KG, there are general partners (*Komplementär*) with unlimited liability and limited partners (*Kommanditisten*) whose liability is restricted to their fixed contributions to the partnership. Although a partnership itself is not a corporate body, it may acquire rights and incur liabilities, acquire title to real estate and sue or be sued. Generally, all partners that are fully liable for the partnership's debts act as managing directors in contrast to the partners subject to limited liability. From a legal perspective, the transfer of shares in a partnership generally does not need to be recorded in the presence of a qualified notary.

The GmbH and Co. KG is a limited partnership in which the sole general partner is typically a GmbH, combining the advantages of a partnership with those of a limited liability corporation.

Other forms

The following, less common forms of association may also be encountered:

- private association (*Verein*)
- cooperative (*Genossenschaft*)
- foundation (*Stiftung*)
- partnership limited by shares (*Kommanditgesellschaft auf Aktien* – KGaA).

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Associations and cooperatives can be useful in structuring cooperation among several independent parties. Foundations resemble common-law trusts to some degree. These three organizations are popular for non-profit activities but are not widely used for business purposes.

The partnership limited by shares is still rare but is becoming more popular.

Commercial and non-commercial activity

German company and tax laws distinguish between trade and business activities (commercial activity) and other activities. Generally, the tax law assumes commercial activity where a company exercises a trade (which is not related to self-employment or passive asset management) for the purposes of making a profit. Capital gains generally are taxable where the property is sold as part of a commercial activity or is held by companies that are, by virtue of the law, trading companies.

Apart from a tax liability for capital gains, the main tax consequence of commercial activity is the liability for trade tax, which is imposed only on commercial enterprises. By virtue of their corporate legal form, company law and tax law deem the AG, the GmbH and the UG to be engaged in commercial activity.

Tax indemnities and warranties

In a share acquisition, the purchaser is taking over the target company together with all related liabilities, including contingent liabilities. Therefore, the purchaser normally requires more extensive indemnities and warranties than in the case of an asset acquisition.

Unlike the United States/Anglo-Saxon legal principle of caveat emptor (let the buyer beware), German law generally does not require the purchaser to examine an entity they intend to purchase in advance. However, according to the German Civil Code (*Bürgerliches Gesetzbuch*), a purchaser forfeits their rights and guarantee claims regarding a defect they are unaware of where gross negligence is involved. The non-performance of due diligence prior to the acquisition of an entity generally does not result in the purchaser being grossly negligent. This is only the case where the purchaser did not perform due diligence despite obvious defects of the target or suspicious facts. The purchaser's decision on whether or not to perform a due diligence thus depends on an assessment of the individual circumstances.

In contrast, the vendor may have a pre-contractual duty to inform the purchaser about certain defects of the target according to the German law principle of culpa in contrahendo. This principle implies that a party with important information to which the other party does not have access must share it with the other party so that it can contract with sufficient knowledge of the facts. The extent of this obligation again depends on the individual case, particularly the value or significance of the transaction.

Tax losses

Use of pre-acquisition losses

In Germany, tax losses may be carried forward indefinitely for trade tax on income and personal or corporate income tax purposes. Personal or corporate income tax losses may also be carried back to the previous fiscal year, up to a maximum of EUR1 million.

Since 2004, the use of tax loss carry forwards is restricted by a minimum taxation scheme. Only EUR1 million plus 60 percent of the taxpayer's current year income in excess of EUR1 million can be offset against tax loss carry forwards. The restriction applies to both corporate income tax and trade tax.

As of 2008, the use of pre-acquisition losses was virtually excluded by the general change of control rules. These rules lead to a partial forfeiture of loss carry forwards where more than 25 percent of the shares in a corporation are acquired by a purchaser or a purchasing group or related parties within a period of 5 years. Where more than 50 percent of the shares are acquired, all loss carry forwards are forfeited. The rules apply to any direct or indirect change in the shareholder structure, so the acquisition of a multinational group at the top holding level may also lead to a forfeiture of losses in a German group company.

However, for share transfers after 31 December 2009, the change of control rules generally provide that unused tax losses of a corporation are not forfeited on a share transfer up to the amount of the domestic built-in gains of the loss company. Therefore, tax loss carry forwards are only forfeited to the extent the losses carried forward exceed the transferee's domestic built-in gains in the business assets at the time of the detrimental change of control.

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This provision covers share acquisitions from third parties as well as related parties. The latter case may become relevant where the criteria under the group exemption clause are not met (as discussed later in this chapter). The built-in gains of the corporation's domestic (i.e. fully taxable) business assets prevent the forfeiture of current-year tax losses as well as tax losses carried forward. The built-in gains are determined by comparing the equity according to the tax accounts and the fair value of the shares of the loss company (which generally equals the purchase price). A determination on a pro rata basis applies where not more than 50 percent of the shares in a loss-making corporation are transferred. Built-in gains not subject to tax in Germany must be deducted (in particular, shares in corporations for which a capital gains exemption applies). An amendment by the 2010 Tax Act to the exemption relating to taxable built-in gains eliminated the restriction to domestic business assets only so that foreign business assets subject to German taxation are taken into account as well. Moreover, where the equity of a loss-making entity is negative, the built-in gains are determined by comparing the equity according to tax accounts and the fair market value of the business assets (instead of the fair market value of the shares) to exclude built-in gains calculated in the shares that pertain to tax assets only.

An internal reorganization before 1 January 2010, such as the interposition of a new holding entity, could also trigger the general change of control rules. For reorganizations after 1 January 2010, the change of control rules for corporations are eased by a new exception applying to share transfers within a group of companies. Under this exception, a change of ownership is not viewed as detrimental where 100 percent of the shares in the transferee and transferor are held directly or indirectly by the same person (i.e. wholly owned subsidiaries of a common parent). Hence, a group exemption provision is not applicable where the transferring and acquiring entity belong to a group of companies but shares in the transferring and/or acquiring entity are held by outside (minority) shareholders.

In addition, a turn-around exemption clause was introduced in 2009. This clause states that the acquisition of shares in a loss-making company is not affected by the change of control rules if it serves the purpose of turning around the company's business. The turn-around (*Sanierung*) refers to a measure that aims at:

- preventing or abolishing illiquidity or over-indebtedness
- preserving the essential business structures at the same time.

According to the rationale for the new law, an acquisition serves the purpose of turning around the business where the acquisition takes place when the company in question faces potential or actual illiquidity or over-indebtedness. Further, to be considered an acquisition of shares for the purpose of turning around the business under the act, the company must show turn-around potential at the time of the acquisition.

The turn-around exemption does not apply where:

- the corporation had largely discontinued its operation at the time of the change in ownership
- a change in the line of business occurs within 5 years after the change in ownership.

The exemption clause was initially introduced as a temporary measure for share transfers taking place until 31 December 2009. This time limitation was later removed.

On 26 January 2011, the EU Commission ruled that this measure constitutes illegal state aid and therefore is not in line with the requirements of the Common Market. While the proceedings of the German government against the ruling were dismissed as inadmissible by the General Court of the EU (EGC, 18. December 2012, T-205/11), numerous taxpayers have brought individual actions before the court. These cases are still pending. In view of the potential ruling of the EU Commission, the German tax authorities had already suspended the application of the turn-around exemption and stayed all appeals against assessments not applying the turn-around exemption since April 2010, subject to a final court decision. The suspension was also implemented by the German legislator in December 2011.

Note that these change of control rules also apply to excess interest carried forward under the new earnings stripping rules.

