PKF
Accountants & business advisers

# PKF newsletter 02|18

## Editorial

Dear Readers,

We hope that 2018 has started well for you. This year is likely to bring huge changes in German tax law. For example, national regulations are currently being adapted to international requirements for the **documentation of transfer prices**. These requirements will as such be applicable even in cases where there are only few transactions with a closely related party in a foreign country. You can read more about this in our Focus section where we highlight, in particular, the extent to which there is a need for action because, inevitably, there will be conflicts with foreign authorities.

In Switzerland, sales tax is still called **value added tax** and, from a German legal perspective, in one way or another Swiss tax law provides surprises. This was reason enough for us to acquaint ourselves with the changes to **MWST** (as sales tax is abbreviated in Swiss German).

The two contributions that follow focus on the **'border crossings'** of **intangible assets** and warehouse goods. The final contribution in our Tax section makes a distinction according to which legal entities that are part of a **VAT group** may make a **variable compensatory payment** and those that ought not to do this.

The rights of customers and **employees** do not go as far as you might think. The first contribution in the 'Legal' section discusses the r**ights of customers in the case of PayPal payments**. "Six days you shall labour, but on the seventh day you shall **rest**" - in the second article you can read how the ECJ has breached this biblical principle.

We have adjusted the **layout** of the PKF Newsletter in order to provide you with current information in a more visible way and to enhance the readability of the PDF on electronic devices.

We hope that you will find the information in this edition to be interesting.

Your PKF Team

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# LATEST REPORTS

## Caution - there is a risk of profits being realised when a single asset is transferred to a commercial partnership

If a single asset, which does not constitute a branch of activity, is transferred to a commercial partnership in return for granting corporate rights then this is basically a transaction akin to an exchange and so profits are realised. According to the administrative opinion to-date, this also applied if the transaction was recorded under a capital account that did not convey any rights pertaining to the company. However, according to the more recent opinions of the Federal Fiscal Court and the Federal Ministry of Finance, recording transactions exclusively under other capital accounts (individual capital accounts, or joint specific-purpose reserve accounts) would lead to the presumption that the transaction was for no chargeable consideration and the contribution would be judged to be profit neutral. The tax authorities want the application of this viewpoint to be obligatory retroactively as of 1.1.2017. Therefore, prior to transferring an asset you should always consider very carefully under which account the transaction should be recorded in order to avoid unwanted tax charges.

## Will there be simplified VAT rules for online retailers as of 2018 already?

According to a proposed EU directive on the modernisation of VAT, from 1.12.2016, the settlement of VAT for the digital business between companies and consumers should be simplified significantly. In the case of services supplied electronically, the tax rules of the home country could simply be applied up to an amount of € 10,000 annually. Furthermore, simplified rules for assessing the residency of customers would apply up to a threshold amount of € 10,000 per year. Moreover, the invoicing rules of the home country only would be valid. It would no longer be the case, as previously, that the invoicing rules of the respective recipient states would be applicable. According to the EU Commission, these thresholds should be applicable from 2018 already.

As of 2021, there should then be a standardised portal for the VAT payable on online sales - the so-called 'One Stop Shop' (OSS). Therefore, for online mail order, only a quarterly tax return for the entire EU would have to be submitted in the member state where the retailer is based.

Please note: In order to be implemented the proposed directive still has to be passed unanimously by all the member states and, moreover, the EU Parliament has to be consulted. We will provide regular updates on the progress and the actual implementation.

# FOCUS

## National requirements in the area of transfer pricing documentation - Currently pending implementation obligations

**The OECD's BEPS (Base Erosion and Profit Shifting) action plan comprises comprehensive measures to combat the tax planning strategies used by multinational groups to erode and shift profits.**

**With the first BEPS Transposition Act, at the end of 2016, the German government brought the existing transfer pricing documentation requirements in line with those of the OECD. In the middle of 2017, the Ordinance on the Nature, Content and Extent of German Transfer Pricing Documentation Requirements (Gewinnabgrenzungsaufzeichnungsverordnung, GAufzV) was revised. In the following section we give an overview of the most important rules in order to demonstrate, subsequently, the consequences for everyday practice in companies.**

**1. General transfer pricing requirements**

The following basic principles were revised in the GAufzV for all taxpayers with cross-border situations.

