

Tax havens in the Age of Global Standards

Domestic Measures against improper use of tax havens

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Definition: *Tax Haven*

- German tax law: The term *Tax Haven* is not mentioned in German tax laws
- Common expression in German tax laws: *Area with low taxation* (better definition: low tax jurisdiction)
- There are different definitions in German tax laws

Definition: *Improper Use*

- Transfer of tax residence
 - Individuals: Giving up of *residence* and *habitual abode* in Germany
 - Corporations: Transfer of *statutory seat* and/or transfer of *place of effective management* abroad
- Transfer of economic interests abroad
 - Transfer of *property* and *income* to foreign subsidiaries, permanent establishments and legal entities (e.g. trusts)
 - Transfer of *capital funds* (cash, shares, bonds, funds etc.)
 - Transfer of *intangible assets* (patents, other rights, business chances)
- Attention:
 - Anti avoidance legislation in Germany do not always require the transfer of persons to a low tax jurisdiction!

Definition: *Improper Use*



Low or high tax jurisdiction

Transfer of tax residence (Individuals)

Transfer of statutory seat or place of effective management (Corporations)

Transfer of business property and income

Transfer of capital funds (cash, shares ...)

Transfer of intangible assets (patents, rights ...)



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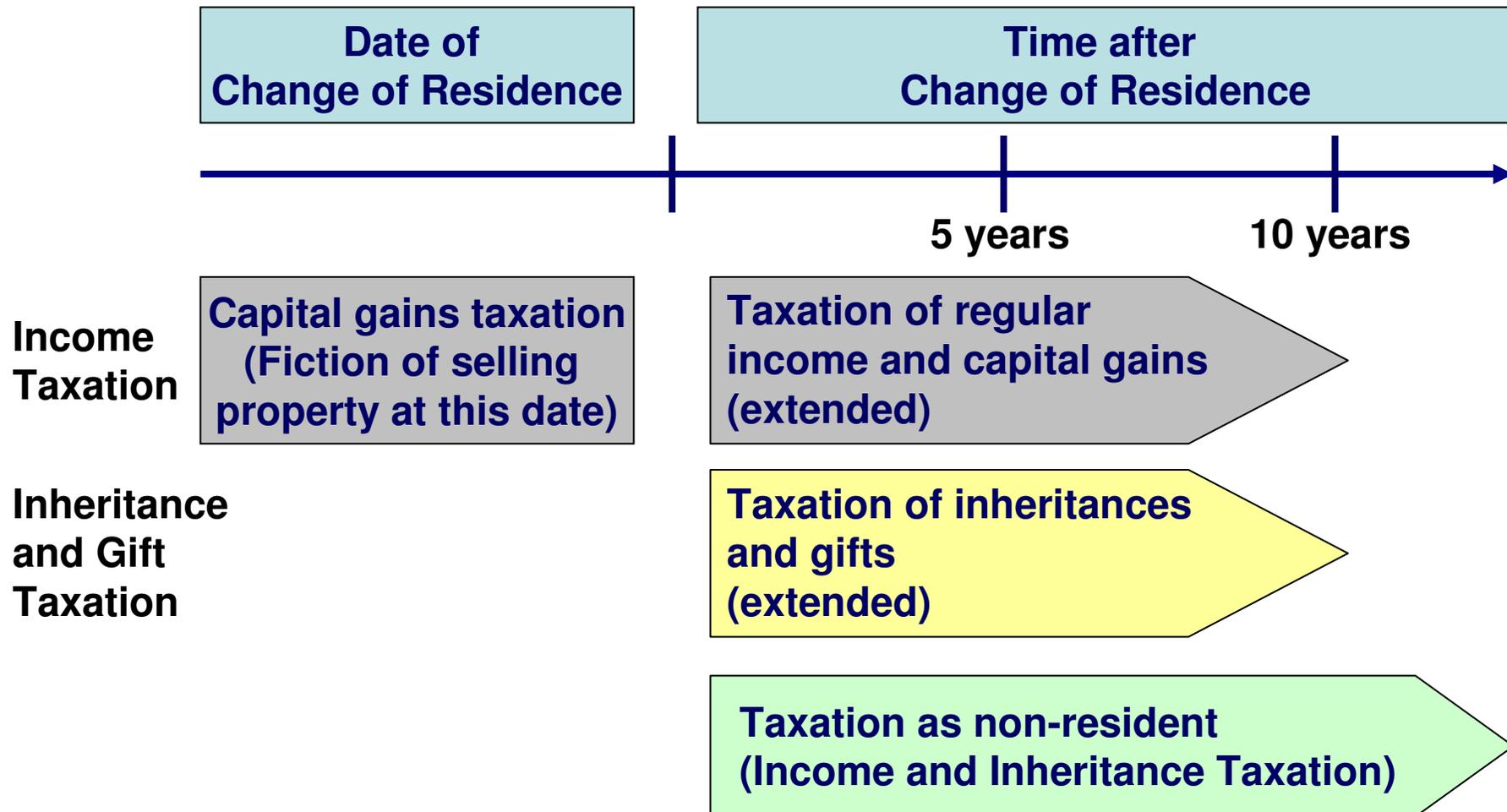


