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## The Anti-Tax Evasion Act

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The German Bundestag (German Parliament) has adopted the Anti-Tax Evasion Act (Act for the Combatting of Tax Evasion – *Gesetz zur Bekämpfung der Steuerhinterziehung*, Federal Law Gazette 2009 Part I No. 48, p. 2302), which entered into full force and effect on January 1, 2010. With this Act, the legislator has extended the scope of the obligations to co-operate and provide evidence under tax law for individuals in cross-border situations, has imposed the denial of favorable tax law provisions in the case of a failure to comply and has stipulated the permissibility of an estimation of the tax base in unclear circumstances.

With this Act, the German legislator authorizes the German Federal Government not to apply certain provisions under tax law, in whole or in part, provided that

- increased **obligations to produce evidence** on the part of the taxable person are not fulfilled, and
- the case concerns **business relationships with persons or associations of persons** in states or regions that do not accept the OECD standards regarding the exchange of information in tax matters.

In addition, the co-operation and record-keeping obligations for natural persons in respect of foreign capital investments are extended significantly and the investigation rights of the financial authorities are also expanded.

With the Act, the Federal Government effectively refers to measures adopted by 17 OECD member states in the course of a conference in October 2008 in Paris.

The following is a description of the new legal situation.

### I. Direct Effects Only by Means of a Government Rule from January 1, 2010

The Anti-Tax Evasion Act has entered into force already on August 1 2009. However, most of the new provisions are only to be applied as of the 2010 assessment period, pursuant to the already enacted government rule (so-called Anti-Tax Evasion Rule (*Steuerhinterziehungsbekämpfungsverordnung* – *SteuerHBekVO*, Federal Law Gazette 2009 Part I No. 60 p. 3046).

### II. Amendments to Income Tax Law

#### 1. Deduction of operating expenses / income-related expenses

Where involved parties are resident in a state that has not committed itself and is not prepared voluntarily, either, to provide information in accordance with the OECD standards, the Federal Government is authorized, in the future, to subject the granting of the **deduction of operating expenses / income-related expenses** to the condition of the obligations to co-operate and to provide evidence being fulfilled. The relevant reference in this regard is Art. 26 of the OECD model convention on double taxation. The OECD (= Organization for Economic Co-operation and Development) is an international organization of 30 member states including, amongst others, more than 20 EU states.

The obligations to co-operate and to provide evidence that are to be stipulated in the future government rule may consider the following aspects / issues:

- Are agreements between related parties (see the side note below) adequate within the framework of their business relationship as defined in the Foreign Tax Relations Act?
- Is the allocation of profits between business divisions without legal capacity adequate?
- Has the taxable person authorized the financial authorities to assert on behalf of such taxable person, in and out of court, potential claims for the provision of information against the **financial institutions specified by the financial authorities?**
- Fulfillment of obligations to keep records and provide evidence otherwise only applicable to related parties, also in the case of business relationships between persons who are not related parties. Pursuant to the Anti-Tax Evasion Rule (*SteuerHBekVO*), the taxable person is obliged, in particular, to prepare records of the following in a timely manner:
  - Nature and extent of business relationships;
  - Agreements and agreed contractual provisions, as well as their amendment;
  - the intangible assets which the taxable person uses or is allowed to use in the course of the business relationships;
  - the functions and risks assumed by the parties involved in the business relationships, as well as related alterations;
  - the auditors employed;
  - the business strategies chosen;
  - the relevant market and competition environment;
  - the parties holding interests in the business partner.
- This obligation to prepare records does not apply only if the aggregate amount of the considerations for deliveries and performances under a business relationship do **not exceed EUR 10.000** in a financial year.

Side note: Related parties

The persons who are related parties pursuant to § 1 para. 2 Foreign Tax Relations Act (*Außensteuergesetz – AStG*) can be **natural persons or legal entities**, such as a GmbH (limited liability company) or Aktiengesellschaft (stock corporation). Pursuant to this provision, not only spouses are related parties, but also other relatives, friends and, in some cases, acquaintances. But also a shareholder holding 25 % or more in a corporation is a related party of such corporation as defined in § 1 para. 2 AStG.

**2. Relief for foreign companies**

**Foreign companies** are only granted relief in the form of an **exemption from capital gains tax** if in respect of the foreign company the **identity** of those **natural persons** is known and plausible who are directly or indirectly holding **more than 10 %** in such company. Pursuant to the Anti-Tax Evasion Rule (*SteuerHBekVO*), the name and domicile of such natural person is to be disclosed.

