



cutting through complexity

Global Transfer Pricing Review

Germany

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TAX



Germany



KPMG observation

Transfer pricing still is one of the highest priority issues for German tax authorities and is receiving increased attention and discussion during German tax audits. In KPMG's experience, German tax auditors often put forward a case of insufficient or incomplete transfer pricing documentation in order to shift the burden of proof to taxpayers and try to achieve significant transfer pricing adjustments by way of an estimate. Other preferred audit targets currently include outbound licensing of brand names and trademarks as well as debt pricing and cash pools.

The Organisation for Economic Co-operation and Development (OECD) authorized approach, stipulated in the new Article 7 of the OECD Model Tax Convention and its commentary was incorporated into German tax law in 2013. These fundamental changes with regard to transfer pricing for permanent establishments were supplemented by additional decree in 2014.

As of 2008, the German tax authorities are allowed to aggressively audit business restructuring cases.

The Base Erosion and Profit Shifting (BEPS) initiative fits into the German tradition of developing measures against profit shifting. Germany has strongly advocated the adoption of the BEPS Action Plan and played a decisive role in the shaping of the actions and supports all of the 15 actions envisaged by the OECD. The German Federal Ministry of Finance is focusing on four key items: digital economy, hybrid mismatch arrangements, prevention of treaty abuse and harmful tax competition.

Transfer pricing study snapshot

The purpose of a transfer pricing study

	Applicable
Legal requirements	●
Protection from penalties	●
Reduce risk of adjustment	●
Shifts burden of proof	●

Basic information

Tax authority name

Federal Ministry of Finance
(Bundesministerium der Finanzen – BMF);
Federal Tax Office (Bundeszentralamt für
Steuern – BZSt).

Citation for transfer pricing rules

German Foreign Transactions Tax Act
(Außensteuergesetz – AStG) Section 1,
General Tax Code (Abgabenordnung –
AO) Section 90 Para. 3 and Section 162
Para. 3 and 4, Corporate Income Tax
Act (Körperschaftsteuergesetz – KStG)
Section 8 Para. 3.

Effective date of transfer pricing rules

The legal basis for the determination of intra-group transfer prices has recently changed in Germany since the revision of Section 1 of the Foreign Transactions Tax Act in 2013. The 2013 Tax Act introduces changes which

clarify the rules for cross-border profit allocation that apply to various legal structuring options such as corporation, partnership, and permanent establishments. Documentation requirements were introduced in 2003 and penalties in 2004.

What is the relationship threshold for transfer pricing rules to apply between parties?

The taxpayer holds direct or indirect ownership of 25 or more percent in the related party, or has direct or collateral possibility to exert a dominating influence to the related party; a third party holds a share of 25 percent or more in the taxpayer and the related party or exerts indirectly or collaterally a dominating influence.

What is the statute of limitations on assessment of transfer pricing adjustments?

In general, four years from tax filing year-end, but the respective tax rules and provisions are much more comprehensive.

Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be submitted to the revenue authority on an annual basis (e.g. with the tax return)?

No. Disclosures related to transfer pricing are not required to be submitted to the revenue authority on an annual basis, e.g. with filing a corporate income tax return. The transfer pricing documentation for so-called extraordinary transactions has to be prepared within six months after the business year-end in which the respective transaction took place. However, it is strongly recommended to prepare contemporaneous transfer pricing documentation.

In general, the transfer pricing documentation for all types of intragroup transactions has to be provided to the revenue authority upon request, typically for the purposes of a tax audit.

What types of transfer pricing information must be disclosed?

No specific disclosure is not required. If management identifies incorrect transfer pricing after filing the tax return, this needs to be indicated and corrected without delay.

What are the consequences of failure to submit disclosures?

Not applicable.

Transfer pricing study overview

Can documentation be filed in a language other than the local language? If yes, which ones?

Yes. Any living language, in practice usually English.

When a transfer pricing study is prepared, should its content follow Chapter V of the Organisation for Economic Co-operation and Development (OECD) Guidelines?

Yes, for all transactions. The manner, content and extent of documentation in a German transfer pricing study is determined by the "Decree-Law in the spirit of Sec. 90(3) of the General Tax Code (GTC)"; which generally follows Chapter V of the OECD Guidelines.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

Transfer pricing methods

Does your country follow the transfer pricing methods outlined in Chapter II of the OECD Guidelines? If exceptions apply, please describe.

Yes.

Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? And if so, how many days?

Yes, 30 days.

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? Please explain.

Taxpayers need to provide documentation within 60 days upon request in a tax audit; for extraordinary

transactions the deadline is 30 days upon request in a tax audit.

If an adjustment is proposed by the tax authority, what dispute resolution options are available?