Anti avoidance measures of German tax legislation

Measurements	Steuergesetz	Tax law	Applicable only to low tax jurisdictions
Transfer Pricing Rules	Außensteuergesetz (AStG)	Foreign Transaction Tax Act	no
Thin Capitalisation Rules	Körperschaftsteuergesetz (KStG)	Corporation Tax Act	no
Controlled Foreign Company (CFC) Rules	Außensteuergesetz (AStG)	Foreign Transaction Tax Act	yes
Expatriation Rules	Außensteuergesetz (AStG) Einkommensteuergesetz (EStG) Körperschaftsteuergesetz (KStG) Erbschaftsteuergesetz (ErbStG)	Foreign Transaction Tax Act Income Tax Act Corporation Tax Act Inheritance Tax Act	partly yes
Treaty Overrides	verschiedene deutsche Steuergesetze	various German Tax Acts and Codes	partly yes

Transfer of Residence to Tax Haven

Taxation of Individuals



Transfer of residence

Income taxation

	Provisions	Restricted to low tax jurisdiction
Taxation in the moment of transfer of tax residence		
a) Fiction: Capital gains taxation		
Shares in German and foreign companies (more than 1% of share capital)	§§ 6 AStG	no
Business property	§ 4 (1) EStG	no
b) Other income tax implications		
Reclaiming of tax incentives for special pension schemes	§ 95 EStG	no
Taxation after transfer of tax residence		
Extended income taxation of non-residents	§§ 2, 5 AStG	yes

Income Taxation of Individuals

Special provisions (§§ 2 and 5 AStG)

