

Navigate through the credit crunch



As you adapt your business plans in the light of the current economic climate a review of your tax position and compliance process could generate significant cash tax benefits and cash repatriation opportunities.

Along with the improvement of cash positions of your business, tax strategies can also deliver earnings benefits – with VAT and employer tax strategies directly increasing pre-tax profit.

This brochure highlights 34 German ideas in the key areas Corporation Tax, Value Added Tax and Employer Tax.

Your Deloitte contact will be happy to discuss how these ideas can be applied in your organization.

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Corporation Tax

Manage your annual tax payments

1. Adjust prepayment amounts of current cash tax.

If the estimated statutory profits suggest that taxable income will decrease next year provide such forecast and a draft tax calculation to the tax office along with the application to lower the income tax prepayments.

You can also try to retroactively apply for an adjustment of previous year prepayments to obtain cash tax prior to filing the annual return for such year. Such application should also include a provisional balance sheet and a tax calculation.

2. File a tax return early to obtain tax credits early.

Tax credits e.g. domestic WHT from dividend distributions by a German subsidiary to domestic German shareholders can in various cases only be claimed through a tax return. Therefore, such cash tax requires to file the return early. In some case one might even consider to file the return early based on provisional statutory figures.

3. Tax prepayment deferral after restructuring.

If a corporation is merged into another (new) corporation, the surviving corporation does not need to make prepayments on the basis of its prior year income. This may create – unless the tax authorities assess special prepayments – a one-time prepayment deferral. The merged corporation may apply for a full reduction of its tax prepayments for the merger year.

Avoid unnecessary cash repatriation cost (21.1% domestic WHT)

4. Proactively obtain exemption certificates.

Only if an exemption certificate exists German authorities allow a company to directly benefit from treaty protection or from the EU Parent-Subsidiary-Directive through reduced WHT rate at source. Even if dividends are not anticipated exemption certificates can allow German companies to immediately benefit from treaty protection or the EC parent-subsidiary directive under certain circumstances: Under German tax laws various issues could give rise to deemed dividend distributions which require to withhold tax unless an exemption certificate exists. It should be taken into consideration that the process can consume considerable time (allow a minimum of two months).

5. German interest limitation may avoid WHT.

Under German tax rules generally, a certain EBITDA related amount of interest expense is deductible immediately. Any excess amount is deferred into future years. However, cash payments of interest which can effectively represent repatriations of profits are regularly not subject to withholding tax under domestic German tax rules. Various strategies exist to increase a German company's leverage which can allow to reach the desired interest expense levels.

These strategies might be extremely useful if the parent company does not pass the test of the German anti treaty shopping rules and applies a withholding tax of 21.1%.

6. Return equity instead of profits.

The return of equity may not be treated as dividends under German tax rules and does not require the payor company to withhold tax. The return of equity may require – amongst others – an assessment of (tax) equity amounts ("steuerliches Einlagekonto") by the tax authorities which is a standard part of the tax return assessment. Obviously, there can also be additional legal requirements which could require timely planning.

7. Relief from WHT outside Parent-Subsidiary-Directive.

ECJ decisions might allow claiming a relief from withholding tax on dividends to EC parent companies that do not qualify for the parent subsidiary directive, i.e. if the ownership is less than 15% [10% from Jan 1, 2009] equity ownership and/or the holding period is less than 12 months. The reasoning for such a claim would be built on the argument that in a pure German context there would be a 100% withholding tax relief for dividends to such parent companies

8. Buy back own shares (treasury stock).

In certain scenarios, a German company could consider to buy back own shares. The share price is paid in cash to its parent company and – if structured adequately – does not become subject to withholding tax.

9. Cross border EC merger.

If a German company is merged cross border into its EC parent company the German activities could give rise to a PE of the EC company. Any retained earnings of the transferred legal entity should not be subject to withholding tax. The merger could generally be effected at carry over basis.

Corporation Tax

Avoid Penalties

10. Avoid late filing penalties.

If timely filing of a tax return may not be accomplished you could consider filing a tax return based on provisional figures to avoid the assessment of late filing penalties.