**(1)** Documentation shall be required not only for relationships under civil law but also for business transactions, with respect to their economic perspectives, where no exchange of services occurs (e.g. agreements relating to the transfer of employees).

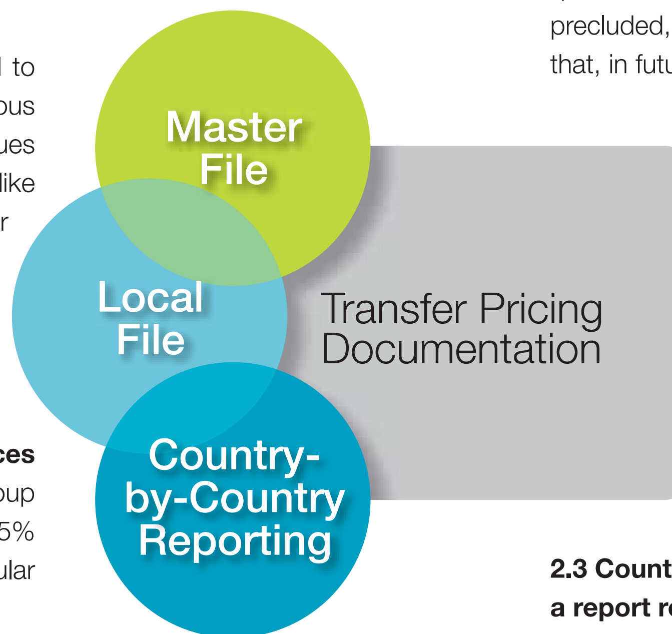
**(2)** The date when the transfer prices were determined has to be shown together with the information sources that were used on this date.
**(3)** If databases have been used then the strategies and criteria for the search as well as the process and result of the search have to be disclosed in such a way so that they are still verifiable at the time of the external audit.

### 2. Three-tier documentation process

For enterprises that exceed certain thresholds, the requirements described under point 1 shall be supplemented in the form of a three-tier classification of the transfer pricing documentation.

### 2.1 Master File - documentation of master data

A parent company shall be obliged to prepare a Master File if, in the previous year, an enterprise generated revenues of more than € 100m. We would like to highlight the following particular reporting requirements:
**(1) Supply chains** - A description is necessary for the five products or services with the highest sales revenues.
**(2) Individual products and services** – A description is essential if a group of companies generates more than 5% of the sales revenue with a particular product or service.
**(3) Functional and risk analyses** – A description of the main contributions that are made by individual enterprises to the value creation in the group of companies. The requirement is specifically for documentation, in the form of a recapitulative functional analysis, of the key functions that are exercised, the significant risks that are assumed and the assets that are used.
**(4) Intangible assets** – Description of the overall policy of the group of companies with respect to intangible assets (development, ownership, protection and utilisation), including a list of the locations of the most important R&D facilities and of the R&D management. Moreover, there has to be a description of the transfer pricing policy of the group of companies with respect to R&D as well as intangible assets.
**(5) Corporate financing** – A description of how the group of companies is financed (incl. financing relationships with unrelated third parties). This also includes information about the companies in the group that exercise central cash management or asset management functions as well as a general description of the transfer pricing policy of the group of companies with respect to the financing relationships within this group of companies.