Conditions

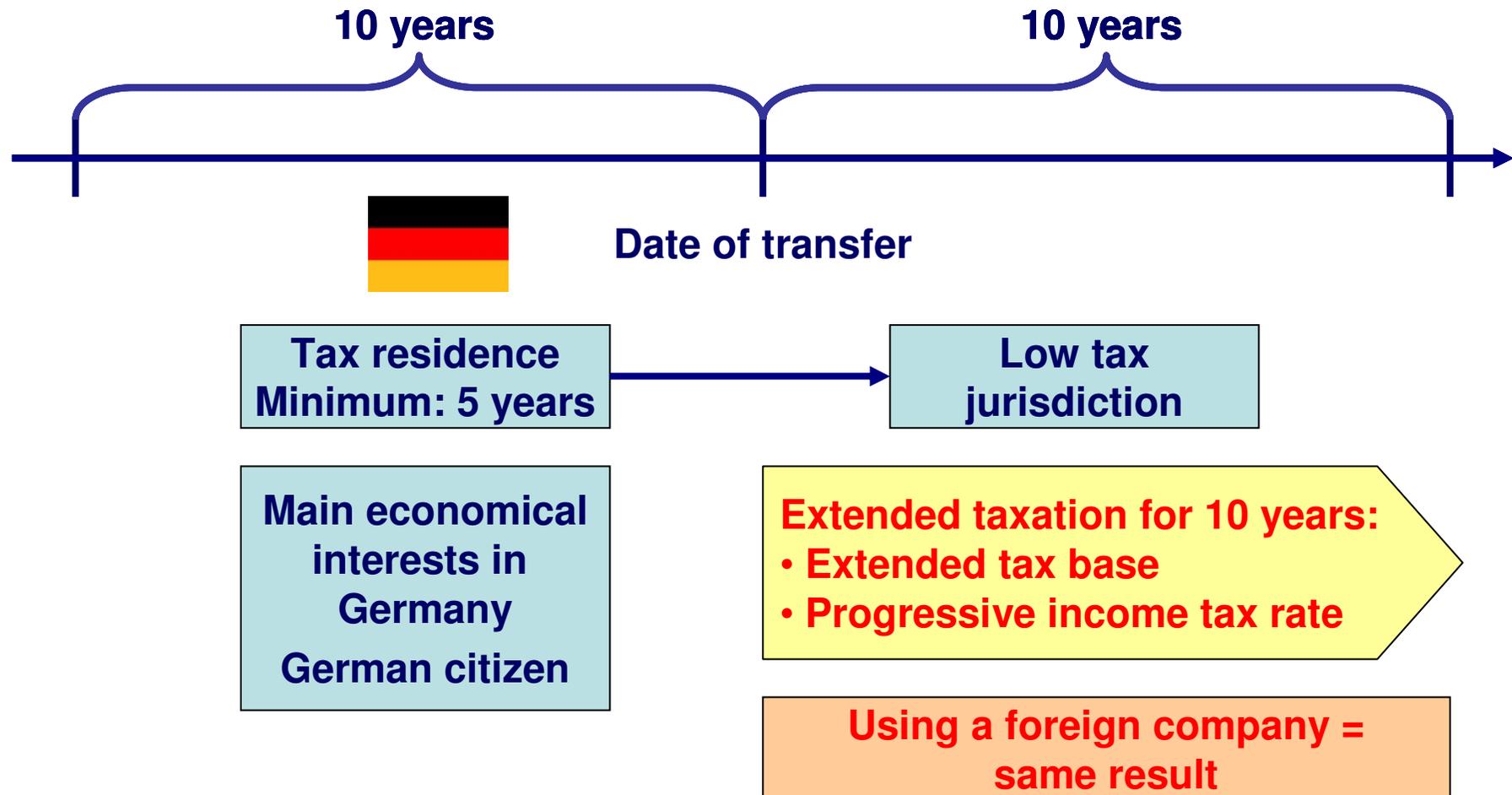
- German citizens
- Minimum of 5 years tax residence in Germany within 10 years previous to transfer of residence
- Transfer to low tax jurisdiction = Foreign income tax less than 66,66% of German income tax
- Main economical interests in Germany
 - Owner or co-owner of business
 - More than 25% income from business
 - More than 1% share-capital in companies
 - Other income or property (if more than 30% of total income/property and more than € 62,000/€ 154,000)

Tax implications

- Extended taxation for 10 years after transfer of residence as non-resident
- Extension of tax base
 - Extension beyond regular taxation of non-residents
 - Excluded is only foreign income
 - Extension especially to following income (examples)
 - Interests from German banks and other creditors
 - Pensions if institution is resident in Germany
 - Capital gains on private property in Germany
- Progressive German income tax rate (not flat tax rate)
- Holding property through a foreign company does in general not prevent this tax treatment

Income Taxation of Individuals

Special provisions (§§ 2 and 5 AStG)



Special provisions (§§ 2 and 5 AStG)

Can Germany execute these regulations?

- Problem 1: EU-law
 - Breach of ***Right of free movement*** ?
 - So far no ruling of the European Court of Justice (ECJ)
- Problem 2: Double Taxation Treaties
 - Restriction of taxation of specific income (e.g. from real estate or business income)
 - Restriction of tax rates (e.g. on dividends)
- Problem 3: Tax collection
 - Difficulties to identify tax payer (if living abroad)
 - Difficulties to calculate low taxation in each applicable case
- Day to day experience
 - German tax authorities execute these provisions very seldom!

Special provisions (§§ 2 and 5 AStG)

Can Germany execute these regulations?

Low Tax Jurisdiction	In line with EU-law	Restricted by DTT	
EU-member state	no (?)	yes (but limited)	
Non-member state with Double Taxation Treaty (DTT)	yes (?)	?	
Switzerland	no (?)	yes (but limited)	
Non-member state without Double Taxation treaty (DTT)	yes (?)	not applicable	

Practical problems: German tax authorities execute these provisions very seldom!