11. Avoid interest charges.

If 15 months after the fiscal year end have expired but the final tax return can still not be submitted and additional tax payments are expected a voluntary tax prepayment avoids the assessment of interest charges of 6% p.a. which is not deductible.

In this context, it might also be worthwhile to take a conservative filing position for provisions that have been recognized in the statutory balance sheet. If the issues that gave rise to the provisions may require additional investigation the corresponding expense might not be deducted in the tax return in the first place but could help later if other adjustments could occur (even in a tax audit) to avoid the post deadline increase of cash tax liabilities which would give rise to interest penalties. If the result of the investigations allow to take the tax deductions these may offset other income adjustment and could therefore avoid additional interest charges.

Defer Income

12. Defer interest income.

Under German tax laws non-interest bearing payables with a term of more than one year need to be discounted which gives rise to income at the level of the debtor in the year of discount. This can be avoided if a minimal interest rate is agreed for such payables. This planning is most likely to be used in domestic scenarios because in a cross border context transfer pricing rules would require an arm's length interest rate right away. Often one can find non-interest bearing domestic payables if an Organschaft is established and the subsidiary's profits have not been paid in cash but were converted into loans.

13. Introduce a deviating fiscal year.

If non-tax reasons exist to change a fiscal year from calendar year to a deviating year end (e.g. adaptation of group standards) a cash tax deferral for the remainder of the calendar year is gained. Tax authority's consent is necessary

Monetise losses

14. Carry back losses into previous years.

Losses can be carried back one year for CIT purposes (not for local trade tax). The use of losses carried back is limited to 0.5m Euros. Any remaining loss balance can be carried forward for indefinite time but will only allow offsetting future income of 1m Euro plus 60% of the remaining positive income.

Carry back must be filed in the tax return of the year in which the loss occurred (tax return amendment).

15. Use losses through tax consolidation (Organschaft).

German tax law allows to offset losses of one group company against positive income of another group company. This requires a parent-subsiary structure where the parent company owns more than 50% of the subsidiary's shares (vote) at the beginning of the subsidiary's fiscal year and that certain legal steps are taken prior to year end (signing of pooling agreement, approval of the agreement by the shareholders, registration with the local court).

16. Use losses though receivables factoring.

If the legal ownership of the loss company and of the profitable company does not match the parent-subsiary scheme as required for Organschaft a receivables factoring plan with built-in discounts creates an expense for the profitable group member (seller) and income of the loss company (factor) upon collection of the full amount of the receivable.

17. Claim relief for losses of a German company's EC-PE.

Recent ECJ decisions may give rise to a filing position in the German income tax return that losses of a German company's PE that is located in the EC may be claimed if they are due to expire in the local country.

Prepay expenses/royalties

18. Prepayment of expenses/royalties.

IP rights, inventory or stock could be sold to the subsidiary in advance in order to receive an immediate cash in-flow (discount necessary, set up of an accrual).

Corporation Tax

Make interest expense tax effective

19. Increase interest deduction above 30% limit.

The new German tax rules disallow a taxpayer to deduct interest expense (net of interest income) over and above 1m Euros which exceeds 30% of tax adjusted EBITDA unless a special equity test is passed. This equity test can be very complex but also very beneficial for the German taxpayer. It basically compares the consolidated equity ratio of the parent company and the individual equity ratio of the German subsidiary. If the latter (equity ratio of the subsidiary) is higher a taxpayer may deduct all its interest expense and reduce its cash tax liability. Whether the test can be passed should be checked each year prior to the end of the fiscal year.

Boost distributable profits for repatriation

20. Create additional profits that can be repatriated.

If sufficient cash for distributions is available but insufficient book reserves or profits exist several corporate restructurings (mergers, hive-downs etc) can be carried out at fair market values for statutory purposes. These may give rise to profits which may be distributed. At the same time, the transfer could be treated at carry-over basis for tax purposes which avoids taxable gains from the transaction.