In principle, the taxpayer can choose to litigate, a strategy rarely chosen because of the lack of economic experience at German tax courts leading to unforeseeable results. The taxpayer can also choose to submit an application for a mutual agreement procedure under Article 25 of the OECD Model Tax Convention at the Federal Tax Office. There is also the possibility of using the complaints system or the European Union (EU) arbitration procedure.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

Yes. Section 162, Paragraph 4, General Tax Code provides that in the absence of materially complete documentation the higher of either 5,000 euros (EUR) or a fraction of five percent to 10 percent of the transfer pricing adjustment made has to be assessed. Therefore, a penalty cannot be removed if no documentation exists, but the exact amount of the penalty is subject to the tax authorities' discretion which may depend on the taxpayer's degree of compliance or the nature of the transfer pricing adjustments. The same applies for penalties sanctioning late filing (maximum surcharge of EUR1 million, with a minimum of EUR100 for each day after the 30/60 days time limit is exceeded) and the tax administration's ability to use the full arm's length range to the detriment of the taxpayer in case no useful documentation exists.

To what extent are transfer pricing penalties enforced?

Always.

What defenses are available with respect to penalties?

With regard to cross-border transfer pricing issues, preparation of comprehensive transfer pricing documentation is required to avoid penalties and surcharges. However, if penalties are assessed they can occasionally be negotiated with local tax authorities to a lower level.

What trends are being observed currently?

German tax auditors often assume a case of insufficient or incomplete transfer pricing documentation in order to make significant transfer pricing adjustments to the taxable income by way of an estimate. Particular attention is currently being paid to the outbound transfer of functions and risks, cash pooling, outbound brand licensing and to permanent establishments.

Special considerations

Are secret comparables used by tax authorities?

Yes, occasionally, but they have lesser evidence value in court.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

No, there is no legal requirement to have local comparables. However, German tax authorities prefer local comparables in benchmarking studies. Benchmarking studies that have no local comparables are sometimes challenged with regard to comparability.

Do tax authorities have requirements or preferences regarding databases for comparables?

There are no legal requirements to use any particular database. It is most common to use the Amadeus database for pan-European comparables searches, which is published by Bureau van Dijk. The German tax authorities have licensed this database and are using it. The tax authorities require that the information from databases is verified through internet research, i.e. to determine the comparability of a certain company; it is insufficient to rely only on the information which is provided by the database. The Dafne database with German comparables and the Orbis database for non-European comparables searches might also be used.

Does the tax authority generally focus on the interquartile range in a TNMM analysis?

Yes, always.

Does the tax authority have other preferences in benchmarking? If so, please describe.

It is not unusual that a German tax auditor would dispute the reliability of the external data available for application of the TNMM. In such cases they may resort to other third party (often internal) or reject the documentation as insufficient and try to make an adjustment based on an estimate.

What level of interaction do tax authorities have with customs authorities?

Low interaction with customs authorities. The customs service occasionally requests transfer pricing documentation.

Are there limitations on deductibility of management fees beyond the arm's length principle?

Yes, some. In general, management fees are deductible assuming the services were rendered to the benefit of the service recipient and the pricing was arm's length (benefit test). However, general domestic deductibility limitations may apply, e.g. in respect of stock option costs, entertainment costs or remuneration of supervisory boards.

Are management fees subject to withholding?

No.

Are there limitations on the deductibility of royalties beyond the arm's length principle?

No.

Are royalties subject to withholding?

Yes.

Are taxpayers allowed to file tax return numbers that differ from book numbers?

Yes. Tax returns need to reflect taxable profits based on arm's length pricing.

If the taxpayer's statutory book numbers do not reflect arm's length prices – in particular if the German profits were below an arm's length level – the taxpayer is required to make the appropriate adjustments for tax purposes. In practice, a deviation of statutory book numbers from tax return numbers is likely to lead to greater scrutiny by the tax auditor.

Other unique attributes?

None.

Tax treaty/double tax resolution

What is the extent of the double tax treaty network?

There is an extensive double tax treaty network. As of 1 January 2015, about 100 double tax treaties with other countries were in place.

If extensive, is the competent authority effective in obtaining double tax relief?

In most cases.

When may a taxpayer submit an adjustment to competent authority?

Once double taxation becomes imminent which is usually considered to take place at the point in time the tax audit report is issued by the auditor.

May a taxpayer go to competent authority before paying tax?

Yes.

Advance pricing agreements

What APA options are available, if any?

Bilateral, multilateral.

Is there a filing fee for APAs?

Yes. An application fee of EUR20,000 and a fee of EUR15,000 for a renewal of an APA. Moreover, in case of a change in the application, a fee of EUR10,000 is applicable. When the transaction volume covered by an APA is less than EUR5 million for the transfer of goods

and less than EUR500,000 for other cases, the aforementioned fees are reduced to EUR10,000, EUR7,500, and EUR5,000.

Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

No.

Are there any difficulties or limitations on the availability or effectiveness of APAs?

No. The German tax authority actively welcomes and supports APAs for transfer pricing purposes. Multinational companies actively use the APA program in their transfer pricing policies.

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