### 2.2 Local File – Country-related and company-related documentation

In the second tier, the **Local File** constitutes country-specific and company-specific documentation. This has to be prepared if cross-border business relationships with closely related parties are worth more than **€ 6m** in the case of supplies and **€ 600,000** in the case of services. The Local File method makes a distinction between the documentation of the facts and the appropriateness. In this case, the date when the transfer prices were determined also has to be shown. In the transposition into national law, the German tax authorities are lagging behind the OECD's recommendations. However, these would be relevant for the documentation for a foreign tax authority:

- Only local comparative data
- Updates of database analyses every three years
- Preparation up to submission of the tax return
- Setting of prices at the time of the transaction
- Reconciliation to the amounts in the annual financial statements

» **Please note:** Even though subsequent transfer price adjustments are not precluded, it is nevertheless expected that, in future, the tax authorities will be sceptical towards subsequent price adjustments and will insist more strongly on ex-ante pricing (price setting approach). By the same token, in the present approach, appropriate ex-ante decisions will not be reviewed ex-post (outcome testing approach).

### 2.3 Country-by-Country Report as a report related to countries

Country-by-country reporting – or CbCR, in this respect see Section 138a of the German Fiscal Code (Abgabenordnung, AO) amended version - obliges groups with consolidated turnover, in the preceding financial year, of at least **€ 750 m** to prepare an overview of financial and tax data. The core of the CbCR consists of various country-related indicators and company-related business activities. In the PKF Newsletter 7-8/2016, we reported in detail on the contents that have to be documented in the three sections. In this

case, information will be automatically exchanged between the tax authorities of countries that have signed international agreements on the exchange of information. The aim of the CbCR is to enable tax authorities to make a preliminary assessment of tax transfer pricing risks and other tax risks with respect to the shifting and erosion of profits. The data are certainly not intended to be used as proof of the inappropriateness of transfer prices.

**Please note:** Furthermore, both the German government as well as the OECD have stressed that the information should not be used for a formulaic apportionment of global profits. Nevertheless, it remains to be seen what the foreign tax authorities will do with the information that is made available to them.

### 3. Submission deadlines

The existing submission deadlines will remain unchanged (60 days when requested by the tax authorities, 30 days in the event of exceptional business transactions). In this regard, the German provisions do not therefore follow the OECD's recommendation under which the Local File documentation should be prepared by the date of the submission of the tax return for the respective company and the Master File by the date of the submission of the tax return for the group parent company.

### 4. Impact on tax compliance

It is necessary to ensure that the information in the transfer price documentation and, ultimately, also in the tax return is complete and correct. This will require internal company processes that will be able to realise such results with reasonable probability and provide notification to the persons responsible for the documentation.

In a commentary on Section 2(3) of the new GAufzV, the Federal Ministry of Finance (Bundesministerium der Finanzen, BMF) stressed that transfer pricing guidelines constitute an important element of an internal control system in the area of transfer pricing and, in this respect, referred to the Administrative Regulations Governing the Application of the German Fiscal Code (Anwendungserlass zur Abgabenordnung, AEAO) in respect of Section 153. Moreover, such guidelines simplify the documentation of transfer prices.

The realignment of a tax compliance system should also include the date of the price setting as well as the necessity to implement systems that, if applied in conformity with the rules, could be expected to produce results that comply with the arm's length principle at transactional level. In practice, this requires coordinated transfer pricing documentation (head office and foreign corporations) as the new provisions will increasingly have an impact across disciplines and borders.

### 5. Effects on German enterprises

From the perspective of enterprises based in Germany, the measures in the BEPS project could result in foreign tax authorities having an interest in the tax substrate. In the future, double taxation risks will increasingly arise if countries with high numbers of employees and a low value of work demand a greater share of taxes.

*WP/StB Daniel Scheffbuch*

TAX

## Changes to the Swiss VAT legislation as of 2018 – New requirements for German companies, too

**For who:** German companies that provide services in Switzerland or for Swiss customers.

**Issue:** Up to now, within the scope of value added tax, the so-called receiver location principle applied in cases where German companies provided miscellaneous services to Swiss companies. According to this principle, the payment of Swiss value added tax (which is abbreviated there, in German, to MWST) is covered by what the Swiss call Bezugsteuer, this literally means 'acquisition tax' but is broadly equivalent to the reverse charge mechanism. There were exceptions, for example, for services in connection with real estate and in the case of construction work services as well as for academic and teaching activities for which Swiss VAT had to be charged at the place where the service was actually performed.