For partnerships, a direct acquisition of interests in a partnership limits the utilization of the trade tax loss carry forwards of the partnership or even triggers their partial or complete forfeiture. This can only be avoided by acquiring the partnership interest indirectly. However, where the partners are corporate entities, even an indirect share transfer may lead to a forfeiture of tax losses.

Finally, the transfer of tax losses carried forward on mergers under the German Mergers and Reorganizations Tax Act has been abolished, so that all losses disappear in a corporate reorganization. Therefore, a step-up to the fair market or an interim value may be implemented to optimize loss utilization.

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In addition, certain restrictions apply with regard to offsetting losses of the transferring entity and the receiving entity where a reorganization is implemented with retroactive effect. Generally, the income and business assets of the transferring corporate entity and the receiving entity are determined as if the business assets of the corporate entity had been transferred to the receiving entity at midnight on the date of the reorganization balance sheet. However, certain restrictions apply with regard to offsetting losses of the transferring entity at the level of the receiving entity. These restrictions were expanded for the offset of losses of the receiving entity. For reorganizations and contributions implemented after 6 June 2013, it is no longer permissible for the receiving entity to offset its losses or interest carried forward against income of the transferring entity generated in the period of retroactivity. Therefore, the income attributed to the receiving entity is fully taxed. The limit on offsetting losses does not apply where the transferring entity and the receiving entity are affiliated companies pursuant to Sec. 271 para. 2 German Commercial Code (*Handelsgesetzbuch* – HGB) before midnight on the date of transfer ('group clause').

Transfer taxes

See transfer taxes in this chapter's purchase of assets section.

Tax clearances

Tax clearances are recommended, especially in cases of complex acquisition structures, such as under the German reorganization law. A taxpayer can apply for a so-called binding ruling with the competent tax authority regarding the application of tax laws to certain specific facts but not on the existence of certain facts. While the tax authorities have discretion to issue a tax ruling, they can only decline to issue a ruling in limited circumstances. The tax authorities are bound by binding rulings granted to the taxpayer where the taxpayer has executed the transaction as described in its application for the ruling.

The taxpayer must pay a fee with the application of the binding ruling unless the value of the dispute does not exceed EUR10,000. The maximum fee is currently capped at EUR109.736, which equals a value of dispute of EUR30 million.

Choice of acquisition vehicle

A foreign purchaser may invest in a German target through different vehicles. The tax implications of each vehicle may influence the choice. Germany does not levy stamp tax or capital duty on funding a German company or branch.

Local holding company

A German holding company is typically used when the purchaser wishes to ensure that tax relief for interest (e.g. resulting from a debt pushdown) is available to offset the target's taxable profits (see choice of acquisition funding) or taxable profits of other German companies already owned by the purchaser within a tax-consolidation scheme (see group relief/consolidation).

Capital gains derived by a resident corporate shareholder are essentially 95 percent exempt from corporate income tax irrespective of the participation quota, holding period and source (domestic or foreign).

As of 1 March 2013, the 95 percent exemption only applies to dividend income of the resident corporate shareholder where the investment accounts for at least 10 percent of the share capital at the beginning of the respective calendar year.

For trade tax purposes, the 95 percent exemption of dividend income only applies where the investment accounts for at least 15 percent of the share capital or an equivalent participation quota in the assets at the beginning of the respective fiscal year.

Foreign parent company

A foreign purchaser may choose to perform the acquisition itself, perhaps to shelter its own taxable profits with the financing costs related to the investment in the German target. Where the German target is a trading partnership, the financing costs of the foreign parent company in connection with the acquisition of the partnership interest are generally tax-deductible at the level of the German partnership, subject to restrictions of the German earnings stripping rules and a 25 percent add-back for trade tax purposes.

Thus, investments in German partnerships by a foreign parent company may potentially provide a double dipping opportunity where debt-financing is taken out at the level of the foreign parent company.

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For a German corporate subsidiary, dividend distributions are subject to withholding tax (WHT) at a rate of 25 percent, increased to 26.375 percent by a 5.5 percent solidarity surcharge. The dividend WHT may be reduced to 15.825 percent where the foreign parent company is not domiciled in a country that has a tax treaty with Germany. If there is a tax treaty or the EU Parent-Subsidiary Directive applies, the WHT may be reduced to tax treaty rates or to zero under German domestic tax law, provided the foreign parent company meets the requirements of the German anti-treaty shopping rules (see anti-treaty shopping rules).

Where the foreign parent company invests through a German trading partnership, generally, the parent has a limited tax liability in Germany on its income from the partnership. A withdrawal of capital from the trading partnership is not subject to WHT.

In principle, a capital gain on disposal of the investment in the German company is subject to tax in Germany under German domestic tax law. Capital gains tax is mitigated by the German participation exemption rules for corporate shareholders, which principally provide for a 95 percent tax exemption, or by the partial income system for individual shareholders, which provides for a 40 percent tax exemption (previously 50 percent) where the German company is a corporate entity. Where individual shareholders hold less than 1 percent of the share capital as private property, a flat tax rate of 25 percent plus solidarity surcharge applies. A full capital gains tax exemption may be available on the disposal of shares in a company if the tax treaty allocates the right to tax capital gains to the foreign parent company's country of residence.

Non-resident intermediate holding company

Interposing an intermediate holding company generally implies an additional layer of taxation on funds repatriated to the investor. A non-resident intermediate holding company may be an option where the investor's country of residence taxes capital gains and dividends received from abroad. An intermediate holding company resident in another territory could be used to defer this tax and take advantage of a more favorable tax treaty with Germany.

The same German tax implications set out earlier for foreign parent companies apply to non-resident intermediate holding companies.

In terms of WHT relief, using a non-resident intermediate holding company is only more tax-efficient than a direct investment where the intermediate holding company meets the requirements of the German anti-treaty shopping rules. To the extent that the non-resident intermediate holding company does not derive its income from own business activities and lacks sufficient substance, the German anti-treaty shopping rules look through to its shareholder (see anti-treaty shopping rules).

Where the shareholder meets the requirements, the intermediate holding company may claim the benefits of a tax treaty or German domestic tax law implementing the EU Parent-Subsidiary Directive. However, the benefits are limited to the extent that the ultimate shareholder could have claimed them.

Anti-treaty shopping rules

According to the German anti-treaty shopping rules, a foreign company has no right to complete or partial reduction of WHT pursuant to a tax treaty and the German Income Tax Act to the extent its shareholders would not be entitled to the refund or exemption if (a) they derived the income directly; and (b) the foreign company's gross earnings for the respective fiscal year are not derived from its own business activities and

- with regard to these earnings, there are no economic or other valid reasons for the interposition of the foreign company, or
- the foreign company does not participate in general commerce by means of a business organization with resources appropriate to its business purpose.

Local branch

As an alternative to directly acquiring the target's trade and assets, a foreign purchaser may structure the acquisition through a German branch. Germany does not impose additional taxes (such as WHT) on branch profits remitted to an overseas head office. The foreign enterprise is taxable as a non-resident taxpayer on income derived from the permanent establishment in Germany. Thus, the branch's income is subject to German tax at normal corporate and trade tax rates. Where the German operation is initially expected to make losses, a branch may be advantageous, because, subject to the tax treatment applicable in the head office's country, a timing benefit could arise from the ability to consolidate losses with the profits of the head office.

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Unlike the disposal of a German subsidiary by a non-resident being 95 percent or 100 percent tax-exempt, a disposal of a German branch to a third party triggers capital gains tax, other than on capital gains relating to shares in corporations, which are in principle 95 percent tax-exempt.

