

Taxation and Investment in Germany 2011

Reach, relevance and reliability



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1.0 Investment climate

1.1 Business environment

Germany is a federation of 16 states (*Länder*), each with its own constitution, government and independent court. The federal government and parliament are responsible for major legislation on economic policy. The federal parliament comprises a directly elected lower house (*Bundestag*) and an upper house (*Bundesrat*), which consists of representatives of the *Länder* governments.

Manufacturing and related services are at the heart of the German economy. The main industries are automotive and chemical, and telecommunications has become very important. The steel-making sector in the Ruhr region has declined, as has the significance of agriculture.

Germany is one of the world's premier trading nations, with a powerful export sector and significant imports. Its main trading partners are the EU and the U.S. The German government has traditionally advocated free trade. The EU sets the levels of common tariffs and detailed rules on other import restrictions.

Germany is an EU member state, as well as a member of the OECD.

Price controls

The Federal Cartel Office will take action against companies that abuse their dominant market position through "excessive" price increases. The Law against Restraint of Competition prohibits price policies meant to force competitors out of the market (e.g. constant offers below cost price).

Intellectual property

Patents, industrial designs and models, trademarks and copyrights are legally recognized in Germany. Enforcement of patent and trademark laws is rapid and satisfactory, and damages can be claimed in cases of infringement.

The 1994 trademark law aligned German legislation with that of other EU member states. A trademark becomes valid as soon as it is entered into the official registry. The usual processing time is 10-12 months, although, for an additional fee, the process can be reduced to six months.

A registered trademark is valid for 10 years and can be protected indefinitely in 10-year increments. However, the trademark owner (or a third party) may apply for the trademark to be deleted if the trademark name is a term of everyday use or if a person has proof of an older right to the name; or if the trademark has not been used for more than five years. Although the Patent and Trademark Office does not specify what constitutes trademark "use," it generally must be used in connection with the goods (e.g. on the item or on its packaging).

A third party that claims to have older rights than the applicant may challenge the registration of a trademark at any time. The date of application to the Patent and Trademark Office is crucial in determining the party with priority. The Patent Office itself does not investigate prior claims of others in the trademark register but leaves it to the owners of existing rights to assert their priority. If an objection is raised, the office compares the older (objecting) trademark with that of the applicant.

Many trademark disputes are settled by "delimitation agreements," whereby the challenged party agrees to use his/her trademark in a restricted manner (e.g. only for certain goods or in connection with specific alterations to the new mark to differentiate it from the existing mark). Such agreements are also used to make the prior holder of a mark withdraw his/her objection against the registration of the trademark.

1.2 Currency

The currency in Germany is the Euro.

Countries participating in the Economic and Monetary Union		
Austria	Germany	Netherlands
Belgium	Greece	Portugal
Cyprus	Ireland	Slovakia
Estonia	Italy	Slovenia
Finland	Luxembourg	Spain
France	Malta	

1.3 Banking and financing

The major domestic commercial banks are the primary source of capital for foreign companies. Every kind of financing is available from German and foreign commercial and investment banks, mortgage institutions and insurance companies. All the major international commercial and investment banks have operations in Germany, most with offices in Frankfurt.

Frankfurt is the financial center. It is home to the European Central Bank, the *Bundesbank* (the national central bank), leading commercial banks, as well as the government's holding company for state assets.

1.4 Foreign investment

The German government welcomes foreign investment that provides new jobs. There are no serious limitations on new projects, except for a law requiring prior government permission for the sale of defense companies to foreign investors. Under the foreign trade law, the government can prohibit or apply restrictions to the acquisition (directly or indirectly) by a non-EU party of a domestic entity if this measure is required to maintain public law and order. No permanent currency or administrative controls on foreign investments apply. Foreign investors are subject to the same conditions as their German counterparts in obtaining operating licenses, securing building permits and obtaining approval for investment incentives.

1.5 Tax incentives

Various incentive programs are available, e.g. for the purchase or production of movable assets in Eastern Germany and for founders of new businesses. Furthermore, various programs exist for the promotion of modern energy generation and efficiency, e.g. solar and wind energy, as well as programs for the promotion of domestic buildings, environment protection, R&D, health care, infrastructure and agriculture. Regional and federal programs are available. Promotion can either be granted as a tax benefit, allowance, guarantee, loan or participation.

1.6 Exchange controls

Germany's policies on capital flows are liberal. There are no exchange controls on ordinary commercial transactions, and companies have unrestricted access to both borrowing and lending abroad. External funding is facilitated by the full convertibility of the Euro, and the foreign exchange market is freely accessible. However, the regional branch of the *Bundesbank* must be notified for statistical purposes of both inbound and outbound transactions.

2.0 Setting up a business

2.1 Principal forms of business entity

The two most common forms of incorporation are the joint stock corporation (*Aktiengesellschaft* or AG), which is regulated by the Joint Stock Corporation Act, and the limited liability company (*Gesellschaft mit beschränkter Haftung* or GmbH), which is governed by the Limited Liability Company Act.

Some companies are incorporated as a commercial partnership limited by shares (*Kommanditgesellschaft auf Aktien* or KGaA). The most common forms of unincorporated firms are: the limited commercial partnership (*Kommanditgesellschaft* or KG), in which the liability of at least one partner is unlimited (general partner) and limited for the other partner(s) (limited partner(s)); and the general commercial partnership (*Offene Handelsgesellschaft* or OHG), in which the liability of the partners is unlimited. Sometimes limited liability companies are founded for the purpose of being the sole general partner in a KG (GmbH & Co KG). These combine the advantages of a GmbH with those of a KG.

Formalities for setting up a company

Companies operating in Germany must be entered in a Commercial Register at the local court.

The registration of a joint stock corporation (AG) or limited liability company (GmbH) is critical for foreign firms establishing a subsidiary in Germany, because, under German law, a parent company remains liable under any pre-incorporation agreement.

Procedures for forming an AG are complicated. Although no permit is needed to form an AG or to issue shares, the founders must draw up articles of association. These must state the following: name of the company, location of its registered office in Germany, objectives, amount of share capital, denominations and type of its shares, and number of members of the board of management or the procedure upon which this number is established. A notary public must record the articles. The founders appoint the supervisory board, whose members in turn appoint the board of management. The members of both boards supervise the company's formation. An additional examination by court-appointed auditors may be required in certain circumstances.

The company must file its registration application with the commercial, provincial or district court in which it is based. At the same time, it must file a deed on the recording of the articles of association, as well as any agreements concerning contributions and acceptances in kind, a calculation of the costs to be borne by the company for formation, all documents on the appointment of the boards, the founders' report on the formation of the company and proof of payment of the founders' shares. The AG comes into existence when the articles of association are entered in the Commercial Register and after the total share capital is subscribed (only 25% must be paid in).

Procedures for forming a GmbH are similar, but simpler. The GmbH has less detailed requirements for stating the firm's major business purpose in the articles of association, lower minimum capital requirements, simpler formalities and more flexibility in legal and business transactions. However, the shares of a GmbH may not be traded on a stock exchange.

Like the AG, the GmbH comes into existence after an application is recorded in the Commercial Register. Before registration, persons who act on behalf of a GmbH are personally liable. Incorporators must agree on the firm's name, place of incorporation (which must be in Germany), intended purpose and amount of capital (including the amounts contributed by each partner). The minimum capital is EUR 25,000. This information must be notarized and entered into the Commercial Register.

The acronym "GmbH" must appear in the firm's official name. The registration takes effect only after 25% of the capital has been paid in; the minimum that must be paid in at registration is EUR 12,500 (additional collateral requirements up to 100% exist where there is only one founding member). Shareholders may be foreign nationals, and they need not have a residence or work permit as long as they retain their residence in their home country. The managing director may be a foreign national but should have a residence permit (for which non-German EU nationals are

automatically eligible); a work permit is not necessary if the managing director is not regarded as a regular employee. There are special agreements with some countries.

The GmbH is the preferred corporate form for foreign investors that want to limit the risk of their activities to the amount of capital they invest in Germany and that do not anticipate raising funds in the capital market (which requires the AG legal form).