Up to now, registering for VAT purposes in Switzerland was only required once the level of revenues in Switzerland went above CHF 100,000 per year. As of 1.1.2018, this regulation will be significantly tightened. If such services are provided in Switzerland (place of supply principle) they will already be subject to Swiss VAT if the worldwide revenues of the German company exceed CHF 100,000 per year. By the same token, as of 1.1.2018, the standard rate of VAT in Switzerland will be reduced from 8% to 7.7%.

The tax liability means that German companies will have to register themselves for VAT with the Swiss

**Taxation in Switzerland with new requirements for German companies, too**

tax authority (ESTV), without being requested to so, within 30 days after the commencement of their tax liability. Furthermore, a tax representative has to be appointed in Switzerland (e.g. a Swiss accountancy firm) and a security deposit of at least CHF 2,000 has to be provided.

For services classified under the Swiss VAT Act as so-called “8.1-Services” (such as, e.g. IT services, consultancy services, etc.), from the Swiss perspective, the receiver location principle will still be relevant. The Swiss recipient has to settle the Swiss Bezugsteuer for these services. If solely these types of services are provided, then the German company will be exempted from the requirement to register for VAT in Switzerland.

» **Recommendation:** German companies that provide services to Swiss companies should acquaint themselves with the VAT (registration) requirements. We would be pleased to provide you with support in this respect and/or, through our PKF network, put you in touch with a Swiss tax expert who, if required, would able to act as a tax representative.

*StB Steffen Schmid*

## Tax deduction for the cross-border provision of software

» **Who for:** Businesses in Germany that use the software and databases of foreign providers.

» **Issue:** The Federal Ministry of Finance (Bundesministerium der Finanzen, BMF) published a circular, on 27.10.2017, about limited tax liability and tax deduction in the case of the cross-border provision of software. According to this, foreign providers are subject to a limited tax liability only if the domestic (German) user has been granted comprehensive rights to use the software and/or the database for commercial exploitation (in particular, rights to reproduce, to edit, to distribute or to publish).

However, the intended use, in terms of the functional use of the software or database (access, read and print functions), does not provide grounds for limited tax liability. The intended and functional use of the software also includes any necessary adjustment and reproduction operations, which would not lead to commercial exploitation as, under copyright law, these are not subject to the permission of the rights holder. The same applies if only the results of the functional use of the software program can be used commercially (e.g. the sale of a calendar that was designed with the help of an image-processing program).

If by providing software across a border the foreign provider is subject to a limited tax liability then the domestic (German) business is obliged to deduct tax in accordance with Section 50a of the German Income Tax Act (Einkommenssteuergesetz, EStG).

» **Please note:** The above-mentioned BMF circular should be applied to all open cases. As the tax deduction under Section 50a(1) no. 3 EStG is one for which you have to register, in cases that have already been registered it would be possible to file a correction (or, if applicable, a nil return), while taking limitation periods into consideration.

*StB Elena Müller*

## Supplies via consignment stock - Federal Ministry of Finance has confirmed the rulings of the Federal Fiscal Court

» **Who for:** Domestic (German) recipients of cross-border supplies of goods.

» **Issue:** The Federal Ministry of Finance *(Bundesministerium der Finanzen, BMF)*, in its circular, from 10.10.2017, concerning the treatment of supplies via consignment stock, accepted the decision of the Federal Fiscal Court (Bundesfinanzhof, BFH) and amended the VAT Application Decree accordingly. According to previous regulations (applicable at the latest on 31.12.2017), in the case of deliveries to the consignment stock in Germany, first of all, the foreign supplier had to declare a purchase from a foreign country. The subsequent deliveries from the stock were then considered a supply to the customer subject to VAT in Germany. The supplier had to register for VAT in Germany, file provisional/advance VAT returns and pay VAT. Exceptions were only possible if the store was a bonded warehouse.

