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Accountants and Consultants

Subject:

German Government Proposes Significant Expansion of Anti-Abuse Rules

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International Tax Alert

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On July 18th, the German Ministry of Finance proposed two law changes that would coincide with the 2008 Tax Reform. The first proposal involves the tightening of the general anti-abuse rule of section 42 of the General Tax Code (GTC). The second proposed change would introduce a new disclosure requirement for certain types of international tax planning structures.

Date/Timing

Subject to enactment of the draft bill, these provisions would take effect from January 1, 2008.

Affecting

All taxpayers doing business in Germany.

Summary of Proposals

Revision of the General Anti-abuse Rule (Section 42 of the GTC)

The new wording of the rule suggests that in order for the legal operations structure to be deemed not abusive, the taxpayer has to demonstrate that the tax advantages resulting from the proposed structure were not the primary business purpose. The “significant” non-tax reason would have to be proven by a third-party test. In the instance where it is difficult to demonstrate, the taxpayer would have to obtain the consent from the Federal Ministry of Finance. If the authorities believe there is an abuse, they can disregard the structure chosen by the taxpayer.

New Disclosure Obligation for International Tax Planning

It is proposed that if the following two conditions are present, the disclosure notification would have to be provided to the German Tax authorities:

- (1) The tax planning structure leads to a fiscal deficit in Germany;

(2) And where:

- a. an asset is recorded in several jurisdictions;
- b. the same income is allocated to several taxpayers or to several permanent establishments of the same taxpayer;
- c. an entity is classified as a taxpayer in one jurisdiction, but not the other (specifically mentioned the U.S. check-the-box election);
- d. an entity is treated as a dual resident;
- e. tax treaty provisions are interpreted or applied differently by treaty partner countries;
- f. payments are characterized differently by different countries; or
- g. the same expenses can be deducted in different jurisdictions.

The “promoter” (e.g. domestic or foreign professional services provider, lawyer, or financial advisor who advised/sells tax planning ideas) of the tax planning structure would be required to notify the Federal Fiscal Agency (FFA) of the proposed plan, the expected tax savings, the legal basis, and the number of clients affected by this proposal (client identities can remain anonymous) within 10 days from the end of the month in which the promoted structure was first introduced. Consequently, the FFA would assign an identification number to the structure, which would have to be disclosed (by citing the identification number) by taxpayers using this planning structure.

The proposed disclosure obligation would generally apply only in cross-border situations.

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