The European joint stock corporation, known as *Societas Europaea* (SE), must be registered in the state where it is headquartered and remain under the supervision of the national authorities of that state. It is not necessary for SE shares to be traded on any stock exchange, but if its shares are listed on a stock exchange, the company is subject to the same laws as an AG.

Forms of entity

Requirements for an AG

Capital. Minimum capital is EUR 50,000. At least 25% of capital cash contributions must be paid in when the company is formed, and all capital must be subscribed. Other capital contributions may be in the form of factories, machinery, patents, know-how, etc. Capital contributions in kind must be 100% paid in and are subject to rigid valuations by court appointed auditors. An amount equal to 5% of annual profits after taxes must go into a legal reserve account until the reserve has reached 10% of equity capital. If shares are issued exceeding nominal value, the amount of the premium must be transferred to the reserve account.

Founders, shareholders. One person can establish an AG. There are no nationality or residence restrictions.

Board of directors. The supervisory board must have at least three members or a multiple thereof, up to a maximum of 21. Individuals may not be members of more than 10 boards. Representatives of parent companies may hold up to five additional board seats in affiliates, for a total of 15. There are no limits on the nationality or residence of directors. The shareholders' meeting elects the shareholders' representatives on the board for a maximum period and the employees or their delegates elect staff representatives for the same period. Re-election is possible.

Management. The supervisory board appoints the management board for up to five years. Each member may be re-appointed for additional terms. Managers need not be shareholders, and there are no restrictions on their nationality or residence. Although the minimum number of board members is one, AGs with capital exceeding EUR 3 million must have at least two members on their management boards (unless otherwise provided in the articles of association).

Employees must establish a works council, which has a voice in certain social and personnel decisions. Labor has 50% representation on the supervisory board of companies with a workforce of more than 2,000; in companies with a payroll of 500-2,000, labor representatives must hold one-third of the seats.

Taxes and fees. There are no taxes on incorporation or capital increases. Costs of entering a company in the trade register and of notarizing the articles of association depend on the company's capital stock and on whether a lawyer is used to draft the articles. Where shares are issued at a premium, the premium is not considered taxable income.

Types of shares. The minimum par value of shares is EUR 1. An AG must issue common (ordinary) shares but may issue preferred shares (which usually carry no vote) up to the full amount of common shares. Multiple vote shares are generally not permitted, although nonvoting shares are permitted. Bearer shares are often used, although registered shares are permitted. Registered shares have the same legal rights, specifically in computer trading, as the traditionally used bearer shares.

Control. A simple majority is sufficient to approve most actions; a majority of more than 75% is required for major decisions. A minority of 5% of equity capital or EUR 500,000 in shares, whichever is lower, may do the following: call an extraordinary shareholders' meeting or put topics on the agenda of the shareholders' meeting; object to a decision of the shareholders' meeting for the formation of reserves if this decision is shown to be "economically unreasonable"; and request a special audit when the business report seems incomplete or assets are believed to be undervalued. A minority of 10% or EUR 1 million, whichever is lower, may force a vote about a

nominated board member and demand a special audit of the annual balance sheets and business report, even if the report seems to be complete.

Requirements of a GmbH

Capital. Minimum capital is EUR 25,000, but only EUR 12,500, including deposits in kind, must be paid in (additional collateral requirements up to 100% exist in cases where there is only one founding member). The registry court must value assets in kind paid in by the group or person establishing the GmbH. Minimum capital for entrepreneurial companies with limited liability (“mini-GmbH”) is EUR 1. A legal reserve equal to 25% of the annual profits is required for entrepreneurial companies with limited liability until the registered capital is increased to EUR 25,000 or above.

Founders, shareholders. There is a minimum of one founding member. Founders may also be companies or private partnerships. The acronym GmbH must appear in the firm’s official name. The official name of entrepreneurial companies with limited liability must have the wording “*Unternehmergeellschaft (haftungsbeschränkt)*” or “*UG (haftungsbeschränkt)*.”

Board of directors. A supervisory board is required if there are more than 500 employees. The board then controls management and no person may serve as director and manager simultaneously. The board must comprise at least three members.

Management. One or several managers are permitted. Members may specify management procedures in the company’s bylaws. Managers need not be shareholders. The rules governing representation of labor are the same as for an AG (see above).

Branch of a foreign corporation

A foreign company does not need a permit to establish a branch in Germany. A branch (unlike a subsidiary) is not a separate legal entity and has no rights or obligations other than those of the head office. A branch is categorized either as a dependent entity lacking its own business profile (like a representative office) or as an independent trading entity. Only independent branches must be entered in the commercial register. The tax treatment is the same for both types of branches.

Corporate income tax is assessed on branch income at a flat rate of 15% (plus the 5.5% solidarity surcharge, which results in a combined rate of 15.8%), regardless of whether branch profits are retained in Germany or repatriated to a foreign head office. Municipal trade tax is levied. It typically ranges between 14% and 17%. The effective corporate rate typically ranges between 30% and 33%. The remittance of branch profits is not subject to withholding tax, but remitted subsidiary profits (dividends) face a 25% (26.4%, including the solidarity surcharge) withholding tax (except for profits remitted to qualifying EU parent companies) with a possible 40% refund for nonresident corporations, giving rise to an effective rate of 15.825%. A tax treaty may specify a lower rate. Strict anti-treaty shopping rules apply.

A branch is not subject to the same disclosure requirements as a subsidiary. In a start-up situation, a branch has the advantage of letting the foreign investor offset German-source start-up losses against home-country taxable income, depending on the home country’s tax system. However, a subsequent conversion of the branch into a German corporation typically results in gain recognition, particularly for goodwill; different rules apply to EU companies. The liability of a branch extends to the foreign head office; a subsidiary in principle does not expose the foreign parent to potential liabilities.

A foreign firm may set up an independent branch by registering it in the local Commercial Register. The certified registration must be made at the local court where the branch will be located. Branch managers may be foreign nationals and are not subject to residence limitations. Foreign corporations must include a certified copy of the articles of incorporation (including a German translation) with the application. They must also include detailed information about both the head office company and the branch, e.g. business objectives, amount of equity and composition of the board.

2.2 Regulation of business

Registration and filing requirements

Government approval is not required to enter into licensing agreements or to pay royalties to foreigners. Licensing and technical assistance agreements need not be registered with the

German Patent and Trademark Office. As a rule, compensation under licensing agreements is based on sales, often on a per-unit basis. Many agreements fix annual minimum royalties that must be paid regardless of actual sales.

The main limitations on licensing in Germany arise under antitrust law. The EC Treaty prohibits contracts that limit competition, although an EU regulation on technology transfer allows the licensor to impose certain restrictions on the licensee, such as limiting production of the licensed product to a geographic region. The EU can revoke exemptions granted under this regulation when the market share of a licensed product exceeds 40%.

The Federal Cartel Office allows domestic and foreign licensors to impose export prohibitions on their licensees when the relevant product is not designated for EU countries. Licensors may also stipulate that the product be exported only to other countries within the EU, although they may not stipulate which countries.

Tie-ins are allowed only to the extent they are necessary to maintain the technical standard of the licensed product. A licensor may not restrict the handling or pricing of competitive products, because such restrictions exceed the scope of a patent or other protected right and would restrict the licensee's business activities. The parties may agree on clauses that prohibit the licensee from directly or indirectly contesting the validity of the patent or other licensed property rights.

A licensing agreement may outlast the patent right for which it is granted if the license also includes longer term provisions for technical know-how and assistance. The duration of the licensing agreement then depends on the duration of these other provisions. Know-how is recognized as a licensable property right. Germany does not limit the licensing of further developments of the initial patent.

Mergers and acquisitions

Under the Law against the Restraint of Competition, the following transactions are deemed to be a merger:

- Acquisition of all or of a substantial part of the assets of another undertaking;
- Acquisition of direct or indirect control by one or several undertakings of the whole or parts of one or more undertakings; control is constituted by rights, contracts or any other means that, either separately or in combination with and having regard to the considerations of fact or law involved, confer the possibility of exercising decisive influence on an undertaking;
- Acquisition of shares in another undertaking if the shares, either separately or together with other shares already held by the undertaking, reach or exceed 50% or 25% (indirect or direct) of the capital or the voting rights of the other undertaking.