Under the new regulations (to be applied in all open cases, at the latest, as of 1.1.2018) the following shall apply. If the domestic (German) customer is already known at the beginning of the transfer operation and if the goods are stored for just a short period in order to cover the production-related demand for goods needed by the customer for the next days and weeks, then the warehousing does not constitute an interruption in the transfer operation. Despite the interim storage, from the perspective of the foreign supplier, a VAT-exempt direct supply to its German customer is presumed. In such cases, the foreign suppliers are no longer required to register for VAT but the buyer has to declare a purchase from a foreign country.

The following scenarios fall under the new regulations:

**(1) Customer is known –** This is the case if a binding purchasing agreement has been concluded. If this agreement is only concluded once the goods have been warehoused because the customer is not obliged from the outset to accept the goods that the supplier has brought to the warehouse then an interruption in the movement of goods shall be deemed to have occurred.

**(2) Goods made to the customer's specifications** – The supplier makes the contractual item in accordance with the customer's special requirements. Nearly all cases of customer consignment stocks would fall under this.

**(3) Call-off stocks** – There can also be direct supplies in the case of the storage of call-off stocks. These can be distinguished from other types of storage in that only one particular customer is allowed to take goods out of the warehouse.

**(4) Short interim storage** – If there is temporal and material link between the supply and (onward) transport then a continuous delivery flow shall be deemed to exist and the storage shall be viewed as being of temporary duration and not detrimental from a tax point of view.

*StB Sabine Rössler*

## Minority interest holders in a VAT group – No variable compensatory payments

» **Who for:** VAT groups with minority shareholders

» **Issue:** Compensatory payments that a subsidiary company makes to a minority interest holder may not contain a variable portion that is calculated on the basis of the subsidiary's earnings and, essentially, places the minority interest holder in the same position as if it had no profit and loss transfer agreement. Otherwise, the condition of transferring the 'entire profits' to the parent company would not be satisfied. Consequently, (from a tax perspective) the profit transfer agreement would not be deemed to have been executed and the recognition of the VAT group would be at risk. This ensued from a recent Federal Fiscal Court (Bundesfinanzhof, BFH) ruling, from 10.5.2017, (case reference: I R 93/15, www.bundesfinanzhof.de) with which the Munich-based judges, responsible for ruling on financial issues, extended their previous opinion.

The background to this was that compensatory payments should provide a minority shareholder with appropriate compensation for the share of profits that have been passed up through the profit and loss transfer agreement. Under the German Sock Corporation Act, these include fixed compensatory payments (guaranteed dividends) and a variable compensation component oriented toward the earnings of the parent company. A German limited company (GmbH) as a subsidiary company is generally free to create its own compensatory payment arrangements.

In order for the profit and loss transfer agreement to be recognised for tax purposes, there is an evaluation, in advance, of the agreement concluded on compensatory payments. In its recent ruling, the BFH expressly emphasised that, for tax purposes, the transfer of the entire profit should be viewed as a separate condition for a valid profit and loss transfer agreement for both legal forms (limited company and stock corporation). If the agreement is not recognised for tax purposes then there is a risk that the profit transfer will be treated as a (hidden) profit distribution.

Compensatory payments to external holders of interests have to be taxed at the subsidiary company (itself) and do not generally put at risk the condition of transferring the entire profit. Moreover, the combination of a guaranteed dividend and a variable compensatory payment would not be detrimental from a tax point of view if the total compensatory payment remained below the dividend portion for an external holder of interests with no profit and loss transfer agreement. If, as a consequence of the compensatory payment, the subsidiary company's profit accrues to the external holder of interests in the same proportion that would have had to be distributed if there had been no VAT group with a profit and loss transfer agreement then, in the opinion of the BFH, the entire profit would not be transferred to the parent company because, in that case, the parent company would only receive a part of the profit. However, a variable compensation component oriented towards the earnings of the parent company would not be detrimental from a tax point of view.

» **More Information:** In 2010 already, the Federal Ministry of Finance ordered the non-application of a previous BFH ruling. A compensatory payment agreed in a way that is permissible under civil law should also be able to include variable or fixed components that are calculated on the basis of the subsidiary company's profits and exceed the possible share in the profits of a holder of interests. It is still open whether or not, in view of the recent ruling, the tax authorities will abandon their opinion.