Joint venture

Joint ventures can either operate though a corporate entity (with the joint venture partners holding shares in a German company) or an unincorporated entity (usually a German limited partnership – *Kommanditgesellschaft*).

Partnerships are generally considered to provide greater tax flexibility. For example, where the joint venture is expected to make initial losses, the partners should be able to use their shares of corporate income tax losses against their existing German profits. However, trade tax losses cannot be transferred and remain at the level of the partnership. Profits of a partnership can be repatriated free of German WHT. Further, financing costs for acquiring a partnership are tax-deductible at the level of the partnership, which allows a debt pushdown. However, any payments to the partners (such as management fees) are not tax-deductible at the partnership level. German real estate investments held by foreigners are often structured using partnerships because no German trade tax arises, provided the business qualifies as non-trading for tax purposes.

Choice of acquisition funding

A purchaser needs to decide whether to fund the acquisition with debt or equity. The main concern is often to ensure that interest on funding can be set off against the target's profits to reduce the German effective tax rate. Tax-deductibility depends on the acquisition vehicle's legal form and place of residence, as well as the legal form of the target.

Debt

The advantage of debt is the potential tax-deductibility of interest (see deductibility of interest), because the payment of a dividend is not tax-deductible at the level of the distributing entity. Where debt is used, the purchaser must decide which company should borrow and how the acquisition should be structured. To allocate the cost of debt efficiently, there must be sufficient taxable profit against which interest payments can be offset. The following comments assume that the purchaser wishes to set off the interest payments against the German target's taxable profits. However, consideration should be given to whether relief would be available at a higher rate in another jurisdiction.

Usually, a German corporation is used as the acquisition vehicle for a share acquisition, funding the purchase price with debt either from a related party (e.g. shareholder loan) or directly from a bank. Dividends received from domestic shareholdings are generally tax-exempt for trade tax purposes if the investment exceeds 15 percent and is held from the beginning of the fiscal year. The exemption applies for corporate income tax purposes if the investment accounts for at least 10 percent of the share capital at the beginning of the respective calendar year. However, 5 percent of any dividend received is treated as non-tax-deductible which effectively reduces the dividend exemption to 95 percent. On the other hand, any business expenses, particularly interest expenses related to German-sourced dividend income, are fully tax-deductible for corporate income tax purposes (for discussion of restrictions on interest expenses and the add-back rules for trade tax purposes, see deductibility of interest).

The most common way to deduct interest expenses and offset them against the target's taxable income is an acquisition through a leveraged acquisition vehicle, followed by the establishment of a tax-consolidation scheme (*Organschaft*). A debt pushdown into the target directly may be achieved by merging the target into the acquisition vehicle or vice versa. Otherwise, interest expenses would remain structurally non-deductible because of the acquisition vehicle's lack of taxable income. In an asset deal, such an offset is automatically achieved where the acquirer of the assets/going concern is provided with the acquisition funding.

Due to the fiscal transparency of partnerships for German corporate income tax purposes, any interest on debt taken out to acquire an interest in a German partnership is tax-deductible at the level of the target, rather than at the level of the acquisition vehicle. Thus, the acquisition of a partnership often results in an automatic debt pushdown for German tax purposes.

If the interest cannot be offset immediately (i.e. there are insufficient taxable profits), the resulting losses can be carried forward for German corporate income and trade tax purposes. In addition, it is possible to carry back losses of up to EUR1 million for German corporate income tax purposes.

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Depending on the existing structures of the purchaser and target groups, it may be possible to introduce leverage into Germany after (rather than at the time of) the acquisition, such as by way of a recapitalization.

Deductibility of interest

As of 1 January 2008, the German thin capitalization rules were abolished and replaced by earnings stripping rules.

These rules generally limit the deductibility of net interest expenses (interest expense in excess of interest income) to 30 percent of EBITDA for tax purposes. Unlike traditional thin capitalization or transfer pricing restrictions applicable in many European countries, this restriction applies to any kind of interest expense, irrespective of whether it is derived from intercompany financing or third-party debt. The rules apply to the net interest expense exceeding EUR3 million in the assessment period.

To assess whether the earning stripping rules result in a restriction on interest deductions, the EBITDA for tax purposes must be accurately modeled in each case. The German Generally Accepted Accounting Principles (GAAP) results need to be decreased by tax-free income, such as dividends, capital gains and exempt foreign-sourced profits, to determine the allowable amount of interest.

Any interest in excess of the 30 percent threshold is non-deductible. Excess interest may be carried forward to future tax years but is subject to change of control restrictions, which may lead to a (full or partial) forfeiture of interest carry forwards on a transfer of shares in the respective company (as further discussed under tax losses in the purchase of assets section earlier in this chapter).

Companies wishing to deduct more interest expense than allowed under these restrictions may be able to take advantage of the so-called escape clause. To qualify, the taxpayer must be able to demonstrate to the German tax authorities that the equity ratio (equity/balance sheet total) of the company is not more than 2 percent (increased from 1 percent by the Economic Growth Acceleration Act for 2010 and later assessment periods) lower than the equity ratio of the consolidated group of which the company is a member. In other words, debt-financing must not exceed that of the group as a whole. Specific rules apply to the calculation of the equity ratio for this purpose, and there is a restriction on the use of debt granted or secured by related parties from outside the consolidated group. The interest on such debt must not exceed 10 percent of the total net interest expense for each entity in the group.

Although the German tax authorities issued a decree in July 2008 on the application of the earnings stripping rules, the new rules are difficult to apply because it is not clear how to determine the correct consolidation level, the applicable accounting principles, or the equity ratio for tax purposes, taking into account certain adjustments and add-backs. Structuring a transaction with a borrowing ratio that leads to interest expenses in excess of the 30 percent EBITDA rule requires careful analysis of whether the conditions of the escape clause can be met.

Where the net interest expenses are subject to the 30 percent EBITDA threshold but less than 30 percent of the tax EBITDA, the unused tax EBITDA provides for an additional interest deduction in future years in which the net interest expenses exceed 30 percent of the current tax EBITDA. Such EBITDA carry forwards are limited to a period of 5 years and must be assessed separately. An EBITDA carry forward is not allowed in years in which an exemption from the earnings stripping rules applies. Taxable EBITDA is subject to full or pro rata forfeiture where the business of that company is transferred as a whole or in certain cases of group reorganizations according to the German Reorganization Tax Act. EBITDA carried forward is not forfeited on a detrimental change of control (i.e. a purchase of more than 25 percent of the shares in a company). Generally, the provision applies for business years ending after 31 December 2009.

For trade tax purposes, the deductibility of interest is further limited by an add-back of 25 percent of any deductible interest expense that exceeds EUR100,000 (together with certain other add-backs).

Withholding tax on debt and methods to reduce or eliminate it

Generally, interest payments to lenders are not subject to German WHT. However, non-resident lenders are subject to non-resident taxation in Germany where the debt provided is secured by, for example, land charges on German real estate owned by the borrower/ target group and no relief can be claimed under the relevant tax treaty. Where a lender fails to qualify for relief, all interest income is subject to corporate income tax in Germany at a rate of 15.825 percent (including solidarity surcharge).

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Checklist for debt funding

- Consider whether the level of taxable profits of the German entities would allow effective tax relief for interest payments and whether a tax deduction may be available at higher rates in other jurisdictions.
- Analyze the debt capacity of the German (target) entities based on projections of EBITDA for tax purposes. Explore the potential applicability of the so-called escape clause under the earnings stripping rules.
- Explore whether a debt pushdown should be completed by a tax group scheme (*Organschaft*) or by way of a merger or other measures.

Equity

An acquirer may use equity to fund the acquisition. German tax law imposes no capital or stamp duty.