The office must be notified, in German, of mergers and acquisitions that meet the following criteria:

- Combined worldwide turnover of the companies exceeded EUR 500 million or more in the business year preceding the merger; and
- Domestic turnover of at least one participating company was more than EUR 25 million; and
- Domestic turnover of another participating company was more than EUR 5 million.

The turnover of affiliated undertakings of the participating companies must be taken into account when calculating whether the turnover thresholds are met.

The Federal Cartel Office does not have to be notified of M&As where the merger has no effect on the German market; the turnover thresholds are not reached; the de minimis clause applies (i.e. an independent company with annual worldwide sales of EUR 10 million or less is merging with another company (not applicable to print media)); or the merger exclusively concerns a market that has existed for five years or more but has an annual volume of less than EUR 15 million.

Mergers with a Community dimension fall within the competence of the EU Commission and need to be notified under Council Regulation (EC) No. 139/2004. The EU has jurisdiction over mergers in two situations:

- 1) Where the combined aggregate worldwide turnover of all of the undertakings concerned is more than EUR 5 billion and the aggregate EU-wide turnover of each of at least two of the undertakings is more than EUR 250 million, unless each of the undertakings concerned achieves more than two-thirds of its aggregate EU-wide turnover in a single member state; and
- 2) Where the aggregate global turnover of the companies concerned exceeds EUR 2.5 billion for all businesses involved, aggregate global turnover in each of at least three member states is more than EUR 100 million, aggregate turnover in each of these three member states of at least two undertakings is more than EUR 25 million and aggregate EU-wide turnover of each of at least two of the undertakings is more than EUR 100 million, unless each achieves more than two-thirds of its aggregate EU-wide turnover within one and the same state.

If a merger would not normally fall within the European Commission's purview, the affected companies may ask the Commission to review it if they would otherwise be obliged to notify three or more member states. The Commission proceeds as a "one-stop shop" only if none of the relevant member states objects within 15 days.

Monopolies and restraint of trade

Market dominance in itself is not illegal in Germany, but the abuse of a dominant position is. The existence of market dominance depends on whether an enterprise, as a seller or a buyer of goods or services, has no (effective) competitors or holds an overwhelming position against its rivals. This may be evidenced by the company's market share, financial power, access to sales and procurement markets, interlocking arrangements with other companies or other obstacles preventing firms from entering the market. Market dominance may be presumed when a company holds a market share of at least one-third.

A group of companies may be regarded as dominating the market when it consists of three or fewer companies that together control one-half of the market or when it consists of five or fewer companies that together control two-thirds of the market. Exceptions apply when the companies that together hold a dominant market share can prove that the competition between them is such that no domination is likely or that the group is not dominant compared with the other competitors. A dominant market position is abused if it is used to impede other market participants, actual or potential, or to demand excessively high or low prices.

2.3 Accounting, filing and auditing requirements

The shareholders of large and medium-size firms (those that exceed two of the following three categories: annual sales of EUR 9.68 million, assets of EUR 4.84 million and a workforce of 50) must elect an independent certified accountant every year to audit the company's financial statements. The board or the shareholders must approve the financial statements. Large and medium-size firms must compile their annual balance sheets within three months of the end of the business year and have it assessed by an independent accountant. This period is extended to six months for small firms (i.e. firms that do not meet the above criteria).

All companies must publish their financial statements, together with a management report, a proposal on the allocation of profits and the report by an independent accountant within 12 months of the end of the business year by depositing them with the electronic federal gazette. Certain exceptions apply for small and medium-size companies. All financial statements must contain comparative data and include details of the company's minority and majority holdings in other corporations and disclose valuation and depreciation of fixed assets.

Companies must set up a depreciation plan and announce details in the business report at least once every three years. Changes in property valuation and depreciation methods must be announced. In addition, some companies voluntarily make other disclosures in "social accounts." Disclosure is obligatory each time a shareholder obtains voting shares in an AG surpassing thresholds of 5%, 10%, 25%, 50% or 75%.

EU directives harmonize company reporting and accounting requirements. The basic rules, codified in the Commercial Code, affect most firms (AGs, GmbHs and KGaAs), although the major requirements apply only to large and medium-sized companies. The rules apply equally to German subsidiaries of foreign corporations.

The German authorities have made significant efforts to improve corporate governance. Several laws have been passed aimed at defining and regulating the actions of management and the board, protecting private investors and restoring confidence in the stock market.

International Financial Reporting Standards (IFRS) is binding on all European corporations that trade on a stock market or issue bonds. Companies listed on a stock market must publish their financial statements according to IFRS in the financial year beginning on or after 1 January 2005. All other companies active on the capital markets were required to switch to IFRS by 2007 at the latest.

3.0 Business taxation

3.1 Overview

The principal taxes applicable to companies in Germany are the corporate income tax, municipal trade tax, value added tax (VAT) and social security contributions. In addition to the normal corporate income tax, a surcharge of 5.5% of corporate income tax paid is levied to finance Germany's reunification. Other taxes include municipal real estate tax, real estate transfer tax, and customs and excise duties.

Municipal trade tax is levied by the local authorities on business profits. The tax rate varies from community to community but averages 14%-17% of income. Municipal trade tax paid for assessment periods ending after 31 December 2007 is no longer a deductible item for trade tax and income tax purposes. The most important corporate bodies established under German law that are subject to corporate income taxation are the AG and the GmbH, but others include the KGaA, trade and industrial cooperatives and mutual insurance companies. Comparable foreign entities are taxed as nonresidents and are only subject to tax on their German-source income. General and limited partnerships (OHG and KG) are not taxable entities for corporate income tax purposes, even though the taxable income of their partners is determined at the partnership level, but they may be taxable entities for trade tax purposes.

Germany's "split-rate" tax system was abolished in 2001 and replaced with a "classical" system of taxation. Under current rules, dividends received by a resident company are generally exempt from corporate income tax regardless of how long the participation in the subsidiary has been held and the extent of the participation. However, 5% of the gross dividend is added back to taxable income as nondeductible business expenses, resulting in an effective tax rate of approximately 1.5% (including municipal trade tax). The 95% exemption for dividends does not apply to certain banks, financial institutions, shares held by finance companies for the purpose of realizing a short-term profit from trading activities ("held for trading exception"), life or health insurance companies or pension funds, unless the EC Parent-Subsidiary Directive applies. Since the end of 2006, the exemption applies only if the dividend has not been treated as a deductible business expense at the level of the distributing company. The 95% exemption generally will apply for trade tax purposes only if certain minimum holding and minimum ownership requirements are met. In addition, certain activity requirements apply for shareholdings in companies that are resident outside the EU.

A similar rule applies for capital gains on the sale of corporate shareholdings. Capital gains arising from the sale of shares by a corporation should be 100% tax exempt with a 5% add-back as nondeductible business expenses. Exceptions apply to certain banks, financial institutions, shares held by finance companies for the purpose of realizing a short-term profit from trading activities ("held for trading exception"), life or health insurance companies or pension funds that do not benefit from the 95% exemption. This also applies for shares that result from certain types of pre-13 December 2006 reorganizations at below fair market value if the shares are sold within seven years from the effective date of the reorganization.

3.2 Residence

Corporations with a registered office or a German place of management and control are deemed to be resident in Germany. Foreign companies that have neither their legal seat nor a place of management and control in Germany are deemed to be nonresident.

3.3 Taxable income and rates

The corporate tax rate is 15%, plus the 5.5% solidarity surcharge, which results in a combined rate of 15.8%.

Resident corporations are subject to corporate income tax on their worldwide income. In practice, however, tax treaties generally provide that income earned in a foreign country will be taxed only in that country and remain tax-free in Germany. Nonresident companies are subject to German corporate income tax only on German-source income. The income of a nonresident company derived from a branch, permanent establishment in Germany or partnership interest in a German

partnership is subject to the normal 15% corporate income tax rate, plus the 5.5% solidarity surcharge and trade tax, resulting in an effective rate of 30%-33%. A nonresident company's other sources of income (e.g. from royalties) are taxed by way of withholding, which may be reduced under an applicable tax treaty.

Taxable income defined

All income of a corporation is generally considered to be business income.

