



Rights granted abroad – Will withholding tax still be due in Germany after all?

BMF performs another U-turn with its government bill of 20 January 2021 and now intends to uphold limited tax liability

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For months now the treatment of licence fee income generated in Germany under licence agreements concluded between foreign companies where the right granted is merely listed in a public register in Germany has been causing great uncertainty among companies. And there is no end in sight. While the Federal Ministry of Finance (Bundesfinanzministerium; BMF) abandoned the position adopted in its **circular dated 6 November 2020**, proposing just a few days later to include a provision removing limited tax liability for such cases in the **draft bill of 19 November 2020**¹ for an Act to Modernise Relief from Withholding Taxes (AbzStEntModG) (for more information see our **Client Alert of 30 November 2020**), the revised **government bill of 20 January 2021**² has now been published, in which the proposed removal of the limited tax liability has been deleted again. However, the BMF intends to offer relief for certain DTT cases in a **new administrative circular dated 11 February 2021**. It seems, though, that the last word on this matter has not yet been spoken.

¹ Draft bill for an Act to Modernise Relief from and Issue Certification for Withholding Taxes (*Referentenentwurf für ein Gesetz zur Modernisierung der Entlastung von Abzugssteuern und der Bescheinigung von Kapitalertragsteuer*) dated 19 November 2020.

² Government bill for an Act to Modernise Relief from and Issue Certification for Withholding Taxes (*Regierungsentwurf für ein Gesetz zur Modernisierung der Entlastung von Abzugssteuern und der Bescheinigung von Kapitalertragsteuer*) dated 20 January 2021.

Background

Germany levies withholding tax on income generated by non-residents from licence rights. In this context, it is sufficient under the wording of the law that, where rights are granted, the relevant right is (also) registered in a public register or list in Germany (cf. section 49 (1) no. 2 (f) or no. 6 of the German Income Tax Act (*Einkommensteuergesetz*; **EStG**)). There is no requirement for any stronger link to Germany; the same applies in the event such rights are disposed of.

In its circular dated 6 November 2020, the BMF confirmed its opinion that these cases were subject to limited tax liability and, consequently, that the non-German party owing the fees was obliged to retain withholding tax. This also covers scenarios in which, owing to a double tax treaty (DTT), ultimately no tax liability arises in Germany. In addition to suffering a loss of liquidity, the companies affected also face a considerable administrative burden.

Shortly afterwards the BMF appeared to have relented, when it proposed in the draft bill for the *AbzStEntModG* dated 19 November 2020 to remove the limited tax liability where the rights granted are merely registered in Germany. In the explanatory memorandum, the BMF accepted that a taxation of the described cases was "not appropriate" and would not meet the legislature's intention. A "substantial link to Germany" would therefore be required in order for limited tax liability to be triggered, such as the use of the right in question in a permanent establishment of the licensee in Germany.

Government bill dated 20 January 2021: Taxability where a right is merely registered in Germany has been retained

Surprisingly, the planned removal of limited tax liability that was still included in the draft bill of November 2020 has been deleted again in the government bill dated 20 January 2021. This means that – according to the current wording – the limited tax liability previously stipulated by the BMF will

remain in place unchanged in cases where the rights granted are merely registered, but not exploited in Germany.

The **consequence** of this is that where **rights are granted for a limited period** the party owing the fees must generally make the tax deduction, remit the tax to the German Federal Central Tax Office (*Bundeszentralamt für Steuern*; **BZSt**) and file a tax return with the BZSt (cf. section 50a (5) sentences 2, 3 EStG; sections 73a *et seq.* of the German Income Tax Implementing Ordinance (*Einkommensteuer-Durchführungsverordnung*; **EStDV**)). For fees received by the payee on or before 31 December 2013, the tax return must be filed with and the tax remitted to the competent tax office rather than the BZSt. The tax deduction may only be dispensed with if an exemption certificate pursuant to section 50d (2) sentence 1 EStG was in effect at the time the fee payment was received. For past cases, such a certificate will generally not have been obtained.

In the event of a **disposal of rights** that is not taxable, the payee must file a tax return with its competent tax office.

BMF circular dated 11 February 2021: Procedural relief for certain cases concerning a temporary granting of rights

With reference to its circular dated 6 November 2020, the BMF published a further administrative circular on 11 February 2021 dealing in particular with procedural matters.

According to this circular, a tax deduction for **fees already received by the payee or to be received up to (and including) 30 September 2021** need not be made where **rights are granted for a limited period in cases falling within the scope of application of a DTT**, if:

- the payee, or the party owing the fee acting on a power of attorney granted by the payee, files an application for exemption from the tax deduction with the BZSt in

analogous application of section 50d (2) sentence 1 EStG by 31 December 2021; such application may also be filed by the party owing the fees without a power of attorney if the contractual relationship has ended and the party owing the fees can show that the payee is neither willing nor able to file the application; a separate application must be filed for each contractual relationship; for cases involving the same payee a combined application is sufficient.;

- the contractual arrangements relating to the fee for which an application for exemption has been filed are disclosed within one month of receipt of the application, and at the latest by 31 December 2021; for intra-group relationships, extended disclosure requirements are to apply also with regard to a potential onward granting of the right to related parties;
- significant parts of the contractual arrangements are submitted in German; and
- no doubt exists as to the payee's DTT entitlement or the relief entitlement under the DTT or section 50d EStG; in the case of tax-transparent partnerships, this requirement must be fulfilled for the partners in such entities.

If the BZSt rejects the exemption application referred to above, tax returns must be filed for the relevant fee payments and the relevant tax deduction amounts remitted within one month after the rejection was communicated.

For **fees received by the payee after 30 September 2021**, the BMF circular states that

the statutory requirements in section 50d (1) to (4) EStG concerning the applicability of limitations on German tax law stipulated in a DTT must be observed in all cases.

Moreover, the BMF circular contains specific provisions governing the determination of the **assessment basis** and the **allocation of aggregated fee payments** for cases where a tax return must be filed and a tax remitted. According to these provisions, the gross fee amount is generally relevant and must be reasonably allocated in line with the grounds for accrual of such expenses (*Veranlassungsprinzip*) using a top-down approach. The BMF thereby makes it clear that the discussed bottom-up approach and the basing of the tax assessment on registration costs only are not acceptable.

Finally, the BMF circular deals with the procedure to be followed where **rights** registered in a public list or register in Germany **are disposed of**. Among other things, the party subject to limited tax liability is to be obliged to file a tax return in all circumstances, even where there is no right to levy tax in Germany under the applicable DTT. In the latter case, however, it will be possible to file a tax return for an amount of EUR 0 without further determination of the domestic income generated with the disposal.

The BMF circular will apply to **all cases that have not yet become final and non-appealable**.

What's next?

The government bill dated 20 January 2021 has now been forwarded to the German Federal Council (*Bundesrat*) (BR-Drs. 50/21). The further timing of the legislative process is, however, as yet unclear. We will keep you posted.

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