The background for this is the following: Pursuant to **§ 50d EStG** (*Einkommensteuergesetz – German Income Tax Act*), it is intended to assert the German capital gains tax especially in cases where the German authority to impose taxes is restricted or excluded by a double taxation convention. However, in certain cases, a taxable person may either request to be **exempted from capital gains tax** or demand **reimbursement** of the tax withheld. However, the exemption or reimbursement **may not take place** if a taxable person only achieves fulfillment of the requirements of such relief by formally involving an intermediate foreign company.

Under the old law, § 50d EStG already restricted the right to exemption or reimbursement: For example, these rights were not granted in cases where the shareholders of a foreign company were natural persons who would not have been granted these rights if they had held the assets of the foreign company directly and if there were no economic or other relevant reasons for the involvement of a foreign company.

With the Anti-Tax Evasion Act, the legislator now adopts more strict requirements for a granting of relief, by rendering the relief conditional upon the **proof of the identity** of the natural persons who are holding a **substantial (more than 10 %) interest**.

Eventually, the intention is to prevent the abusive utilization of advantages in cases where companies are involved that are domiciled in countries which do not take part in the exchange of information with the Federal Republic of Germany that is usually provided for in double taxation conventions.

**3. Flat tax on capital income (Abgeltungsteuer) and partial income taxation method (Teileinkünfteverfahren) in the case of foreign companies**

Where foreign companies generate income which leads to the application, as a general rule, of the flat tax or the partial income taxation method in Germany, the tax authority is authorized to link the application of the relevant provisions to the

**condition of a „power of attorney for tax matters“.**

With such power of attorney, **the financial authorities** are to be **authorized by the taxable person** to assert on behalf of such taxable person, in and out of court, **potential claims for the provision of information** against the financial institutions precisely specified **by the financial authorities**.

This way the financial authorities are to be granted access to bank information which otherwise could not be obtained because of the refusal of an exchange of information between Germany and the country concerned.

#### 4. Exceptions

The obligations to provide evidence and to co-operate described under Nos. II. 1 to 3 above are not to be applied, if

- a convention exists between the Federal Republic of Germany and the country concerned which provides for the granting of such information as is required for the purpose of taxation in Germany. Typically, this could be a double taxation convention in accordance with the OECD model convention on double taxation;
- even without such convention, the country concerned provides the necessary information to an extent meeting the requirements of the OECD model convention on double taxation, or
- the country concerned indicates its willingness to grant information, whereas such willingness may be expressed by conducting specific discussions with the Federal Republic of Germany regarding the conclusion of a bilateral agreement on the exchange of information in tax matters.

#### III. Amendments to the Law of Taxation of Corporations (in particular, GmbH, AG)

Pursuant to a provision of the German Corporation Tax Act (Körperschaftsteuergesetz – KStG) (§ 8b para. 1 KStG), dividend payments received, for example, by one corporation from another, are almost entirely exempt from taxation at the level of the corporation. Pursuant to § 8b para. 2 KStG, similar provisions apply to profits generated by a corporation from the disposal of its interest in another corporation. In both cases, the tax exemption amounts to 95 % of the dividend payments or disposal profits.

Pursuant to the Anti-Tax Evasion Act and the Anti-Tax Evasion Rule, **these two tax exemptions** may be rendered conditional upon the fulfillment of special obligations to provide evidence and to co-operate.

Again, the validity of such conditions requires in this case that involved parties are resident abroad and, thus, cannot easily be included in the investigation of the relevant facts from a tax perspective. In addition, it is a requirement that the country concerned does not provide information in accordance with the OECD standards or refuses any willingness to do so.

The specific obligations to provide evidence and to co-operate have a content similar to the one described under No. II. above.

Eventually, it is the intention of the legislator also in the case of this provision to provide an incentive for the country concerned to enter into a double taxation convention with Germany on the basis of the OECD standards.

#### IV. Amendments to the German Tax Code (Abgabenordnung)

##### 1. Stricter obligations to provide information

Pursuant to § 90 of the German Tax Code (Abgabenordnung – AO), taxable persons are under an obligation in Germany to co-operate in the investigation of the facts that are relevant from a tax perspective. This obligation is fulfilled by the complete and truthful disclosure of the facts that are relevant for taxation. This applies, in particular, where there are factual links to foreign countries.

Pursuant to the Anti-Tax Evasion Act, the tax authorities may (§ 90 para. 2 sent. 3 AO, as amended) request the taxable person

- to verify the correctness and completeness of the information provided **by means of an affidavit;**
- **to authorize the financial authorities to assert on behalf of such taxable person, in and out of court, potential claims for the provision of information against the financial institutions specified by the financial authorities!**

In Germany, any person assuring the correctness and completeness of facts in an affidavit in spite of knowing that these facts are incorrect or incomplete, in whole or in part, commits a criminal offence.