In general, the commercial balance sheet is authoritative for determining the taxable income. Options under German tax law are, however, permitted to be exercised without corresponding disclosure in the commercial balance sheet provided the assets concerned are recorded in current listings, which will have to substantiate detailed information about the relevant assets.

In this context, deferred tax assets and deferred tax liabilities, recognizing accounting and valuation differences between commercial and tax balance sheets, have to be stated according to the internationally recognized balance sheet method ("temporary concept"). The obligation to capitalize deferred tax assets also covers explicitly tax reliefs anticipated on account of unrealized tax loss carryforwards, as well as tax credits and interest carryforwards. These are, however, only permitted to be taken into account if they are expected to be used for netting losses within the five financial years following the balance sheet date.

Deductions

In general, all expenses are deductible if they are incurred as a result of the company's business operations. Certain expenses may be disallowed (e.g. expenses related to exempt income) or may be deductible only up to a limited amount.

As from fiscal year 2008, taxpayers may immediately deduct only (net) interest expense up to 30% of annual pre-interest, pre-loss carryforward profits for tax purposes, increased by the tax depreciation incurred (taxable EBITDA – earnings before interest, tax, depreciation and goodwill impairment/intangible asset amortization). The 30% limitation applies to all interest regardless of whether the debt is granted by a shareholder, related party or third party. Excess interest may be carried forward indefinitely. An EBITDA carryforward is generated if the taxpayer has net interest expense lower than 30% of the EBITDA for tax purposes. The difference between 30% of the EBITDA and the net interest expense (the excess EBITDA) may be carried forward and used in the following 5 years when the net interest expenses exceed 30% of current EBITDA. The 30% limit does not apply where (1) the annual (net) interest burden is less than EUR 3 million; (2) the taxpayer is not part of a group of companies; or (3) under the "group clause," the taxpayer demonstrates that the equity ratio of the German borrower does not fall short by more than two percentage point from the worldwide group's equity ratio.

The EBITDA threshold is calculated on the basis of the current year EBITDA of the German business (i.e. the year for which interest deductions should be claimed). A tax group for German tax purposes is treated as one business.

Interest expense exceeding the 30% limitation is nondeductible for German corporate income tax and trade tax purposes (unless one of the exceptions applies). The interest carryforward is subject to change-in-ownership rules (a direct or indirect ownership change of more than 25%/50% to one shareholder (or a group of shareholders with similar objectives)), which could result in a partial/complete forfeiture of all interest carryforwards.

Unlike under the former thin capitalization rules, interest expense disallowed under the interest deduction limitation will not trigger withholding taxes, but may lead to double taxation even within Germany.

The 30% limitation does not apply where the borrowing business can show that its equity ratio does not fall short by more than two percentage points from the worldwide group's equity ratio. The group clause test is applied based on financial statements for the German business at the end of the previous fiscal year. A uniform accounting standard must be used for the German business and the group financial statements (primarily IFRS and, if no IFRS accounts are available, any European GAAP or U.S. GAAP as a last resort).

Depreciation

Depreciable assets comprise fixed assets (tangible and intangible) with a useful life exceeding one year and diminishing in value over time through wear and tear. Land is not depreciable. Permitted methods include the straight-line method in which the same percentage of the original value is deducted each year for all assets; in some cases, movable assets may be depreciated according to the units-of-production method. For financial years up to and including 2007, taxpayers could use the declining-balance method. This option was repealed as from 2008, but subsequently reinstated as a result of the global economic crisis and was temporarily available in 2009 and 2010.

For acquisitions made after 31 December 2003, depreciation for tax purposes is calculated monthly. However, this rule does not apply to the depreciation of new buildings and the declining-balance method (where applicable).

Accelerated depreciation for exceptional wear and tear resulting from technical or economic causes may be applied only if the straight-line method is used. Low-value assets of less than EUR 150 can be deducted immediately and certain pools of assets with acquisition costs of between EUR 150 and EUR 1,000 can be recorded as a collective item with a write-off period of five years. Alternatively, as from 2010, low-value assets of up to EUR 410 may be depreciated immediately.

The Ministry of Finance publishes tax depreciation rates for a number of assets, based on useful life periods.

For industrial buildings, the annual straight-line rate is, in general, 3%.

Inventory is valued at cost or market value, whichever is lower. Last-in, first-out (LIFO) is generally acceptable for tax purposes; other cost flow assumptions, such as first-in, first-out (FIFO), are generally not acceptable for tax purposes.

Certain additional types of depreciation are available for small and medium-sized companies as a tax incentive.

Write downs of shares in corporations by corporate shareholders will not be effective for tax purposes because of the exemption for capital gains from shares. Write-downs on certain shareholder loans will be restricted from fiscal year 2008 for the same reason.

Purchased goodwill is amortized over 15 years using the straight-line method for tax purposes.

Provisions

The tax law permits the creation of provisions for certain liabilities or anticipated losses (e.g. surety obligations, warranties, damage claims, litigation expenses and future pension payments to employees). Companies may create an accrual to deal with the infringement of third-party patents and similar rights if the owner of the rights claimed compensation for damages or if such a claim is expected. Provisions for obligations must be discounted by 5.5% for tax purposes, except for provisions with a duration of less than 12 month on the closing date.

Losses

Losses that cannot be offset against gains in the same year may be carried forward indefinitely and carried back for one year. The loss carryback is limited to EUR 511,500 for corporate income tax purposes. No carryback is possible for trade tax purposes. No restrictions are imposed on the utilization of loss carryforwards of up to EUR 1 million; however, the utilization of loss carryforwards exceeding EUR 1 million is capped at 60% of income. Therefore, the remaining 40% of income will be taxed at the general rates ("minimum taxation"). The concept of minimum taxation also applies for trade tax purposes.

A two-tier change of ownership rule applies as from 1 January 2008. All corporate income tax and trade tax losses will be forfeited if more than 50% of the shares in a loss corporation are directly or indirectly transferred to one buyer (or a group of related buyers) within a period of five years. In the case of transfers of more than 25% but less than 50% to one buyer (or a group of buyers) within a period of five years, losses will be forfeited on a pro rata basis. As from 1 January 2010, loss carryforwards will not be forfeited if a single person or entity owns directly or indirectly 100% of the shares in the transferring and the receiving company. Loss carryforwards continue to be available to the extent built-in gains in the loss company are subject to tax in Germany.

3.4 Trade tax

Trade tax is an income tax levied by municipalities, at a minimum rate of 7%. All entrepreneurs with commercial activities carried out through a subsidiary or a nonresident's commercial permanent establishment in Germany, are liable for trade tax. Corporations are always deemed to carry on commercial enterprises (trade or business), regardless of actual activities. Individuals, alone or in partnerships, are not liable for trade tax on professional or other independent services unless activities are deemed to be commercial under the income tax law.

Trade tax is based on taxable income as calculated for corporate income tax purposes; however, several income adjustments apply.

The tax rate varies from community to community, but averages 14%-17% of income. As from fiscal year 2008, the municipal trade tax is no longer deductible as a business expense.

3.5 Capital gains taxation

There is no separate capital gains tax in Germany; capital gains are included in taxable income unless exempt under the participation exemption. Generally, all capital gains realized by an enterprise from the disposal of business assets are treated as ordinary business income. However, gains from the sale of certain fixed assets (e.g. real property and buildings) may be rolled over if the proceeds are used for reinvestment purposes.

Capital gains derived from the sale of shareholdings between corporations are generally 95% tax-exempt (100% exemption, with a 5% add-back as nondeductible business expenses).

3.6 Double taxation relief

Unilateral relief

In non-treaty situations or treaty situations where the treaty provides for a tax credit, German taxpayers with foreign-source income may credit foreign taxes paid to the extent they relate to income that is subject to tax under domestic law. Alternatively, the taxpayer may deduct foreign tax paid as a business expense. If the income is exempt from German tax, no tax credit or deduction will be possible.

Tax treaties

Germany has a broad tax treaty network, with most treaties following the OECD model treaty.

