YPOG Briefing:

Obligation to report domestic tax arrangements pursuant to Sec. 138l et sqq. Tax Code according to the Draft "Growth Opportunities Act" (Wachstumschancen-gesetz)

Hamburg, 3 August 2023 | Stefan Richter and Daniel Rudi

As part of our series of briefings on the various amendments of tax laws (Global Minimum Tax Directive Implementation Act and Growth Opportunities Act) proposed by the German Federal Ministry of Finance this July, we present in this briefing the proposal for a reporting obligation for domestic tax arrangements pursuant to Sec. 138l et sqq. Tax Code Draft.

Obligation to report domestic tax arrangements

The current draft of the Growth Opportunities Act provides for the introduction of a reporting obligation for domestic tax arrangements pursuant to Sec. 138l et seq. Tax Code Draft. The following summary provides an overview of the planned introduction and highlights the implications for affected taxpayers.

1. Background

The Act on the Introduction of an Obligation to Report Cross-Border Tax Arrangements (Gesetz zur Einführung einer Pflicht zur Mitteilung grenzüberschreitender Steuergestaltungen) of 21 December 2019 and the associated implementation of the DAC6 Directive have already introduced an obligation to report cross-border tax arrangements (Sections 138d to 138k Tax Code). The law is applicable as of 1 July 2020. In the meantime, a reporting obligation for domestic tax structures was also envisaged in this legislative process, but was ultimately discarded.

After the coalition parties had already declared in the coalition agreement to extend the reporting obligation also to domestic tax arrangements, this has now been implemented with the draft of the Growth Opportunities Act.

According to the explanatory memorandum, the aim of the reporting obligation for domestic tax arrangements is to detect unintentional loopholes in the law earlier than before and to be able to react to them. In addition, the tax offices are to be put in a position to evaluate the information obtained from the reportings in support of the assessment and to promote the uniformity of taxation.

2. Reportable Arrangements

The rules on the reporting obligation on domestic tax arrangements are closely aligned with the legal provisions on the reporting obligation on cross-border tax arrangements. Domestic tax planning is understood to mean:

- Any arrangement that is not a cross-border tax arrangement (Sec. 138d para. 2 in conjunction with Sec. 138e Tax Code),
- which has as its object a tax on income or wealth, trade tax, inheritance or gift tax or real estate transfer tax,
- which has at least one characteristic within the meaning of Sec. 138l para. 3 Tax Code Draft, and
- from which a reasonable third party, taking into account all material circumstances, can reasonably expect that the main benefit is the obtaining of a tax advantage.

The characteristics of reportable domestic tax arrangements within the meaning of Sec. 138l para. 3 Tax Code Draft largely correspond to the characteristics of cross-border tax arrangements pursuant to Sec. 138e para. 1 Tax Code. These include, for example:

- Loss-making companies are acquired in order to utilise their losses,
- income in property, gifts or other non-taxed or lower-taxed income or revenue is converted, i.e. reclassified,
- circular transactions of assets or rights, where the assets concerned revert to the original user or taxpayer after a series of transactions.

However, new indicators have also been introduced, according to which a design subject to reporting may exist, subject to further conditions, if:

- The same tax-relevant facts are to be allocated several times to several users or other taxpayers or to one user or taxpayer. This is intended to capture legally unintentional multiple considerations that lead to a reduction of tax claims,
- tax-effective losses and wholly or partially tax-exempt income are generated by coordinated legal transactions for a specific purpose. This is intended to record coupling transactions in which tax-privileged profits are generated and combined with tax-effective losses,
- tax advantages in the area of tax deduction from capital gains are generated through inappropriate legal steps.

Pursuant to Sec. 138l para. 5 Tax Code Draft, a reporting obligation on domestic tax arrangements only exists if the user meets certain size criteria in at least two of the last three financial years preceding the calendar year in which the reportable event occurred. Specifically, these are either a turnover threshold of €50 million, a sum of positive income of more than €2 million or income pursuant to Sec. 8 para. Corporate Income Tax Act (KStG) of more than €2 million. An obligation exists irrespective of the size criteria in group cases, in the case of foreign control, in the case of an investment fund or special investment fund as well as in the case of certain investors in an investment fund. There is also a reporting obligation if assets of at least €4 million are the subject of a transfer relevant for inheritance or gift tax purposes, as well as in the case of direct or indirect acquisitions of real estate companies with a real estate value of at least €5 million.

3. Reporting Procederes and Sanctions

The intermediary or the user himself is subject to the reporting obligation if there is no intermediary or if he has designed the domestic tax arrangement for himself. The user is also obliged to report if personal information is involved and the intermediary is subject to a duty of confidentiality and has not been released from this duty.

The report of a domestic tax arrangement must be made to the Federal Central Tax Office (Bundeszentralamt für Steuern) within a period of two months after the end of the day in which the first of the following events occurs:

- The domestic tax design is made available for implementation,
- the user of the domestic tax arrangement is ready to implement it, or
- at least one user of the domestic tax design has taken the first step of implementing that tax design.

After receipt of the report, the Federal Central Tax Office assigns a registration and disclosure number to the reporting party, which must be stated in the tax return in which the tax advantage is to be reflected for the first time. In the event of a breach of the reporting obligation, fines of up to € 10,000 may be imposed.

4. Conclusion

In view of the low level of knowledge gained so far from the reporting obligation for cross-border tax arrangements despite the high level of bureaucratic effort, the extension to domestic tax arrangements should be viewed critically. If the draft bill is implemented, this will mean a considerable time and administrative effort for taxpayers and their tax advisors as well as bureaucratic effort for the tax administration. In addition, the expansion of the reporting obligations will lead to a high degree of legal uncertainty, as the criteria for the reporting obligation in particular are often only unclearly formulated and lead to questions and delimitation problems.

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