

STRICTER TRANSFER PRICING RULES IN GERMANY?

Revised Draft ATAD of Implementation Act

The German Ministry of Finance ("BMF") published a **revised draft law** regarding the implementation of the Anti-Tax Avoidance Directive ("**ATAD draft bill**") on 24 March 2020. What at first glance seemed to be a simple implementation of the corresponding **EU directive** turned out to be a comprehensive collection of "concretizations", including aggravations in the **area of transfer pricing**.

EU COUNCIL DIRECTIVE 2016/1164 OF 12 JULY 2016

The starting point is the EU Council Directive 2016/1164 of 12 July 2016, that aims to tackle tax avoidance practices. The ATAD draft bill implements Article 5 (**exit taxation**), Article 9 and Article 9b (**hybrid mismatches**) of the EU Council Directive and reforms the **computation of controlled foreign income** (Articles 7 and 8). For details we refer to separate communication made available.

Furthermore, the revised draft law wants to give the regulations regarding a **fair distribution of taxation rights** for multinational companies a contemporary design. In addition, the legislator intends to implement a reliable legal basis for **Advance Pricing Agreements**. This shall also reflect the developments on the OECD level. In particular, the following transfer pricing issues are affected by the ATAD draft bill:

REFORM OF THE ARM'S LENGTH PRINCIPLE

The arm's length principle shall be further specified and expanded, e.g. the ATAD draft bill standardizes the price setting approach and abolishes the hierarchy of transfer pricing methods. Furthermore, the transfer pricing methods are defined in the draft. In the future the taxpayer has to choose the most appropriate transfer pricing method.

INCREASED SIGNIFICANCE OF ECONOMIC ANALYSIS

The ATAD draft bill increases the importance of an **economic analysis** of the facts. The application of the interquartile range – being state of the art in today's transfer pricing practice – becomes part of the German transfer pricing laws. Furthermore, the ATAD draft bill emphasizes that a **hypothetical transfer price** should be based on state-of-the-art economic valuation methods.

BUSINESS RESTRUCTURINGS AND THE TRANSFER PACKAGE

The **terms transfer package** in case of business restructurings and **intangible asset** are legally defined. The period for price adjustments of transfer packages is reduced **from 10 to 7 years**. In addition, if the price fluctuation of the transfer package does not exceed 20 %, the taxpayer is not obliged to adjust the transfer price. Two of the escape existing clauses are removed, but the most relevant **exception** of the current regulations (the so-called 25 % rule) shall stay in force.

ABOUT BDO

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THE OECD'S DEMPE APPROACH

Also included is the **OECD's DEMPE approach** for intangible assets, which postulates that an analysis of the **development, enhancement, maintenance, protection and exploitation** of an intangible asset is conducted.

FINANCIAL TRANSACTIONS

So far, countries have not been able to agree on a common approach regarding **financial transactions** on an OECD level. Therefore, the German legislator decided to include in the ATAD draft bill unilateral stipulations on whether and to what extent interest payments are deductible for tax purposes. Furthermore, the **credit rating** of the corporate group becomes the benchmark for the computation of the interest rate of intercompany financial transactions for inbound loans.

As a rule, the financing function within a corporate group shall be treated as a **low-risk and low-value-adding** service that is usually remunerated on a cost-base. This might make the implementation of **economically meaningful cash pools difficult**. However, the function and risk profile of the respective entity is decisive.

ADVANCE PRICING AGREEMENTS

A new national legal basis for **advance pricing agreements** applicable to all international cases of potential double-taxation is introduced. The new § 89a of Fiscal Code shall come into force upon promulgation of the new law and will be applied to all new filings.

MASTER FILE THRESHOLD LOWERED TO A TURNOVER OF € 50 MILLION FROM 2021 ONWARDS

The threshold for the compulsory creation of an overview documentation for transfer pricing (so-called "**Master File**") for fiscal years starting after 31 December 2020 (i.e. 2021) is reduced from € 100 million to **€ 50 million annual turnover** of the taxpayer. This is justified by corresponding regulations in neighboring countries.

ELECTRONIC FILING OF THE MASTER FILE AT THE END OF THE FOLLOWING FINANCIAL YEAR

The Master File is supposed to be **created on a yearly basis** and **submitted electronically**. Filing is due at the end of the following fiscal year at the latest. Therewith, taxpayers are obliged to **update the Master File continuously**.

The electronic filing has to be conducted with local authorities and in addition with the Federal Tax Office in cases where the Country-by-Country-Reporting requirements are met.

The fiscal year for which the first electronic submission shall take place is currently still open. It is possible that the Master File to be created for the 2020 financial year must already be submitted electronically.

Hands, documentation requirements will be **aggravated considerably**. Up to now, a documentation had to be presented upon request only, e. g. during a tax audit. It was not necessary to prepare documentation in a timely manner or to file it automatically

COMMENCEMENT

The ATAD draft bill was not discussed by the government as previously intended on 8 April 2020. Due to the ongoing Corona-crisis, the future timeline remains uncertain. In the light of the expired deadline for the implementation of the ATAD rules, it appears to be possible that only those rules could be implemented that are directly connected with ATAD. This might speed up the agreement about the contents of the draft bill.

REQUIRED ACTIONS

Multinational groups should check for **possible effects** of the current ATAD draft bill. Therefore, the further development of the implementation process should be observed.

EFFECTIVE SUPPORT FOR YOUR COMPANY BY BDO

Please get in touch with your BDO contact person in order to receive a **Quick-Check identifying the actions necessary**. We would be happy to assist you to adjust your transfer pricing system if considered beneficial. If necessary, we will involve colleagues from other departments, e. g. when checking or adapting your compliance structures and IT systems or while assisting you with the integration of IT tools. If required, we work together with colleagues from the respective BDO member firms from our international network in more than 160 countries.