Transfer of residence - Individuals (§ 6 AStG)

Exit tax – holders of “substantial” participations

- If an Individual, who has been subject to unlimited tax liability for at least 10 years, holds 1% or more of the shares of a German corporate entity and relocates his tax residence, this is deemed to be a sale of such shares
- This is also the case, e. g. when the shares are transferred to a foreign company
- This virtual capital gain is the difference between the fair market value and the acquisition costs
- As the European Court of Justice decided in 2004, that the French exit tax in the case of holding substantial participations and transferring residence is a breach of the Freedom of Movement (Art. 43 ECT) Germany had to react

Transfer of residence - Individuals (§ 6 AStG) Legislation after the Lasteyerie du Saillant Decision of ECJ (11.03.2004 – C – 9/02)

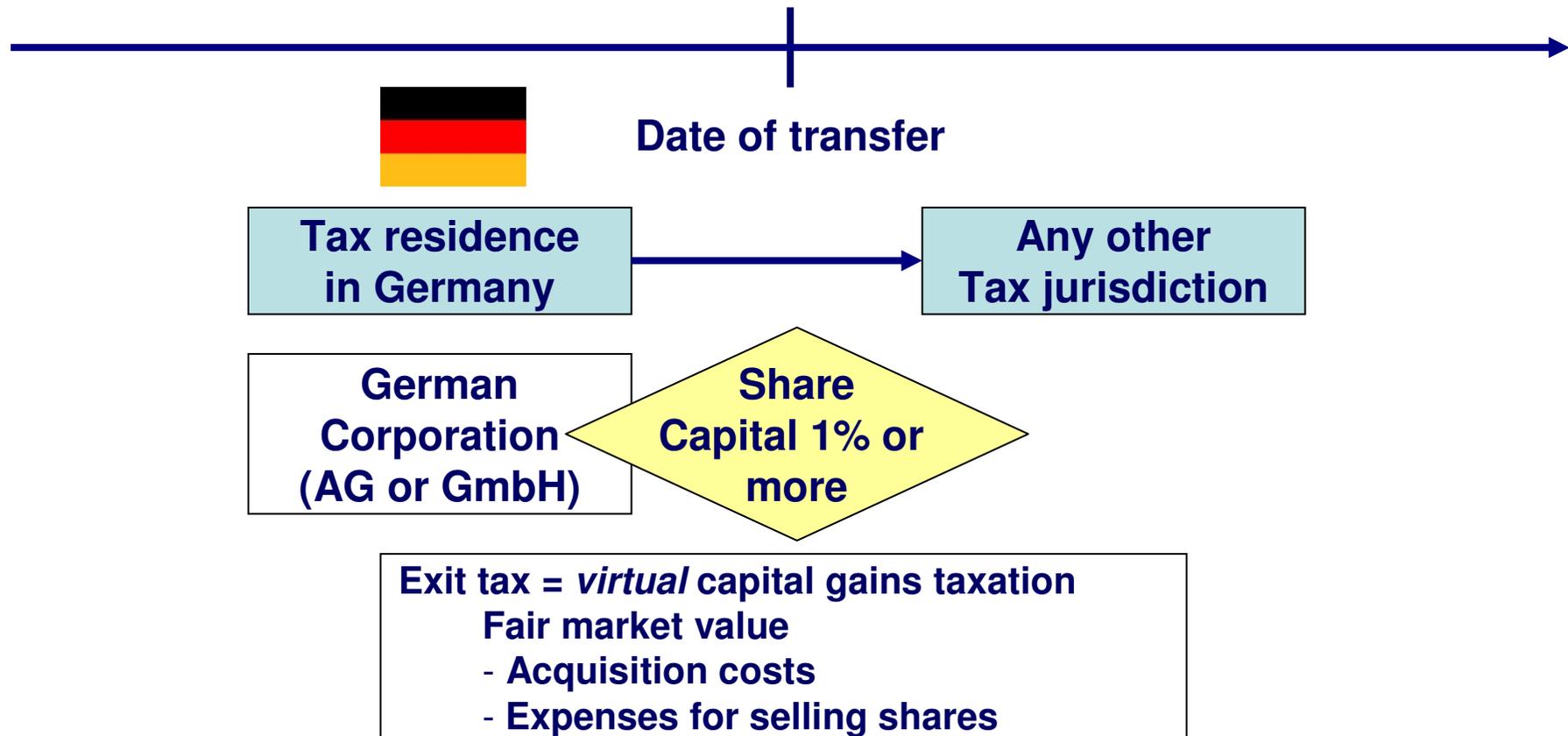
- Exit tax provision is still in force, but has been amended in 2006
- This amendment has only effect for EU-/EEA-Citizens, who relocate their tax residence into another EU-EEA-State
- Germany has the right to assess the generated gains upon the shareholders transfer of residence but will grant an unlimited deferral of payment free of interest

Transfer of residence - Individuals (§ 6 AStG) Non EU-/EEA-Citizens

- Capital gains fictitious derived by a non EU-/EEA-Citizen will be taxed
- These individuals can only apply for a limited deferral of payment (up to 5 years)
- They can only qualify for this deferral of payment, when payment would be a considerable hardship