Value Added Tax

Maximise VAT recovery

21. Explore opportunities to claim foreign VAT earlier.

A number of jurisdictions allow the filing of VAT refund claims earlier than at the elapse of the year for which the refund claim is filed, i.e. in quarterly or half-year claims. Where considerable refund amounts are involved it might be worth to consider to file such earlier claims even if this creates some additional administration cost.

22. File compliant and complete VAT refund claims.

VAT refund authorities become more focused and scrutinized on formal requirements to be fulfilled to get such VAT refund application accepted. These range from the availability of original invoices containing input VAT to the signature of the claim by an authorized representative of the firm and to the availability of a valid and actual certificate of VAT residency. Incomplete applications result either in an immediate refusal or a significant delay of processing.

23. Increase VAT recovery on employee and travel expenses.

Explore the possibility and the formal requirements to be fulfilled as regards documentation for the VAT recovery on employee and travel expenses; make use of actual legislation in certain jurisdictions concerning the cap/statute of limitations periods for retrospective claims on under-recovered input VAT on these expenses (e.g. Conde Nast Claims in the UK).

24. Improve Bad Debt Relief efficiencies.

Collect sufficient back-up documentation to claim bad debt relief as early as possible.

VAT return management

25. Ensure timely and proper VAT return filing.

Timely and proper filing with early input VAT recovery and appropriate output VAT reporting shall avoid late filing and late payment penalties as well as interest charges.

26. Use data interrogation to ensure correct processing.

The use of data interrogation software as provided by Deloitte (ABACUS) and used by tax authorities (IDEA) helps to ensure to avoid double invoicing for the same supply (VAT overpayment) or double input VAT recovery (repayment obligation with interest),

27. VAT grouping or degrouping/Branch – HQ planning.

In countries where VAT grouping is not automatic (unlike Germany) consider to elect group companies into a VAT group to maximize cash-flow savings on intra-group charges or to de-group a company in case it has a negative impact on the overall input VAT recovery ratio due to its VAT exempt supplies. Combine VAT grouping with headquarter – branch service structures for VAT cash-flow saving on intra-group/intra-branch services

Invoicing and tax point planning

28. Request timely invoicing papers from vendors.

Consider to require explicit requests to vendors for timely invoicing and for proper and complete format of their invoicing in order to ensure input VAT recovery. Ensure timely processing of purchase invoices and where negotiable with tax authorities an input VAT recovery on the basis of input VAT estimates for a month in cases where invoices are on their way but not received yet.

29. Review self-billing arrangements.

Self-billing has the advantage that the invoice necessary for input VAT as a proof is in any case available at the service/goods recipient being the issuer of the invoice on behalf of the vendor.

Review VAT position in relation to one-off transactions

30. Accelerate VAT refund through VAT registration.

Even one-off transactions can result in VAT registration requirements in foreign VAT jurisdictions. While this results in an additional VAT administration cost for the VAT registration and related (limited) VAT reporting requirements such registration can allow to recover foreign input VAT incurred in relation to the one-off transaction much faster than through 8th or 13th EU VAT Directive refund claims (even a voluntary registration where allowed should be envisaged for that purpose).

Employer Tax (GES)

31. Cross charges of assignment related costs.

At the time of payment of costs related to the assignment of an employee to an affiliated foreign company (e.g. salary, benefit in kind, taxes, etc), a contemporary and complete cross-charge to the foreign company should be put into practice and immediate payment should be requested.

32. Income tax payments for employees on assignment.

Encourage your employees that are currently on assignment to/from a foreign company to submit the relevant information for the preparation of the income tax returns to the engaged tax provider in order to receive any income tax refunds from the German tax authorities that are related to the assignment.

It should be examined closely if it is necessary and if it is consistent with the assignment policy of your company that the company bears the assignment related German and foreign income taxes of employees who are currently assigned to/from a foreign company.

33. Wage withholding taxes.

It should be applied for wage tax exemption certificates for employees who are currently assigned to a foreign company in a country with a double tax treaty. This could be beneficial in case a net salary agreement has been arranged.

34. Avoid Penalties.

Wage tax returns should be filed timely and correct in order to avoid additional payments.

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