



BDO Seidman, LLP
Accountants and Consultants

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Issue:

German Federal Tax Court Expands Availability of Treaty Benefits

International Tax Alert

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Issue:

In a recently published decision, the German Federal Tax Court (“Bundesfinanzhof” or “BFH”) overturned its long-standing opinion that a typical foreign holding company (whose shareholders are residents of another country) should generally not be entitled to treaty reduced withholding tax rates on dividends received from a German subsidiary. Essentially, the BFH has now adopted a more generous view on foreign holding companies’ eligibility for benefits under German income tax treaties and the EU parent-subsiidiary directive.

Affecting:

U.S. (and other non-German) multinationals and investors owning shares of German subsidiaries through third-country holding companies. A refund of German dividend withholding taxes paid could be available.

Details:

The case involved a multinational group whose ultimate owners were residents of the United States, Australia and Bermuda. The group’s European (including German) operating entities were held by a Dutch holding company (BV). When the German subsidiary paid a dividend to the Dutch holding, the tax authorities denied the latter the benefits of the EU parent-subsiidiary directive, referring to the BFH’s previous reading of Sec. 50d (III) of the German Income Tax Code. Sec. 50d (III) states, in general, that a foreign entity (here: the BV) is not entitled to treaty or directive benefits if it is owned by persons who themselves are not entitled to such benefits, if there is no business reason for interposing the entity and if it has no business activities of its own (functionless base company). In the past, a holding function was generally not deemed sufficient to overcome this test. German withholding tax was imposed at the rates applicable to residents of the United States, Australia and Bermuda.

Details (continued...):

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The BFH has now ruled that the benefits under a treaty or the EU parent-subsidiary directive can indeed be granted to a holding company even if it has no employees, premises or office equipment. The court, in the case at hand, observed that the Dutch holding company existed for long-term organizational and strategic reasons, that it held other subsidiaries in addition to the German one and that the group had significant business activities in the country where the holding was located (the Netherlands). All this led the court to the conclusion that the holding was not a mere conduit and thus entitled to the 0 percent withholding rate under the EU parent-subsidiary directive.

It appears that most holding companies should be able to meet these standards. If dividends were subjected to German withholding tax under similar circumstances, a refund should be available, subject to the statute of limitations.

To learn more about the possible impact of the BFH decision on your specific fact pattern, we would welcome your call.

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