However, Germany would levy 26.375 percent WHT (including solidarity surcharge) on dividends paid by a German company. The WHT may be avoided through the EU Parent-Subsidiary Directive or reduced under a tax treaty or domestic law provided applicable conditions are met, particularly the minimum participation, holding period and substance requirements. Dividend payments are not tax-deductible in Germany.

Although equity offers less flexibility should the parent subsequently wish to recover the funds it has injected, the use of equity may be more appropriate than debt in some situations, particularly where the target (group) is loss-making or the deductibility of interest expenses has already reached its limit under the earnings stripping rules. Therefore, a tax-efficient structure normally requires an appropriate mix of debt and equity so that the interest expense remains deductible under the earnings stripping rules. In addition, there may be non-tax reasons for using equity.

Reorganizations

The discussion thus far has focused on the purchase of an entire business for cash. Where only part of a business is targeted and the seller refuses to agree to an asset sale, the provisions of the new German reorganization law, discussed later in the chapter, may permit a hive-down of the targeted assets into a subsidiary, the shares of which can then be sold. Accordingly, where two businesses are to be combined, the merger provisions may permit the combination to be structured as a share-for-share exchange without triggering an immediate tax liability. Due to several anti-avoidance rules, a tax-exempt reorganization followed by a disposal of shares in the company involved may lead to adverse tax consequences if the disposal date is close to the reorganization date. The reorganization may become retroactively subject to tax as a result.

The German reorganization tax act was amended to facilitate cross-border reorganizations within the EU. These amendments were required following the SEVIC judgment of the Court of Justice of the EU, the Council Directive 2005/56/EC on cross-border mergers of limited liability companies, and the Merger Directive, which had until then been ignored by the German legislation. The new rules apply to all reorganizations registered with a commercial register after 12 December 2006.

The reorganization tax act now covers not only to reorganizations carried out under the German reorganization act but also to reorganizations in other EU jurisdictions that are comparable to reorganizations under German law. Transactions involving companies from non-EU and non-EEA countries usually still lead to immediate taxation of the transaction at both company and/or shareholder/partner level.

Generally, the reorganization tax act provides for all reorganizations to be carried out at fair market value, leading to the taxation of hidden reserves. Where Germany has the right to tax the transferred assets, reorganizations can only be effected at book value on written application. In such cases, an interim value (below fair market value) may be chosen in order to utilize existing tax losses carried forward, subject to the minimum taxation rules, by offsetting them against any profits on reorganization.

One of the most significant privileges of reorganizations under the reorganization tax act is that most reorganizations can be carried out with a retroactive effect of up to 8 months for tax purposes. For example, the legal procedures of the reorganization can be carried out up to 31 August 2014, if the effective date of the reorganization for tax purposes was 31 December 2013.

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Merger of a German corporation into a German partnership

A merger of a corporation into a partnership can be carried out at book value so that no gain is recorded at the level of the transferring corporation, but the German tax authorities retain their right to tax any hidden reserves in the assets of the transferring corporation.

At the shareholder level of the transferring corporation, different effects should be considered:

- Any tax-effective depreciation on the shares in the transferring corporation is reversed, leading to a taxable profit. Such profit is 95 percent tax-exempt for corporate shareholders and 40 percent tax-exempt (50 percent prior to 2009) for individual shareholders.
- Retained earnings of the transferring corporation are treated as deemed dividend distributions and taxed at the shareholder level. Such dividends are 95 percent tax-exempt for corporate shareholders. They are also subject to 26.375 percent WHT (including 5.5 percent solidarity surcharge), which is generally creditable by domestic shareholders.
- For tax purposes, the shares in the transferring corporation generally are deemed to be contributed to the partnership. The replacement of the shares in the transferring corporation with the assets of the corporation due to the merger may then lead to a profit or loss on merger. Transaction costs and the deemed dividend distribution also may be deducted when calculating the merger profit or loss. A merger profit is 95 percent tax-exempt at the level of a corporate partner in the assuming partnership, but any loss on takeover is not tax-deductible.

Since a partnership is transparent for German income tax purposes, Germany's right of taxation could be restricted on some mergers, for example, where the assuming partnership has non-resident partners that are only subject to a limited tax liability in Germany. Following the merger, any operating profit or capital gain is taxable at the level of the non-resident partner, so a tax treaty could restrict the right of taxation. However, in most cases, the right of taxation remains with Germany to the extent the business assets constitute a permanent establishment.

Tax losses, interest and EBITDA carried forward, as well as current-year losses, are not transferred to the receiving partnership. Thus, such losses may only be offset against any merger profit resulting from a transfer of the assets at fair market value or an interim value. Normally, the tax losses carried forward are not entirely used since the tax losses carried forward for corporate income tax and trade tax purposes usually differ. Moreover, the set-off of tax losses carried forward is further restricted by the minimum taxation rules. In addition, any interest carried forward resulting from the limitations of the earnings stripping rules is not transferred to the receiving entity.

Merger of a German corporation into another German corporation

A corporation can be merged into another by compensating the shareholder(s) of the transferring entity with new shares in the receiving entity or, in exceptional cases, without any compensation. A formal liquidation of the transferring entity is not required. On the merger, the transferring entity can increase the cost base of its assets, including self-created intellectual property. The increase in the cost base triggers taxable income at the level of the transferring entity and increases the depreciation base at the level of the receiving entity. In most cases, a merger gain (i.e. a gain resulting from an excess of the value of assets received over the shares held in the transferring entity) at the level of the receiving entity is tax-free. However, in the case of an upstream merger where a subsidiary merges into the parent company, the merger gain is only 95 percent tax-exempt. In all cases, a merger loss is not tax-deductible.

Any previous write-downs of shares in the transferring company must be reversed. Where these write-downs were tax-deductible (i.e. for write-downs prior to 2002), the reversal is subject to corporate income and trade taxes in full. Write-downs occurring after 2001 are not tax-deductible, so the reversal is 95 percent tax-exempt for corporate income and trade tax purposes.

Tax losses, interest and EBITDA carried forward (earnings stripping rules) by the transferring entity are forfeited on the merger (see merger of a German corporation into a German partnership).

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Contribution of assets into a German corporation in return for new shares

When the transferring entity receives new shares in the receiving entity, the following assets can be transferred to a German corporation under the German mergers and reorganizations tax act:

- assets and liabilities that constitute a branch of activity (*Betrieb* or *Teilbetrieb*), which can be categorized as such where they have a certain degree of independence and are potentially capable of functioning as an independent business
- an interest in a partnership
- a stake in a corporation.

Such a transfer is generally performed at fair market value, triggering a taxable gain or loss. However, the contribution of a branch or a partnership interest can be done at cost. This does not trigger additional tax costs where the following requirements are met:

- The contributed assets are subject to German corporate income tax at the level of the receiving entity.
- The liabilities contributed do not exceed the assets contributed.
- Germany's taxation rights on the contributed assets are not excluded or limited as a result of the contribution.

The contribution of a stake in a corporation may be effected tax-neutrally if the receiving entity owns the majority of the voting rights in the contributed corporation after the contribution. Any existing shareholding is included when considering this condition.

A tax-free contribution may be later subject to partial, retroactive taxation where, within 7 years following the contribution, either the shares granted in exchange for the contributed assets or the contributed shares themselves are sold. However, the sale of the contributed shares does not lead to retroactive taxation where the contributing entity is a corporation that could have disposed of the shares tax-free anyway.