*StB Sabine Rössler*

# LEGAL

## It is permissible for employees to work for 12 days without a day rest

» **Who for:** Employers and employees.

» **Issue:** According to a European working time directive, employers have to grant their employees at least one free day in every week. A Portuguese appeal court recently brought a suit before the ECJ and requested a preliminary ruling. In this case, the ECJ had to decide whether or not an employee could reasonably be expected to work occasionally for more than seven consecutive days. In the underlying case, this had been demanded of a former employee of a Portuguese casino.

**ECJ has derived the maximum number of days that can be worked at one stretch**

By way of a legal action against the casino, the former employee was now demanding compensation in the amount of the remuneration for the overtime that he had supposedly worked.

The above-mentioned regulation on working hours in the European Directive 2003/88 EC stipulates in Art. 5 that "per each seven-day period, every worker" shall be granted "a minimum uninterrupted rest period of 24 hours plus the eleven hours' daily rest." However, the employer was of the opinion that the working time directive only granted a rest day for each seven-day period and, however, it did not specify there when this rest day had to be granted. The ECJ shared this opinion and, in its judgement of 9.11.2017 (C-306/16), explained that Art. 5 of the EU Directive 2003/88 in no way stipulates further when the minimum rest period of 24 hours per each seven-day period plus the eleven hours should be granted.

The wording of Art. 5 of the Directive requires the Member States merely to ensure that a minimum rest period is available to each employee during a seven-day period without, however, specifying when that must be granted. In its judgement, the ECJ added that the seven-day period was a reference period. This is a set period within which a certain number of consecutive rest hours must be granted irrespective of when.

» **Recommendation:** Therefore, if the first rest day is taken at the beginning of the working week and the rest day for the subsequent working week at the end of it then this could result in a permitted working period of up to 12 consecutive working days without this constituting an infringement of the EU working time directive. We would be pleased to help you with the interpretation as well as the drafting of employment contract clauses.

*RA Frederic Schneider*

## The Federal Court of Justice has significantly limited the buyer protection in the PayPal payment system

**» Who for:** Sellers and buyers who use the PayPal payment service.

**» Issue:** With its so-called PayPal buyer protection policy, under its general terms of business, the online payment service PayPal provides a scheme that allows a buyer to request the reversal of a payment transaction if the buyer has not received an article or if it differs significantly from what was described. The Federal Court of Justice (Bundesgerichtshof, BGH) recently ruled on two cases where, after debits had been returned accordingly from their PayPal accounts, sellers had brought actions against the respective purchasers for renewed payment of the purchase price. In this respect, it was questionable if the purchase price claim had already lapsed when the seller's PayPal account had been credited for the first time. The BGH has now rejected this. According to the court's interpretation, when using the PayPal system there is a tacit agreement that in the event of a debit being returned to the purchaser's account the purchase price claim would once more apply. In the same way that instead of the PayPal buyer protection the normal warranty right is available to the purchaser, likewise, with an equitable interpretation, a seller should be entitled to claim the purchase price again.

Online retailing is keeping the courts busy

It has thus been clarified that the advertised PayPal buyer protection does not go so far that, after a refund, purchasers would already be on the safe side. The purchaser does indeed get his/her money back to begin with, however, the seller could claim his/her purchase price once again. Therefore, PayPal buyer protection does not constitute a type of 'insurance' - this is perhaps something that many consumers believe. Nevertheless, the buyer is protected to the extent that it remains a matter for the seller to bring a legal claim and the seller also bears the burden of proof.

**» More Information:** An informative press release (no. 187/2017) was published (in German) by the BAG on the two rulings from 22.11.2017 (case reference: VIII ZR 83/16 and VIII ZR 213/16) at www.bundesgerichtshof.de.

*RA/StB Frank Moormann*

## AND FINALLY...

"Less is more."

**Ludwig Mies van der Rohe,**
**Architect, 27.3.1886 – 17.8.1969**

**Impressum**

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