Germany Tax Treaty Network			
Algeria	Greece	Mexico	Serbia ⁽²⁾
Argentina	Hungary	Moldova ⁽¹⁾	Singapore
Armenia ⁽¹⁾	Iceland	Mongolia	Slovakia ⁽³⁾
Australia	India	Morocco	Slovenia
Austria	Indonesia	Namibia	South Africa
Azerbaijan	Iran	Netherlands	Spain
Bangladesh	Ireland	New Zealand	Sri Lanka
Belarus	Israel	Norfolk Island	Sweden
Belgium	Italy	Norway	Switzerland
Bolivia	Ivory Coast	Malta	Tajikistan
Bosnia-Herzegovina ⁽²⁾	Jamaica	Mauritius	Thailand
Bulgaria	Japan	Mexico	Trinidad/Tobago
Canada	Kazakhstan	Moldova ⁽¹⁾	Tunisia
China	Kenya	Mongolia	Turkey

Croatia	Korea (ROK)	Morocco	Turkmenistan ⁽¹⁾
Cyprus	Kuwait	Namibia	Ukraine
Czech Republic ⁽³⁾	Kyrgyzstan	Netherlands	United Kingdom
Denmark	Latvia	New Zealand	United States
Ecuador	Liberia	Norfolk Island	Uruguay
Egypt	Lithuania	Norway	Uzbekistan
Estonia	Luxembourg	Pakistan	Venezuela
Finland	Macedonia ⁽²⁾	Poland	Vietnam
France	Malaysia	Portugal	Zambia
Georgia	Malta	Romania	Zimbabwe
Ghana	Mauritius	Russia	

(1) The treaty with the former Soviet Union continues to apply. (2) The treaty with Yugoslavia continues to apply. (3) The treaty with Czechoslovakia continues to apply.

3.7 Anti-avoidance rules

Transfer pricing

The Foreign Tax Act and the General Tax Code generally govern cross-border transactions between related parties. Administrative regulations contain comprehensive rules for determining transfer prices, service charges for intercompany services (including royalties), for sharing R&D cost and administrative service centers and for secondments of personnel.

German related parties must apply the arm's length principle when engaging in cross-border transactions with affiliated enterprises. A person may be deemed to be a related party/affiliated company if it is related by a direct or indirect shareholding of 25% or more to another entity or if both entities have a common parent that holds at least 25%. Two entities will be deemed to be related if one entity has a controlling influence (regardless of the shareholding) over the other party or if a third party has a controlling influence over both entities. Finally, an entity will be considered a related party if it is in a position, when agreeing to the terms of a business relationship, to exercise influence (on the business relations) that is caused by other factors than the business relationship or if one party has a commonality of interest in the realization of the other's income. The criteria for qualification as a related party can be met either from a legal perspective or based on the facts of the particular case.

A taxpayer may choose one of the standard transfer pricing methodologies, i.e. the comparable uncontrolled price, resale price or cost plus method. These methods prevail over other methods that a taxpayer may use if adequate comparables are available. The transactional net margin method may be used only if the company is engaged in routine functions and if the other methods described above cannot be used. The profit split method may be applied only if the standard methods do not lead to reliable results. The German tax authorities generally do not accept the comparable profits method.

A German taxpayer's income may be adjusted upward to an arm's length compensation where the company's reported income is lower than it would have been had it conducted business with unrelated business partners. From 2008, a transfer of "functions" (i.e. parts of a taxpayer's business) to another country should trigger an exit taxation for the taxpayer based on the assumption that potential future taxable income is transferred abroad. The tax burden resulting from transfer pricing adjustments can be substantial, particularly since German tax authorities can levy significant penalties (up to 10% of the income adjustment) for failure to comply with the transfer pricing rules.

Transfer pricing documentation must be prepared within 60 days of a request by the tax auditor for "normal" transactions. Extraordinary transactions require contemporaneous documentation (i.e. documentation that is prepared within six months of the fiscal year end of the relevant fiscal year).

Penalties must be imposed if documentation is not submitted or if documentation is basically of no use. Penalties amounting from 5% to 10% of the income adjustment (at least EUR 5,000) must be imposed in cases of non-compliance. In the case of late submission of requested documents, the penalty is limited to EUR 1 million, but at least EUR 100 per day.

Thin capitalization

The German thin capitalization rules were replaced as from fiscal year 2008 by a new interest deduction limitation (see above). The new rules took effect as from 1 January 2008 for calendar year taxpayers. For taxpayers with a deviating fiscal year, the new rules apply for all fiscal years starting after 25 May 2007 (and not ending before 1 January 2008).

Controlled foreign companies

Under the Foreign Tax Act, certain profits considered as passive income of controlled foreign companies (CFC) resident in a low-tax jurisdiction controlled by German resident shareholders may be attributed proportionally to those shareholders and included in their taxable income. Such an attribution requires in particular that:

- One or more German residents hold, directly or indirectly, more than 50% (a percentage of 1% or even below 1% may apply in case of passive investment income) of the shares or voting power in the CFC at the end of the respective fiscal year for which an income attribution occurs; and
- The CFC receives passive income; and
- The passive income is subject to tax at an effective rate less than 25%.

If the CFC rules apply, the tax haven income of a foreign subsidiary that does not conduct active operations is taxable in Germany as though the income was earned by the German parent company. Active income is defined as income derived from:

- Agriculture and forestry;
- Exploitation of natural resources, energy generation, manufacturing, and processing of goods;
- Banking or insurance business (unless captive);
- Trading (unless captive);
- Services (unless captive);
- Leasing of movable and immovable assets and licensing (only of self-developed intangibles);
- The taking on of debt and on-lending to a German business or to a foreign active business;
- Profit distributions of corporations;
- The sale of shares to another corporation, as well as the dissolution or reduction of its capital; and
- Certain reorganizations if they fulfill the requirements of the sale of shares to another corporation.

Exceptions to the definition of active income mainly apply if the activities are carried out with the assistance of or support by a German related company and if the foreign intermediary company does not have sufficient economic substance to run a business.

Following the European Court of Justice decision in the *Cadbury Schweppes* case, the CFC rules will generally remain in effect, but taxpayers have the right in certain cases to demonstrate that an EU/EEA-resident CFC carries out genuine commercial activities and whether the Mutual Assistance Directive (or a comparable exchange of information agreement) applies. The CFC income attribution will not apply if the taxpayer can demonstrate that these requirements are met.

The definition of "low taxation" for CFC purposes is broadened for profits earned by a foreign CFC in fiscal years starting after 31 December 2010. Credits and refunds at the shareholder level will be

taken into account when determining whether the effective tax rate abroad falls below the 25% threshold.

In the case of low-taxed partnerships or permanent establishments that earn passive income as described above, Germany will switch unilaterally from the exemption method to the credit method despite a treaty exemption.

General anti-avoidance rule

In general, taxpayers are entitled to order their affairs through legal means so that they pay the minimum tax imposed by the appropriate Act. However, the German tax law contains a general anti avoidance rule whereby the abuse of tax planning schemes is not permissible. An abuse will be deemed to exist where an inappropriate legal option is selected which, in comparison with an appropriate option, leads to tax advantages unintended by laws for the taxpayer or a third party. The anti-avoidance provision will not apply where the taxpayer provides evidence of nontax reasons for the selected option and those are relevant when viewed from an overall perspective. The application of the GAAR rule depends on all of the relevant facts and circumstances of the case. A general indication for the existence of an abuse is that a scheme is entered into or carried out for the dominant purpose of obtaining a tax benefit and there are justifiable business reasons for the scheme. In addition to the GAAR, German tax law contains several specific anti-avoidance rules, e.g. on transfer pricing, thin capitalization and CFCs.

3.8 Administration

Tax year

The tax assessment period is generally the calendar year, although a resident company may elect a deviating fiscal year to be its tax year. A company may only change its fiscal year (and hence its tax year) to a deviating fiscal year with the consent of the tax authorities (but may change it back from a deviating fiscal year to a calendar year without the tax authorities' consent). Fiscal years may not be longer than 12 months, but they may be shorter.

Filing and payment

Corporate taxes in Germany are assessed on an annual basis, but advance payment is required in quarterly installments (on 10 March, 10 June, 10 September and 10 December). Municipal taxes are due on 15 February, 15 May, 15 August and 15 November.