The taxable gain is decreased pro rata by 1/7 for each year that elapses from the time of the contribution to the time of the sale. The taxpayer must demonstrate to the tax authorities by 31 May of each year that the shares were not sold during the past year. A failure to provide such evidence to the tax authorities in good time leads to a deemed share transfer and retroactive taxation on a pro rata basis.

Demerger

In addition to the aforementioned contributions, a branch of activity, interest in a partnership or a 100 percent stake in a corporation can be contributed in return for new shares in the transferee or, in exceptional cases, without any compensation. The main differences between this and the previously discussed contribution are that new shares can be granted to the shareholder of the transferring entity and that this scheme is solely applicable to corporations. Generally, three models are possible:

- In a split-up, an entity transfers all of its assets and liabilities to two or more receiving entities, either pre-existing or created for this purpose. The transferring entity is dissolved without being liquidated, and the owners of the transferring entity take ownership interests in the receiving entities in return for their dissolved interests.
- In a split-off, an entity transfers part of its assets and liabilities to one or more receiving entities, either pre-existing or created for this purpose. The transferring entity is not dissolved. The owners of the transferring entity take shares in the receiving entity in return for surrendering their indirect ownership rights in the property transferred. Split-offs include transactions in which the owners of the transferring entity all receive pro rata ownership rights in the receiving entity (sometimes called spin-off). Split-offs also include transactions in which certain owners of the transferring entity surrender all or part of their interest in this entity in return for an increased interest in the receiving entity.
- In a hive-down, an entity transfers part of its assets and liabilities to one or more receiving entities, either pre-existing or created for this purpose, and in return takes ownership rights in the receiving entities.

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These types of transaction are generally carried out at fair market value but can also be achieved tax-free subject to certain conditions. For split-offs, both the assets and liabilities retained and those transferred must constitute self-contained businesses, interests in trading partnerships, or 100 percent ownership of corporations to ensure that the split-off is performed tax-neutrally at book value. The split-off of other assets must be carried out at fair market value, leading to a capital gain. For split-ups and hive-downs, the same applies to the assets transferred. However, where shares in a corporation are being hived-down into another corporation, it is enough that the receiving corporation holds a majority of the first corporation's voting shares after the reorganization (see contribution of assets into a German corporation in return for new shares).

Complete continuity of ownership between the transferring corporation and the receiving entity (i.e. no separation of shareholder groups) is a condition of tax-free treatment in split-offs and split-ups, unless the shareholders in the transferring corporation have held their shares for at least 5 years. However, it is not necessary for all shareholders of the transferring corporation to take pro rata ownership interests in the receiving entity. The interest retained in the transferring entity can be reduced in return for an increased interest in the receiving entity and vice versa. Unanimous shareholder approval is required.

Where, within 5 years of a split-up or split-off, interests in the entities representing more than 20 percent of the value of the original interests in the transferring entity are conveyed to third parties, the entire reorganization is retroactively subject to tax.

Where a corporation is divided by a split-up, all loss carry forwards are forfeited. In a split-off, tax losses carried forward are not transferred to the receiving entities and some existing tax losses are forfeited.

Contribution of assets into a German partnership

Under German reorganization tax law, all the shares in a corporation, self-contained businesses or interest in a partnership can be contributed tax-free, provided Germany's taxation right in relation to these assets is not removed or limited. While the contribution of shares into a corporation can be tax-neutral provided the receiving entity owns the majority of the voting shares following the contribution, the contribution of shares into a partnership is eligible for tax-neutral treatment under this regime only if all the shares are transferred. However, a transfer of single assets (including individual non-qualifying shares in a corporation) between two businesses owned by the same taxpayer or the attribution of assets to a partnership for tax purposes (*Sonderbetriebsvermögen*) is possible according to the Income Tax Act, section 6 (5). According to German tax law, a transfer of shares by a partner to the partnership of which they are a member is also possible at tax book values. Other than the reorganization schemes described earlier, such a transaction is ineligible for retroactive application.

Change of legal form

The German reorganization act and reorganization tax act allow for the conversion of a corporation into a partnership and vice versa. From a tax perspective, the conversion of a corporation into a partnership triggers the same tax consequences as the merger of a corporation into a partnership, as described earlier. The conversion of a partnership into a corporation is treated as a contribution of a branch of activity into a corporation in return for new shares, as noted earlier.

Hybrids

Consideration may be given to hybrid financing – that is, using instruments treated as equity for tax purposes for one party and as debt (giving rise to tax-deductible interest) for the other. Various hybrid instruments and structures were devised to achieve an interest deduction for the borrower with no income inclusion for the lender. However, legislative changes made in 2013 deny the tax-effectiveness of certain double dip structures, particularly hybrid financing structures.

Discounted securities

The tax treatment of securities issued at a discount to third parties normally follows the accounting treatment. As a result, the issuer should be able to obtain a tax deduction for the discount accruing over the life of the security. An advantage of discounted securities is that discount, unlike interest, does not give rise to WHT.

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Deferred settlement

An acquisition often involves an element of deferred consideration, the amount of which is based on the business's post-acquisition performance and can only be determined at a later date. Under German tax law, the right to receive an unknown future amount is not regarded as an asset that must be valued upfront for German tax purposes. Instead, any consideration is treated as a retroactive adjustment of the initial consideration paid, and the tax calculation of both seller and buyer is amended retroactively for the deferred consideration received.

Other considerations

Concerns of the seller

The tax position of the seller can be expected to significantly influence any transaction. Due to differences in the tax treatment of assets and share sales, owners of corporate target entities generally are less inclined to sell the entity's assets than its shares.

Asset deal

The taxation of capital gains depends on the legal form of the seller and the type of asset disposed.

Where the seller is an individual who sells their whole business, the capital gain may be subject to a favorable tax regime. For a corporation, capital gains are generally fully taxable; however, where the business assets include shares, the 95 percent participation exemption applies on the sale of the shares.

The new provisions on the transfer of contingent losses allow the seller to realize built-in losses subject to certain limitations. While immediate deduction of realized built-in losses is allowed on the transfer of an entire business or partnership interest, built-in losses that are realized due to the transfer of a liability in other cases generally may not be fully deducted in the year of transfer but must be spread over a period of 15 years.

Disposal of a partnership

The taxation of a capital gain incurred on the disposal of a partnership interest depends on the type of partner concerned, that is, whether the partner is an individual or a corporate entity and, in the case of a disposal by an individual, whether their interest is sold fully or partly.

Where a partner sells their whole interest in the partnership, any capital gain is not subject to trade tax if the seller is an individual. Additionally, an individual can apply for the same tax relief as described earlier with respect to the transfer of the total business by means of an asset deal. If only part of the partnership share is sold, trade tax becomes due. In addition, none of the tax reliefs granted on the disposal of the whole interest are usually available when disposing of part of an interest (i.e. neither the limited tax exemption nor the reduced average tax rate apply).

For a corporate partner, the capital gain is subject to corporate income tax and trade tax, irrespective of whether the participation is sold in whole or in part.

For corporate members, the part of the capital gain attributable to interests in shares held by the partnership is taxed in the same way as if the shares were held directly by the seller (see next section).

Disposal of shares

Since 2002, German taxpayers have enjoyed certain tax exemptions on capital gains realized on the sale of shares in a corporation:

- Sellers who are resident or non-resident individuals can exclude 40 percent (50 percent pre-2009) of the gain realized for income tax purposes and, if applicable, for trade tax purposes (40 percent exemption).
- Individual sellers holding less than 1 percent of the shares in the company as private property are subject to a flat tax rate of 25 percent plus solidarity surcharge.
- Resident and non-resident corporate sellers can generally exclude their entire gains for corporate income and trade tax purposes (100 percent exemption). The same applies where the shares are held by a German branch of a foreign company or a German partnership with a corporate partner.