The financial authorities may request both measures, if

- the taxable person has business relationships with financial institutions in a country with which no double taxation convention on the basis of the OECD model convention has been concluded;
- the country concerned does not provide information to the extent to which information is usually provided under the double taxation convention on the basis of the OECD model convention, or
- the country concerned does not indicate any willingness at all to grant information, i.e. if such country does not even conduct any discussions with Germany regarding the conclusion of a double taxation convention.

If the taxable person violates its co-operation obligations under § 90 para. 2 sent. 3 AO, there will be a – rebuttable – presumption to the effect that he/she **has taxable income in these countries** or, respectively, that **his/her income is higher** than the income declared. This provision enables the financial authorities to conduct an **assessment of the tax base**. If the taxable person then wishes to contest this tax assessment in the course of the taxation proceedings, he/she is therefore forced to become actively involved.

## 2. Stricter record-keeping obligations

Where a taxable person generates income from employment, investments, from rental and leasing or other taxable private income pursuant to § 22 EStG and **this income, on aggregate, exceeds Euro 500,000,- in a calendar year**, the following has to be observed:

The **records and documents** pertaining to this income (this includes the income and the income-related expenses) have to be **kept for six years**.

Where spouses file a joint tax return, the case of each spouse will be looked at individually. There will be no addition of the spouses' income. Accordingly, it has to be examined for each **spouse** individually whether the obligations regarding the keeping of records apply.

The record-keeping obligation comes into existence, for the first time, in the calendar year following the calendar year in which the aggregate amount of the positive income generated from the types of income stated above exceeds the amount of Euro 500,000.

**Irrespective** of these requirements, **the financial authorities can obligate a taxable person to keep** the relevant tax documents if he/she has failed to fulfill his/her co-operation obligations under

§ 90 para. 2 sent. 3 AO, as amended, i.e. if he/she either has not issued an affidavit or has refused to grant the power of attorney requested by the financial authorities.

According to the legislative history, the stricter record-keeping obligation is supplemented, in addition, by the right of the financial authorities, following the request vis-à-vis the taxable person to keep the documents that are relevant from a tax perspective, to conduct a **tax field audit**.

**Caution: However**, according to the wording of the new provision in the Anti-Tax Evasion Act, the tax authorities are **already** entitled to **conduct a tax field audit, as soon as** a taxable person **exceeds**, for example, **the income threshold of Euro 500,000,-** and is subject to the six-year record-keeping obligation under statutory law. In that case, according to the wording of the statute, a tax field audit may be conducted, even if the taxable person has issued a respective affidavit and has granted in the polls attorney for the benefit of the financial authorities.

## V. Miscellaneous

To date, it is the responsibility of the customs authorities to conduct cash spot checks for the purposes of **combating money laundering and the financing of terrorism**. However, in the view of the legislator, the restriction to these purposes is too narrow, since even in the case of obvious offences, such as tax evasion or fraud to the detriment of social security agencies, the customs authorities are unable to pursue this any further.

Therefore, the legislator clarifies with the Anti-Tax Evasion Act, by means of an amendment of § 1 of the Customs Authorities Act (*Zollverwaltungsgesetz*), that in the future the customs authorities may also become involved in the course of its spot check activities if it suspects a case of tax evasion, a tax offence or fraud to the detriment of social security agencies. So far, the customs authorities were not generally entitled to take any measures in these cases.

## VI. Outlook

The new law has entered into force on January 1, 2010. It is intended to serve as a means and incentive to encourage other countries to enter into an obligation bilaterally to provide information in tax proceedings. Already at this stage, numerous countries (including, for example, Andorra, Monaco, Liechtenstein, Luxembourg, Austria, Switzerland,

Costa Rica, Uruguay, Hong Kong, Macao, Singapore, Malaysia) have declared to be willing to cooperate on the basis of the OECD standards. Therefore, the taxable person will have to review whether his or her business relationships concern countries which fulfill the requirements of the Anti-Tax Evasion Act and the Anti-Tax Evasion Rule (SteuerHBekVO). Otherwise, more stringent tax law

provisions might apply. However, the new **obligations to keep and prepare records** will apply **independently from any foreign element** to all taxable persons, if they exceed the stipulated annual income threshold (EUR 500,000).

This publication merely serves as a basis for discussion and is no substitute for legal advice. We would be pleased to provide you with additional information or to render advice with regard to a specific situation.

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