Final tax returns must generally be filed by 31 May of the following year. If a professional tax consultant prepares the return, the due date is automatically extended to 31 December of the following year; however, the tax authorities may request that a taxpayer file the tax return before 31 December. Fines are imposed for unauthorized late payments; they are usually 1% per month of the amount of overdue tax, plus a punitive fine, depending on the case.

Employers are responsible for withholding wage withholding tax on remuneration paid to their employees. They must remit wage withholding taxes on a monthly basis for all employees if the combined wage tax of such employees exceeds EUR 4,000 in the previous year and on a quarterly basis if the wage withholding tax for all employees is EUR 1,000-EUR 4,000 in the previous year. The dates are the same as for VAT. If the total wage withholding tax amounts to less than EUR 1,000 for the previous year, wage withholding tax may be remitted once a year.

The tax authorities may determine fines for late filing, which may amount to up to 10% of the overdue tax. A three-day grace period applies for wire payments.

Consolidated returns

German tax law allows groups of companies to form a tax group (*Organschaft*). In this case, current losses of companies that are part of the group may be offset against the profits of the head of the consolidated tax group (and profits transferred to the parent from other tax group subsidiaries). To form an *Organschaft*, the parent company (either a German company, German partnership maintaining a trade or business, a German individual or the German-registered branch of a foreign company) must hold the majority of the shares or the voting rights in a German corporation from the beginning of the subsidiary's fiscal year. Moreover, a profit and loss pooling agreement with a minimum duration of five years must be signed by the members of the tax

consolidation, which also must be registered in the subsidiary's fiscal year before the end of the fiscal year for which the *Organschaft* will be effective.

Statute of limitations

The statute of limitations for tax assessments is four years beginning from the end of the year the tax became due or is being assessed. The statute of limitations is 10 years in the case of deliberate fraud and five years for negligent fraud. The period for the collection of tax is five years.

Tax authorities

The German tax authorities carry out the public administration of all fiscal affairs in the country. There are several levels in the tax authorities: (i) the highest authorities, the Federal Ministry of Finance and the highest authorities of the Länder; (ii) as higher federal authorities, the Federal Monopoly Administration for Spirits and the Federal Central Tax Office; (iii) as intermediate authorities, the federal finance offices, regional finance offices and the Customs Criminological Office; and (iv) as local authorities, the main customs offices including their agencies, the customs investigation offices, the tax offices and the special revenue of the Länder. The subject matter and the jurisdiction of each authority is determined by law and include residence, habitual abode, place of management, legal seat of a corporation and location of the business, agriculture or real estate.

Rulings

The tax offices and the Federal Central Tax Office may, upon an application by the taxpayer, issue an advance ruling on the tax treatment of specific circumstances, where this is of special interest in light of significant tax implications. A fee is charged for processing an application and is calculated on the basis of the value of the advance ruling for the applicant (i.e. on the amount of tax at stake).

4.0 Withholding taxes

4.1 Dividends

The dividend withholding tax rate is 25% (26.4%, including the solidarity surcharge, an increase from 20% (21.1% with the surcharge)). A 40% refund is granted to nonresident corporations (subject to anti-treaty shopping rules) upon application with the Federal Central Tax Office, which should result in an effective withholding tax rate of 15.825% on dividends for nonresident corporations in non-treaty/non-EC Directive situations.

Under the Parent-Subsidiary Directive, domestic withholding tax will be reduced to zero if dividends are distributed to a qualifying EU shareholder that has held at least 10% of the subsidiary for at least 12 months. The distributing company may only apply the lower rate of withholding tax under a treaty or the Directive if the parent company obtained an exemption certificate from the German Federal Tax Office before the payment is made. Anti-abuse rules apply.

4.2 Interest

There is no withholding tax on interest paid, except for publicly traded debt, interest received through a German payment agent (usually a bank), convertible bonds and certain profit participating loans where a German resident company is the debtor. In these cases, withholding tax is levied at a rate of 25% (26.4%, including the solidarity surcharge). The withholding tax rate may be reduced by an applicable tax treaty or if the requirements of the EC Interest and Royalties Directive are met.

4.3 Royalties

The statutory withholding tax rate on royalty and lease payments on movable property paid to nonresident corporations is 15% (15.8%, including the solidarity surcharge). A 30% (31.7%, including the solidarity surcharge) withholding tax applies to royalty and lease payments if paid to persons other than corporations (e.g. individuals) and such persons opt for the deduction of business expenses in calculating the withholding tax base. Withholding tax on royalties may be reduced under a tax treaty or the EC Interest and Royalties Directive. The administrative procedure is similar to the procedure for dividends (i.e. an exemption certificate must be obtained before payment of the royalties).

4.4 Branch remittance tax

Germany does not levy a branch remittance tax.

4.5 Wage tax/social security contributions

While wage tax is a withholding tax (as it reflects the deduction of personal income tax for the employee at source), social security contributions are a burden on the employer (as they are equally divided between the employer and the employee) (see also 7.2).

5.0 Indirect taxes

5.1 Value added tax

VAT is levied at each stage of the production and distribution chain. In general, taxable supplies of goods or services within the German territory that are carried out by a VAT entrepreneur, as well as intra-community acquisitions and imports of goods, fall within the scope of German VAT.

With regard to the supply of goods and services, VAT generally arises at the time the supply is carried out, regardless of whether the supplier receives consideration from the recipient (an exemption applies to advance payments). Smaller companies and self-employed individuals with annual sales of less than EUR 250,000 (in the previous calendar year, EUR 500,000 from 1 July 2009 to 31 December 2011) may request a deferral of VAT until payment is received.

The standard rate of German VAT is 19%, with a reduced rate of 7% applying to certain "necessities." VAT-exempt transactions include financial and insurance services; transactions subject to the real property transfer tax; the export of goods; intra-community supplies; the granting of loans; medical services; social welfare activities; cultural activities; and educational activities.

To compute VAT liability, a VAT entrepreneur must determine the total output VAT (VAT charged to customers for supplies of goods and services and VAT liable on intra-community acquisitions) within a reporting period. From this total, the entrepreneur deducts the input VAT, which is the VAT paid to suppliers on the supply of goods and services and the VAT liable on intra-community acquisitions and imports of goods. The positive difference between output VAT and input VAT is paid to the tax authorities. There are a number of formal requirements for the deduction of input VAT, e.g. concerning the content of the invoices received. Moreover, input VAT may not be deducted if the underlying supply is related to certain VAT-exempt transactions.

Generally, VAT is neutral within the chain of VAT entrepreneurs entitled to deduct input VAT, although the liability of VAT towards the tax authorities is incumbent on the VAT entrepreneurs. The VAT is ultimately borne by the final consumer, who is not allowed to deduct VAT.

VAT entrepreneurs that are registered for VAT purposes in Germany must calculate their VAT liability and file preliminary VAT returns to the German tax authorities on a monthly basis (on a quarterly basis for VAT entrepreneurs with a total annual VAT of more than EUR 1,000 and less than EUR 7,500 in the previous calendar year). Preliminary VAT returns must be filed electronically. The filing deadline for preliminary VAT returns is 10 days after the end of the reporting period (which also is the payment deadline). In addition to the preliminary VAT return filing procedure, VAT entrepreneurs must file an annual VAT return (filing deadline is end of May of the following year). In the case of cross-border transactions, further reporting obligations may apply for taxpayers (i.e. European Sales Lists and Intrastat declarations).

The German VAT Act provides for the creation of a VAT group, in which the fiscal parent company is considered the VAT entrepreneur and files a consolidated VAT return. A VAT group generally applies if a subsidiary is financially, organizationally and economically integrated into its parent company (fiscal parent). A financial integration generally exists if the shareholder as a fiscal parent owns more than 50% of the shares of the subsidiary (fiscal entity). An organizational integration exists where the fiscal parent ensures that its "business decisions" are implemented within the fiscal entity, i.e. the fiscal unity parent can control the fiscal entities. Economic integration exists if the subsidiary's business is closely related to the parent company's business. Intra-group transactions within the VAT group are deemed to be internal transfers and not taxable for VAT purposes.