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Generally, a minimum interest, holding period, or tax treaty protection is not required to qualify for these exemptions. However, within a seven-year holding period following a tax-free reorganization, a sale may have adverse tax consequences under German reorganization tax law (see earlier in the chapter). Banks and other financial institutions that sell stocks held for short-term trading purposes cannot benefit from the capital gains exemptions because receipts are considered trading income. Recent developments suggest this short-term trading rule may also apply to non-financial institutions.

As of 2004, 5 percent of the capital gain is deemed to be a non-deductible business expense for corporate sellers, thus effectively reducing the 100 percent exemption to a 95 percent exemption. While current expenses, such as financing costs, are tax-deductible, expenses incurred on the sale of shares reduce the amount of the capital gain, so they are only 5 percent tax-deductible.

The capital gains tax exemption does not apply to the disposal of shares held by life and health insurance companies.

Company law and accounting

Under German commercial law, International Financial Reporting Standards (IFRS) can be substituted for German GAAP as reporting standards for listed and non-listed companies. However, German GAAP are mandatory for statutory financial statements, particularly as the basis for the distribution of dividends, for insolvency law, and for tax reasons. German reorganization law is mainly laid out in the so-called *Umwandlungsgesetz* (UmwG), which sets out the rules for commercial law and the accounting treatment for mergers (*Verschmelzungen*) as well as demergers (spin-offs, split-offs, carve-outs) and conversions.

As for M&A transactions, a business combination (which, under IFRS, is defined as the bringing together of separate entities or businesses into one reporting entity) may be categorized as either a merger or an acquisition. In essence, a combination is regarded as a merger where it effects a pooling of business interests (i.e. where one company's equity is exchanged for equity in another company) or where shares in a newly incorporated company are issued to the merging companies' shareholders in exchange for the equity, with both sides receiving little or no consideration in the form of cash or other assets.

German company law and accounting standards allow for various M&A methods. Generally, for mergers, companies have the choice of keeping current book values or changing to fair values according to German reorganization law in their statutory financial statements. Acquisitions are accounted for based on the contribution made in exchange for economic control over the company or over assets and liabilities that constitute a branch of activity. In contrast to German GAAP, merger accounting is not allowed under IFRS; all business combinations must be accounted for as acquisitions.

One of the main practical distinctions between acquisition accounting and merger accounting is that acquisition accounting may give rise to goodwill. The net assets acquired are brought onto the consolidated (share deal) or statutory (asset deal) balance sheet at their fair values, and goodwill arises to the extent that the consideration paid exceeds the sum of these values. Under IFRS, goodwill is not amortized over its useful economic life (impairment-only approach). Under German GAAP, goodwill in the consolidated financial statements is amortized on a systematic basis over its estimated useful life. For practical reasons, a useful life of 15 years, as defined by German tax law, is usually applied to amortize goodwill in both statutory financial statements under German GAAP and the tax balance sheets. Acquisition accounting principles also apply to purchases of trade and assets, with any goodwill and fair value adjustments appearing on the acquirer's own balance sheet. In merger accounting, goodwill does not arise. Any remaining difference is treated as a capital contribution or as a merger gain or loss, depending on the shareholder resolution.

Another important feature of German company law concerns the ability to pay dividends. Distributions of profit may be made only out of a company's distributable equity under German GAAP (e.g. retained earnings or available capital reserves). Thus, for groups, the distributable equity reserves must be determined by aggregating the corresponding statutory German GAAP accounts of the holding company and its subsidiaries separately, rather than by simply looking at the equity reserves of the group at consolidated level. Regardless of whether acquisition or merger accounting is adopted in the group accounts, the distribution of pre-acquisition profits of the acquired company may be restricted.

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Additionally, distributions recorded in the company's accounts must meet certain legal capital maintenance rules. Violation of these rules triggers a personal liability for management and shareholders. In particular, these rules may need to be applied where simple upstream loans are made to the parent company instead of dividend payments. Previously, the scope of these rules was much wider. Even now, it remains important that upstream loans are not impaired at grant date and that management continuously monitors the credit-worthiness of the borrower. Share capital increases, particularly payments in kind rather than cash, must also meet legal requirements for capital maintenance. Otherwise, the management and shareholders may become personally liable.

Germany generally imposes no government controls or restrictions on investments in assets and business entities or on capital movements into or out of Germany. However, the foreign trade regulations (*Außenwirtschaftsverordnung*) require reporting certain flows of capital for statistical purposes. The foreign trade act (*Außenwirtschaftsgesetz*) empowers the government to restrict the acquisition of interests in German companies and real estate by foreign persons. Currently, no such restrictions are in force, and there is no reason to expect that they will be imposed in the foreseeable future.

Germany has anti-trust legislation to safeguard free competition. M&A transactions above a certain size (essentially, involving companies or corporate groups with a joint worldwide turnover exceeding EUR500 million) and including at least one German entity with a turnover exceeding EUR25 million must be registered with the federal cartel authority and can be prohibited by this authority if considered to be detrimental to competition. EU anti-trust laws may pre-empt German anti-trust laws or add to them, depending on the transaction.

When planning an M&A transaction, labor law considerations should be taken into account. Under a provision in force in one form or another throughout the EU, the purchaser of a business automatically takes over all employment contracts associated with it. It makes no difference in this respect whether shares or assets are purchased, although difficult questions arise when not all assets of a business are acquired, such as the acquisition of one of several business divisions (branches of activity). Continuation of the employment contracts does not in itself prevent immediate downsizing following the acquisition, but this must be conducted in accordance with general German labor law legislation, which, compared with that of many countries, favors employees.

Further, Germany has an employee codetermination system for virtually all businesses. The system has several variants, The simplest variant, which involves election by employees, is the works council (*Betriebsrat*). The works council has a variety of rights to be informed and to be heard on personnel and other intracompany matters, along with codetermination rights (where their consent is required).

Employees must comprise one-third of supervisory board members at companies with 500 or more employees. Limited liability companies exceeding the threshold of 500 employees must establish a supervisory board if they do not already have one according to their articles of association. Advocates of this system regard it as at least partially responsible for the traditionally good German management-labor relations and relatively low level of strike activity. Foreign owners unfamiliar with supervisory boards sometimes consider this practice to be unusual.

Group relief/consolidation

Generally, each entity is taxed on a standalone basis, unless the entities constitute a consolidated tax group. Entities that are part of such a consolidated group are taxed together as a single body (*Organschaft*).

There are three types of tax-consolidation in Germany: VAT-consolidation, trade tax-consolidation and corporate income tax-consolidation. In all three cases, group members (controlled entities) are consolidated under a group leader (controlling entity). All types of consolidation require the financial integration of the group members.

Financial integration requires at least a direct or indirect majority of the voting rights of the controlling entity in the controlled company.

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Only European stock corporations (*societas Europaea*), stock corporations, partnerships limited by shares and, subject to certain requirements, other corporations (particularly GmbH) established in an EU/EEA Member State whose place of management and control is in Germany qualify as potential group subsidiaries. Due to the transparency of a partnership for corporate income tax purposes, the partnership's income is attributed to its partners and taxed in their hands. Therefore, for a partnership, corporate income is effectively consolidated.

Corporate income tax and trade tax consolidation require only the financial integration from the beginning of the fiscal year and a signed profit and loss pooling agreement between the group member and the group leader. This agreement is subject to various formal requirements and must actually be performed. Further, the agreement is enforceable by creditors (e.g. to force the group leader to transfer funds to a group member to cover its losses).