Where a nonresident VAT entrepreneur carries out services that are taxable in Germany to other VAT entrepreneurs, the reverse charge mechanism applies, meaning that the recipient of the service (rather than the supplier) will be liable for VAT. Therefore, the supplier of the service only invoices the net amount with a note that the recipient is liable for VAT under the reverse charge mechanism. The recipient of the service declares the output VAT due as well as the input VAT (if the recipient is entitled to deduct input VAT) in the same tax return. The reverse charge mechanism also applies to other transactions, e.g. services rendered with respect to the construction or renovation of real estate or transactions subject to the real property transfer tax.

If a foreign company is not subject to corporate taxes in Germany, the Federal Tax Office will reimburse any turnover taxes deducted in Germany upon application (formal requirements apply). The mechanics of a VAT refund depend on the VAT laws of other countries. The tax authorities have published a list of countries that do not participate in the VAT-refund procedure.

5.2 Capital tax

Germany does not levy capital tax.

5.3 Real estate tax

Real estate transfer tax (RETT)

Germany levies RETT on the transfer of German real estate. Taxable transfers for the purposes of RETT are defined broadly and include transactions to address the circumvention of tax liability. Generally, a purchase agreement or any other legal transaction providing for the transfer of ownership of real estate triggers RETT, the same applies to transfers without such agreement (e.g. by operation of law in a statutory merger) and a number of other transactions. A direct or indirect transfer to new partners of 95% or more of interests in a partnership owning real property within a period of five years triggers RETT. Moreover, a direct or indirect acquisition of 95% or more (at once or in several tranches) of shares in a corporation or interests in partnership owning real property by one acquirer or an integrated group of acquirers also triggers RETT.

RETT depends on the federal state in which the real estate is located and amounts to a rate of 3.5% up to 5.0% of the consideration (or alternative tax base, i.e. the assessed value).

As from 1 January 2010, exceptions to RETT apply for certain intragroup restructurings.

Municipal real estate tax

The municipal authorities levy an annual real property tax on all immovable property regardless of whether the property is held as a business asset or for private use. The tax base is the assessed value of the real property, which is generally much lower than the market value. The effective tax rate depends on the intended use of the property and is calculated using a multiplier, which varies by municipality.

5.4 Transfer tax

See above under Real estate tax.

5.5 Stamp duty

No.

5.6 Customs and excise duties

Customs duties are levied on goods imported from outside the EU. Germany levies excise duties on various items, including tobacco, alcohol, petrol, oil and heating oil.

5.7 Environmental taxes

Taxes levied on oil, natural gas and electricity provide revenue used to lower employers' contributions to the state-run social security system.

5.8 Other taxes

No.

6.0 Taxes on individuals

6.1 Residence

An individual present in Germany for more than six months is considered a resident and is subject to German tax. Ownership of a house or apartment, or simply a physical presence in circumstances that suggest an intention to remain in Germany, also might trigger resident status. A simple relocation from Germany is enough to end tax residence, although taxation of German-source income may continue for a nonresident.

6.2 Taxable income and rates

Residents are liable to income tax on their worldwide income, while nonresidents are generally liable to tax only on certain German-source income.

Taxable income

German residents are taxed on all income from domestic and foreign sources derived from wages and salaries, capital gains and other types of income. Nonresident individuals are subject to income tax only on German-source income. In most cases, tax is generally levied by way of withholding at source, which is a final tax.

Income from private capital investments (see below) that has not been subject to the 25% final withholding tax must be declared in the taxpayer's income tax return and will also be taxed at a rate of 25%.

Gains from the disposal of immovable property are taxed within 10 years of acquisition (on gains exceeding EUR 600 during the tax year). However, the latter tax is dropped for residential buildings where the taxpayer has lived in the tax year and the two preceding years. Capital gains derived from the sale of non-business assets are tax-exempt if they are held long enough to be considered non-speculative (e.g. 10 years for real property, one year in most other cases).

Deductions and reliefs

Each resident taxpayer is entitled to a personal exemption of EUR 8,004 (EUR 16,008 for a married couple filing a joint return).

Individual taxpayers may take deductions for the following items:

- Premiums or contributions to private life, accident, unemployment, disability and health insurance up to a total of EUR 2,800 especially for self-employed individuals and EUR 1,900 especially for public servants and employees;
- Costs of professional training up to EUR 4,000 per year;
- Donations to registered charities, cultural or sports organizations;
- Alimony up to EUR 13,805 paid to a divorced partner; and
- Taxes paid to an officially recognized German church.

There also are deductions for children. Eligible taxpayers automatically receive a monthly child benefit of EUR 164 for each of the first two children, EUR 170 for the third child and EUR 195 for the fourth and each additional child. At the end of the year the tax authorities calculate whether the child benefit or child tax allowance is more advantageous for the taxpayer and automatically adjust the final tax. Nonresident taxpayers may claim the child allowances if they are subject to extended unlimited taxation (i.e. taxed as a resident in Germany).

Rates

The tax rates for resident individual taxpayers range from a minimum of 15% on income exceeding EUR 8,004 as from fiscal year 2010 to a top rate of 45% for income exceeding EUR 250,731 (EUR 501,462 for married couples). A solidarity tax of 5.5% of income tax is levied on personal income.

For individual shareholders, a "partial income" system applies, especially to capital gains. The sale of a shareholding of 1% or more in a corporation by a private individual will always be taxable

under the partial income system, irrespective of the holding period. Under the partial income system, only 60% of capital gains resulting from the sale of corporate shareholdings are included in a domestic individual shareholder's taxable income. Gains from the sale of non-business assets by individuals are not taxable if the assets are held long enough for the gain to be considered non-speculative (e.g. 10 years for real property).

A 25% (26.375%, including the solidarity surcharge) final withholding tax applies to private capital investment (e.g. resulting from the receipt of dividends or the disposal of minor shareholdings), regardless of the holding period. An allowance of EUR 801 (EUR 1602 for married couples) is granted. Gains from the sale of bonds and the sale of minor shareholdings (less than 1%) are also subject to the final withholding tax of 25% (26.375%, including the solidarity surcharge).

For certain capital income (e.g. dividends), the taxpayer may request taxation according to the "partial income" system provided the taxpayer holds directly or indirectly at least 25% of the shares in the relevant company (during the entire fiscal year) or holds at least 1% of the shares if employed by the company.

Nonresidents are taxed at a flat rate of 15% on income from free-lance journalism or writing activities, artistic works or sports as well as income from licenses, unless the income is exempt under an applicable tax treaty. A 30% withholding tax rate (31.7%, including the solidarity surcharge) applies to individuals who opt for the deduction of business expenses in calculating the withholding tax base.

6.3 Inheritance and gift tax

Inheritance and gift tax rates range from 7% to 50%, with various exemptions available. Business property/assets are valued at fair market value. Under certain conditions, the inheritance of business property can be 85% or 100% tax free.

6.4 Net wealth tax

Germany eliminated the net worth tax in 1997.

6.5 Real property tax

A real property tax is levied annually at the local level on immovable property owned by private individuals or companies.

6.5 Social security contributions

Employed individuals are required to make a contribution for pension, health and unemployment insurance. The employer bears 50% of the total contribution (see 7.2).

6.6 Other taxes

No.

6.7 Compliance

The tax year for individuals is the calendar year.

An individual can file a tax return to declare additional expenses and receive a refund. Tax returns are generally due by the end of May of the year following the tax year. The final tax is assessed after filing of the tax return. If an employee receives other income or if an individual receives income other than employment income, quarterly instalments and must be paid.

7.0 Labor environment

7.1 Employee rights and remuneration

There is no single law governing the individual and collective aspects of employment in Germany. Labor-management relations are primarily the result of collective bargaining between trade unions and employers.

The German civil code regulates employment contracts. The commercial code partly covers the employer-employee relationship and contains regulations on commercial agents.

German labor law is aligned with EU guidelines governing wage agreements. Within one month of hiring an employee, employers must put into writing the terms of the employment contract. Absent a choice-of-law clause in an employment contract, courts must apply German law whenever local personnel are employed, even if the employer is a foreign corporation. If the employee works abroad, the law of the country that governs the branch applies to the employee.

In any enterprise with more than five employees, workers may set up a works council to help resolve personnel issues (e.g. working hours, vacation schedules, salary and wage structures, payments for piece-work and incentive premiums). The works council must be consulted about any change that affects working conditions (e.g. changes in production methods and facilities). It also has an important voice in hiring, transferring or dismissing employees.