The group leader can be any person, corporation or partnership engaged in a commercial enterprise with a permanent establishment in Germany. However, the shares in the controlled subsidiary have to be allocated to the German permanent establishment for the tax group to be recognized.

Losses sustained by group members after the effective date of consolidation are attributed to the group leader for trade and corporation tax purposes. Pre-consolidation corporate income tax losses and, since 2004, trade tax losses are not affected by the consolidation and remain within the particular group member for use after the tax consolidation is terminated (e.g. by termination of the profit and loss assumption agreement).

For VAT purposes, consolidation requires the financial, organizational and economic integration of the group members into the group leader:

- Organizational integration requires the controlling entity to be able to assert management influence on a group member (e.g. where the same persons manage both companies or the group member contractually yields management authority to the group leader).
- Economic integration requires a substantial economic relationship between the activities of the group members and the group leader, ideally such that the group member functions economically like a branch of the group leader. This is often the most difficult of the three requirements to meet, especially where the intended group leader is a pure holding company.

For VAT purposes, the tax consolidation automatically becomes effective when these requirements are met.

Transfer pricing

Where an intercompany balance arises between the purchaser and the target after the acquisition, failure to charge interest on the balance may give rise to transfer pricing problems in the relevant jurisdiction. For example, where the balance is owed to the target, the tax authorities could impute interest on the balance if interest is not charged at an arm's length rate. Failure to charge fees, such as for cross-guarantees provided where the German target is the guarantor, may give rise to transfer pricing adjustments.

Dual residency

There may be advantages in seeking to establish a dual resident company, such as by benefitting from rules that are not followed in other jurisdictions (e.g. special business expenses in the case of partnerships).

Foreign investments of a local target company

The controlled foreign company (CFC) anti-avoidance legislation is designed to prevent German companies from accumulating profits offshore in low-tax countries. Unless the offshore lower-tier company is carrying out certain acceptable activities or meets other specific conditions, its profits are apportioned and allocated to the German parent company and are subject to German tax.

Therefore, the structure of the potential target should be reviewed for CFC risks in advance.

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Comparison of asset and share purchases

Advantages of asset purchases

- Direct allocation of the transaction financing to the acquired assets.
- Step-up to a higher depreciation base and goodwill amortization.
- Assumption of business-related liabilities only, although certain liabilities are unavoidable under the German Civil Code (BGB), section 613a, the German Commercial Code (HGB), section 25, and the General Tax Act (AO), section 75.
- Easy integration of profitable target operations into the loss-making company in the purchaser's group, permitting future offset of profits and losses.
- Selective acquisition of only those assets that are desired; debt-free acquisition of the business.

Disadvantages of asset purchases

- Approval of partners/shareholders possibly required.
- Legally more complicated due to the need to specify assets acquired, regulate delivery, arrange for continuation or renegotiate contractual relationships, etc.
- Possible difficulties in transferring certain pension obligations to the buyer.
- Need to renew licenses and permits associated with the business.
- Higher capital outlay if purchased debt-free.
- Potentially higher capital gains tax for the seller.
- Likely to be subject to VAT unless the whole business is transferred.
- Real estate transfer tax base may be higher.

Advantages of share purchases

- Greater legal simplicity; no need to assume contracts or re-apply for licenses and permits.
- Potential 95 percent capital gains tax exemption for the seller.
- Potential integration of target corporation into existing tax-consolidated group.
- For partnership interest, double dips may be possible. Also, step-up for tax purposes available.

Disadvantages of share purchases

- Target business in a corporation form (i.e. where the target is a form of tax-transparent partnership, an interest purchase generally is treated as an asset deal for tax purposes).
- Tax depreciation is unaffected by the value of the purchase price (unchanged historical asset depreciation values).
- Acquisition of all business-related liabilities.

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Germany – Withholding tax rates

This table sets out reduced WHT rates that may be available for various types of payments to non-residents under Germany's tax treaties. This table is based on information available up to 1 February 2014.

Source: *International Bureau of Fiscal Documentation, 2014*

	Dividends[1]		Interest[2] (%)	Royalties (%)
	Individuals, companies (%)	Qualifying companies[3] (%)		
Domestic rates				
Companies:	25	0	0/25	0/15
Individuals:	25	N/A	25	15
Treaty rates				
Treaty with:				
Albania	15	5	5[4]	5
Algeria	15	5[5]	10	10
Argentina	15	15	10/15[6,7]	15/–[8]
Armenia[9]	15	15	5	0
Australia	15	15	10	10
Austria	15	5	0	0
Azerbaijan	15	5[10]	10	5/10[11]
Bangladesh	15	15	10	10
Belarus	15	5[12]	5	3/5
Belgium	15	15	0/15[13]	0
Bolivia	10	10	15	15
Bosnia and Herzegovina[14]	15	15	0	10
Bulgaria	15	5	0/5	5
Canada	15	5	0/10[15]	0/10[16]
China (People's Rep.)[17]	10	10	10	7/10[18]
Croatia	15	5	0	0
Cyprus	15	5	0	0
Czech Republic	15	5	0	5
Denmark	15	5	0/25[19]	0

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	Dividends[1]		Interest[2] (%)	Royalties (%)
	Individuals, companies (%)	Qualifying companies[3] (%)		
Ecuador	15	15	10/15	15
Egypt	15	15	15	15/25[20]
Estonia	15	5	10	5/10
Finland	15	10	0	0/5[21]
France	15	5	0	0
Georgia	10	0/5[22]	0	0
Ghana	15	5	0/10	8
Greece	25	25	10	0
Hungary	15	5	0	0
Iceland	15	5	0	0
India	10	10	10	10
Indonesia	15	10	10	7.5/10/15[23]
Iran	20	15	15	10
Ireland	15	5	0	0
Israel	25	25	15	0/5
Italy	15	15	0/10	0/5
Ivory Coast	15	15	15	10
Jamaica	15	10	10/12.5	10
Japan	15	15	10	10
Kazakhstan	15	5	10	10
Kenya	15	15	15	15
Korea (Rep.)	15	5	10/25	2/10
Kosovo	15	15	0	10
Kuwait	15	5	0	10
Kyrgyzstan	15	5	5	10
Latvia	15	5	10	5/10
Liberia	15	10	10/20	10/20[24]
Liechtenstein	15	0/5	0	0[25]

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	Dividends[1]		Interest[2] (%)	Royalties (%)
	Individuals, companies (%)	Qualifying companies[3] (%)		
Lithuania	15	5	10	5/10
Luxembourg	15	5	0	5
Macedonia (FYR)	15	5	5	5
Malaysia	15	5	10	7
Malta	15	5	0	0
Mauritius	15	5	0	10
Mexico	15	5	0/5/10[26]	10
Moldova	15	15	5	0
Mongolia	10	5	10	10
Montenegro	15	15	0	10
Morocco	15	5	10	10
Namibia	15	10	0	10
Netherlands	15	10	0/15	0
New Zealand	15	15	10	10
Norway	15	0	0	0
Pakistan	15	10[27]	10/20	10
Philippines	15	10	10/15[28]	10/15
Poland	15	5	0/5	5
Portugal	15	15	10/15	10
Romania	15	5	0/3[29]	3
Russia	15	5[30]	0	0
Serbia	15	15	0	10
Singapore	15	5	8	8
Slovak Republic	15	5	0	5
Slovenia	15	5	5	5
South Africa	15	7.5	10/–[31]	0
Spain	15	5	0[32]	0
Sri Lanka	15	15	10	10

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	Dividends[1]		Interest[2] (%)	Royalties (%)
	Individuals, companies (%)	Qualifying companies[3] (%)		
Sweden	15	0	0	0
Switzerland	15	0[33]	0	0
Syria	10	5	10	12
Taiwan	10	10[34]	10[35]	10
Tajikistan	15	5	0	5
Thailand	20	15	0/10/25[36]	5/15
Trinidad and Tobago	20	10	10/15	0/10
Tunisia	15	10	10	10/15[37]
Turkey	15	5	10	10
Turkmenistan	15	15	5	0
Ukraine	10	5	2/5	0/5
United Arab Emirates[38]	10/15[39]	5	0	10
United Kingdom	15	10/5[40]	0	0
United States	15	0/5[41]	0	0
Uruguay	15	5	10	10
Uzbekistan	15	5	5	3/5
Venezuela	15	5[42]	5	5
Vietnam	15	5/10[43]	5	7.5/10[44]
Zambia	15	5	10	10
Zimbabwe	20	10	10	7.5

Notes:

1. The dividend rates apply, under a number of treaties, also to the income of silent (or sleeping) partners from their partnership share and to payments on jouissance rights that do not entitle the owner to participation in the liquidation surplus. Other treaties, however, provide for no restriction or, in exceptional cases, for another rate. The individual tax treaty should be consulted.
2. Many treaties provide for an exemption for certain types of interest, e.g. interest paid to the state, local authorities, the central bank, export credit institutions or in relation to sales on credit. Such exemptions are not considered in this column.
3. Unless stated otherwise, the reduced treaty rates given in this column generally apply if the recipient company holds directly or indirectly at least 25 percent of the capital or the voting power, as the case may be, of the company distributing dividends.
4. This treaty does not limit the taxation of profit-dependent interest, such as interest on profit-sharing bonds; thus, the domestic rate applies to such interest.
5. The rate applies if the recipient company owns at least 10 percent of the capital or the voting power in the German company, as the case may be.
6. The lower rate applies to interest payments in connection with the sale on credit of equipment.
7. The lower rate applies to interest paid to a bank; conditions may apply.
8. The domestic rate applies to copyright royalties, including films, unless the beneficial owner is the author or his heir, and to equipment rentals; there is no reduction under the treaty.
9. The treaty concluded between Germany and the former USSR.
10. The rate applies if the Azerbaijani company owns directly at least 25 percent of the capital with a value of at least EUR 150,000 in the German company.

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11. The higher rate applies to copyright royalties for literary and artistic works, including films, etc.
12. The rate applies if the Belarusian company holds at least 20 percent of the capital in the German company and the value of the holding is at least EUR 81,806.70.
13. The zero rate applies if the recipient is an enterprise; this does not apply to (a) interest on bonds and (b) interest paid by a company to a company owning at least 25 percent of the paying company's voting power or shares.
14. The treaty concluded between Germany and the former Yugoslavia. The treaty applies with respect to Bosnia and Herzegovina, Kosovo, Montenegro and Serbia. Germany and Montenegro signed an exchange of notes to continue the application of the Germany-former Yugoslavia, which entered into force on 31 March 2011. Germany and Kosovo signed an exchange of notes to continue the application of the Germany-former Yugoslavia, which entered into force on 10 June 2011.
15. The lower rate applies to interest on public bonds.
16. The lower rate applies to copyright royalties for literary and artistic works, excluding films, etc.
17. The treaty does not apply to Hong Kong and Macau.
18. The lower rate applies to equipment rentals.
19. The higher rate applies to profit-dependent interest, such as interest on profit-sharing bonds.
20. The higher rate applies to trademarks.
21. The lower rate applies to copyright royalties for literary, artistic and scientific works, including films, etc.
22. The zero rate applies if the Georgian company holds at least 50 percent of the capital in the German company and the value of the holding is more than EUR 3 million; the 5 percent rate applies if the Georgian company holds at least 10 percent of the capital of the German company and the value of the holding is more than EUR 100,000.
23. The 7.5 percent rate applies to fees for technical services. The 10 percent rate applies to equipment rentals and to know-how.
24. The higher rate applies to copyright royalties, excluding films, etc., and to trademarks.
25. The 5 percent rate applies if the recipient company directly owns at least 10 percent of the voting power in the German company. The zero rate applies if the recipient company has owned directly at least 10 percent of the voting power in the German company for an uninterrupted period of at least 12 months at the time when the dividends are paid.
26. The zero rate applies, inter alia, to interest paid by public bodies on public bonds. The 5 percent rate applies to interest paid to a bank; conditions may apply.
27. The rate applies if the recipient company owns at least 20 percent of the capital in the German company.
28. The 10 percent rate applies to interest payments in connection with the sale on credit of equipment, and to interest on bank loans and public bonds.
29. The lower rate applies if and as long as Germany under its domestic law does not levy withholding tax on interest paid to a resident of Romania.
30. The rate applies if the Russian company holds at least 10 percent of the capital in the German company and the value of the holding is at least EUR 81,806.70 (DEM 160,000). The minimum value of the holding is set at EUR 80,000 with effect from 1 January 2010 (protocol of 15 October 2007).
31. The 10 percent rate applies if the interest is subject to tax in South Africa. Otherwise, the domestic rate applies; there is no reduction under the treaty.
32. The treaty generally does not limit the taxation of profit-dependent interest, such as interest on profit-sharing bonds (i.e. the domestic rate applies to such interest). However, if the beneficial owner is a resident of Spain, the maximum rate of withholding tax is 15 percent.
33. The rate applies if the recipient company owned at least 10 percent of the capital in the German company for at least 12 consecutive months.
34. A 15 percent rate applies if the distributing company is a German real estate investment company that is tax exempt regarding all or part of its profits or that can deduct the distributions in determining its profits.
35. A 15 percent rate applies if the interest is the distributed income of a German real estate investment trust or a German real estate asset trust that is tax exempt regarding all or part of its profits or that can deduct the distributions in determining its profits.
36. The zero rate applies to interest on public bonds. The 10 percent rate applies to interest paid to a financial institution if the payer is engaged in an industrial undertaking as defined.
37. The lower rate applies to copyright royalties, excluding films, etc., and to know-how.
38. The treaty entered into force on 14 July 2011 and is retroactively applicable from 1 January 2009.
39. The rate is 15 percent, if the distributing company is a real estate investment company, that is tax exempt regarding all or parts of its profits or that can deduct the distributions in determining its profits.
40. The 10 percent rate applies if the beneficial owner is a pension scheme. The 5 percent rate applies if the recipient company holds directly at least 10 percent of the capital in the German company.
41. The zero rate applies if the corporate shareholder owns 80 percent or more of the voting stock of the US corporation for the 12-month period ending on the date on which entitlement to the dividend is determined and qualifies under certain provisions of the limitation on benefits article of the treaty. The 5 percent rate applies if the recipient company owns at least 10 percent of the voting power in the German company.
42. The rate applies if the recipient company owns at least 15 percent of the capital in the German company.
43. The lower rate applies if the Vietnamese company owns at least 70 percent of the share capital in the German company.
44. The lower rate applies to fees for technical services.

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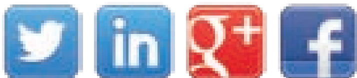
KPMG in Germany

Dr. Heide Gröger
KPMG AG
Wirtschaftsprüfungsgesellschaft
Klingelhöferstraße 18
Berlin 10785 Germany

T: +49 30 2068 4463
E: heidegroeger@kpmg.com

kpmg.com

kpmg.com/socialmedia



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