Workers' participation laws govern employee works councils and employee representation on the boards of directors. In a company with more than 100 employees, the works council may elect a business council, which discusses company decisions with management and then passes the information on to the works council. In a company with more than 500 but fewer than 2,000 employees, one-third of the seats on the supervisory board must be reserved for worker representatives. For companies with more than 2,000 workers, one-half of the supervisory board must comprise employee representatives (coal and steel industries have a similar but separate scheme). The policymaking supervisory board of large companies must comprise an equal number (10 in companies with more than 20,000 employees) of shareholder and labor representatives. The chairman of the supervisory board, who is elected by the shareholders, has a second vote in the event of a tie.

Working hours

Working hours in Germany are governed by law. Collective labor and works council agreements usually regulate the details. The normal working day is eight hours and can be extended to 10 hours, up to a maximum of 60 days per year or when the six-month average does not exceed eight hours per day. Certain exceptions apply to healthcare, restaurants, transport and agriculture. Shift work is permitted, and there must usually be an 11-hour break between shifts.

Collective labor and works council agreements are specific on shift work. Overtime pay starts at a 25% premium but is often higher. Employers may choose to pay higher overtime pay or to give workers additional time off instead. Employees with executive functions are not covered by the law on working hours and usually do not receive overtime pay.

The minimum annual vacation period is 24 working days for full-time employees (five-day week). On average, the workforce is entitled to an annual vacation of 30 days, by collective labor agreement.

7.2 Wages and benefits

German wages often are set by collective labor agreements. Wages in foreign-owned companies are similar to those in domestic firms.

Germany does not have a general minimum wage - in principle each industry agrees on minimum wages in its collective bargaining negotiations. Some collective labor agreements have been declared universally binding by the government and some industries face statutorily regulated minimum wages (e.g. construction, cleaning, postal services, security, mining, nursing, large-scale laundry and waste management).

Wages and salaries vary by location, seniority and gender of the employee. Despite a law on equal pay and opportunities, men often earn 10%–30% more than women for the same job.

Pensions

A privately funded and managed element has been added to the pay-as-you-go pension scheme and tax advantages are granted to payments into the state pension system. The Personal Pension Plan Act encourages private-sector employees, who are entitled to compulsory social retirement benefits (state pension), to build up individual-asset-backed pension plans. Personal pension plan contributions are tax exempt, within the limits specified under the pension plan legislation. The Pension Law gradually exempts payments into the state pension fund from tax, but it taxes pension payouts.

Germany's comprehensive state pension scheme requires compulsory pay cherub deductions (see below).

Most large German companies offer voluntary company pension plans that supplement the state retirement-pension scheme.

The legal retirement age is 67 for men and women. Under certain conditions retirement at 60 is possible for unemployed and women born before 1952.

Social insurance

Wages and salaries constitute only a part of the cost of labor. Mandatory social insurance contributions for employers and employees combined reach on average 40% of gross income below annually defined ceilings. Typically, employers and employees each pay half of the charges.

Non-wage worker costs include the following:

- **Compulsory health insurance:** Compulsory health insurance covers employees and their families. The numerous public sector health insurance schemes collect monthly contributions of 15.5% gross monthly pay up to EUR 4,125. All workers with annual salaries lower than EUR 49,500 must be enrolled in the compulsory scheme. The employer pays 7.3% and the employee 8.2% of gross monthly pay up to the social security contribution ceiling of EUR 4,125 per month.
- **Voluntary health insurance:** Salaried workers whose income exceeds the ceilings for compulsory health insurance for three calendar years in a row either pay voluntary contributions to a public sector health insurance scheme or choose private health insurance. Privately insured persons may claim from their employer a contribution toward their premium equal to that required for the compulsory health insurance.
- **Nursing-care insurance:** Wage and salary earners who have children pay 1.95% of gross monthly income up to EUR 4,125. Employers and employees each pay one-half of the contributions. Workers and employees without children pay 0.25 percentage points more, an amount that is not matched by higher contributions from their employers. This does not apply to persons: under 23 years of age, born before 1 January 1940 or currently drafted in military or civil service. If the employee has opted for private health insurance, he/she must still enroll in the compulsory nursing-care insurance, but the account will be administered by the private carrier.
- **Accident insurance:** Accident insurance covers employees for accidents incurred on the job or while travelling to or from work and is financed entirely by employer contributions, based on gross wages and salaries. The tax-exempt contribution amounts to about 2% of gross wages and salaries, but varies according to the danger category in which a company is classified.
- **Unemployment insurance:** All wage and salary earners pay 3% of gross income up to a monthly earnings maximum of EUR 5,500 (EUR 4,800 in the former Eastern states). Employers and employees each pay half.
- **Pension insurance:** The statutory pension scheme calls for contributions of 19.9% of gross monthly income up to EUR 5,500 (EUR 4,800 in the former Eastern states). Employers and employees each pay half.

Employees coming from outside Germany normally are subject to social security contributions. Very often, however, a social security agreement exists between Germany and the employee's home country that will allow the employee to remain in his/her home scheme for a limited number of years under certain conditions. Germany has such agreements with 45 countries. The home country employer must file an application for a certificate of coverage (form E 101 in Europe) to request the exemption from German social taxes. Not all agreements cover all branches of social coverage, however, so it may not be possible to obtain complete exemption.

7.3 Termination of employment

The law governing dismissals protects from dismissal those workers hired after 1 January 2004 who work for companies with a workforce of 10 or more, unless there is specific justification. Dismissal notice periods vary according to the length of the labor contract. Within the probation period of up to six months, dismissal is possible with two weeks' notice and for no specific reason. Otherwise, the minimum notice period is four weeks. This notice period expands to two months after five years of employment and to seven months for contracts of longer than 20 years' duration. Members of works councils may be dismissed only in grave instances. Women may not be dismissed during their pregnancy and within four months of giving birth.

Employers must inform the works council of planned layoffs. Trade unions enforce these rules rigorously. In practice, companies wishing to lay off staff are usually forced to make generous redundancy agreements with the works council or the individual. The common severance pay starts at 50% of a monthly gross salary for every year of job tenure and can range as high as 12 months' salary (15 months for older employees with at least 15 years' job tenure).

Notice periods may be modified, within limits, in collective-bargaining agreements. The rules for firms employing fewer than ten persons are considerably less stringent.

7.4 Labor-management relations

Trade unions are organized by industry. Most come under the umbrella of the German Trade Union Federation (DGB). Some white collar workers form their own professional organizations and negotiate their salaries outside of the traditional trade union structure.

Union officials and employers' associations negotiate on a regional level. One region drafts a pilot agreement, which is then adopted nationwide, perhaps with minor changes. There are separate contracts for pay and other conditions (e.g. shifts and vacations). Once agreed, collective labor agreements traditionally apply to an entire industry nationwide.

German labor law requires arbitration and approval of a strike by 75% of union members. The law limits the reasons for which strikes may be called and provides for penalties for infractions. Under German law, strikes may not be called until negotiations break down. Nevertheless, the Federal Labor Court has upheld "warning strikes" (work stoppages and demonstrations) during negotiations and the right of apprentices to join strikes and work stoppages. The Social Law blocks federal compensation for workers on short time or laid off because of a strike in another part of the country. The legislation provides for disputes to be settled by a "neutrality committee," with the right of appeal to the Federal Labor Court.

7.5 Employment of foreigners

All nationals of the EEA enjoy the right to live and work in Germany.

Direct entry with a subsequent long-term stay is legally impossible for nearly all non-EEA foreign workers who do not arrive with a job offer from a company in Germany. Individuals who want to work in Germany must first apply for a visa at German embassies in their home countries, unless employer-specific "facilitations" apply. (Facilitations might apply for senior executives or intra-company transfers.) To obtain work permits from the local authorities, prospective employees must present valid residence permits and completed work permit applications signed by the future employer. Because of continued high unemployment, non-EEA nationals are given work permits only under the "green-card program" or if they or their employer can prove that they are indispensable (e.g. long experience with the firm or industry) and if a local job seeker cannot fill the post. Work permits are not transferable to other jobs or firms.

8.0 Deloitte International Tax Source

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