Transfer of residence (§ 6 AStG)

Exit Tax – Holders of “substantial” participations



Inheritance and Gift Taxation of Individuals

Special provisions

Extended taxation as resident

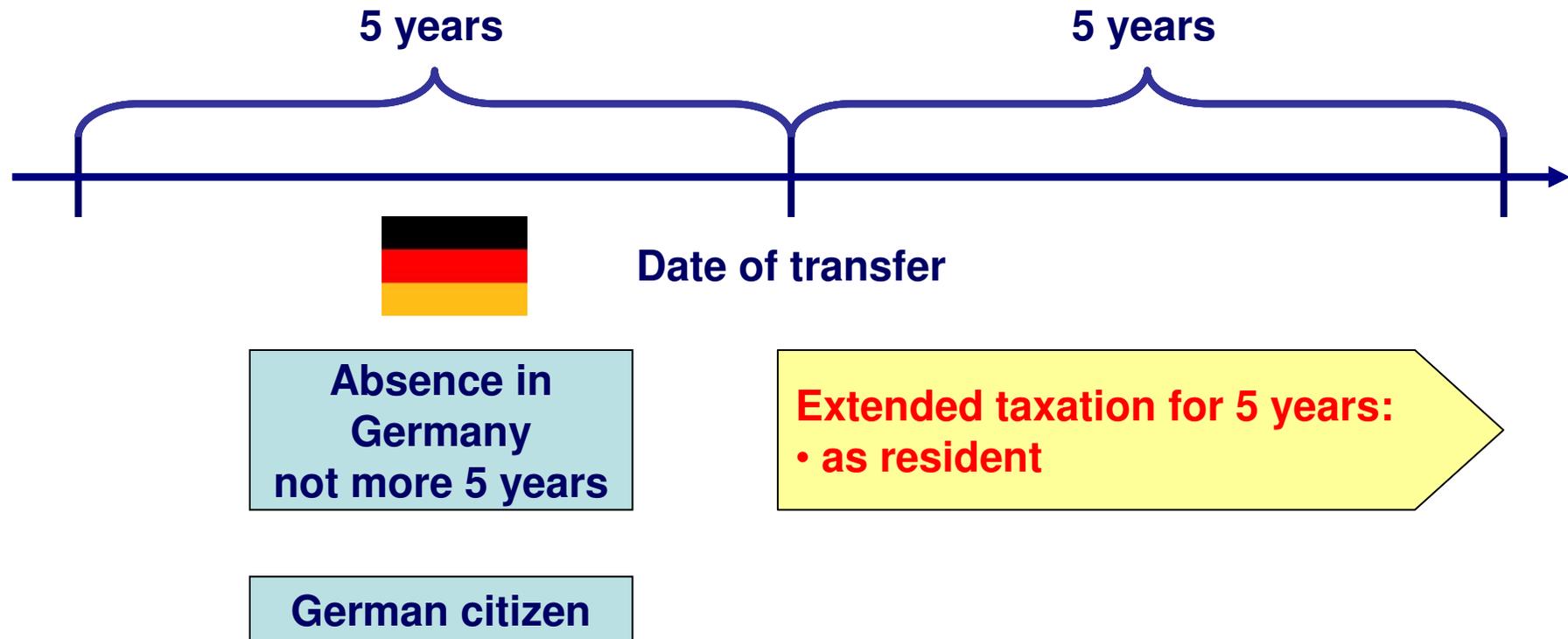
- **Conditions**
 - German citizens
 - Not living abroad for more than 5 years
- **Tax implication**
 - Regular taxation as resident
 - for additional 5 years
- **Remarks**
 - § 2 (1) No. 1 b ErbStG
 - No cover by Double Taxation Treaties (only 6 DTT for inheritance tax; and i.g. special rules for transfer of tax residence)
 - No cover by EU-law: ECJ / *van Hilden – van der Heijden* (23.02.2006 - C - 513/03)

Extended taxation as non-resident

- **Conditions**
 - The same conditions as for the extended income taxation of non-residents
 - Transfer to low tax jurisdiction = Foreign inheritance tax less than 66,66% of German inheritance tax
- **Tax implications**
 - Transfer of all property except foreign property is taxable
 - for a period of 10 years
- **Remarks**
 - § 4 AStG
 - Little cover by DTT
 - Breach EU-law (Freedom to transfer capital funds)?

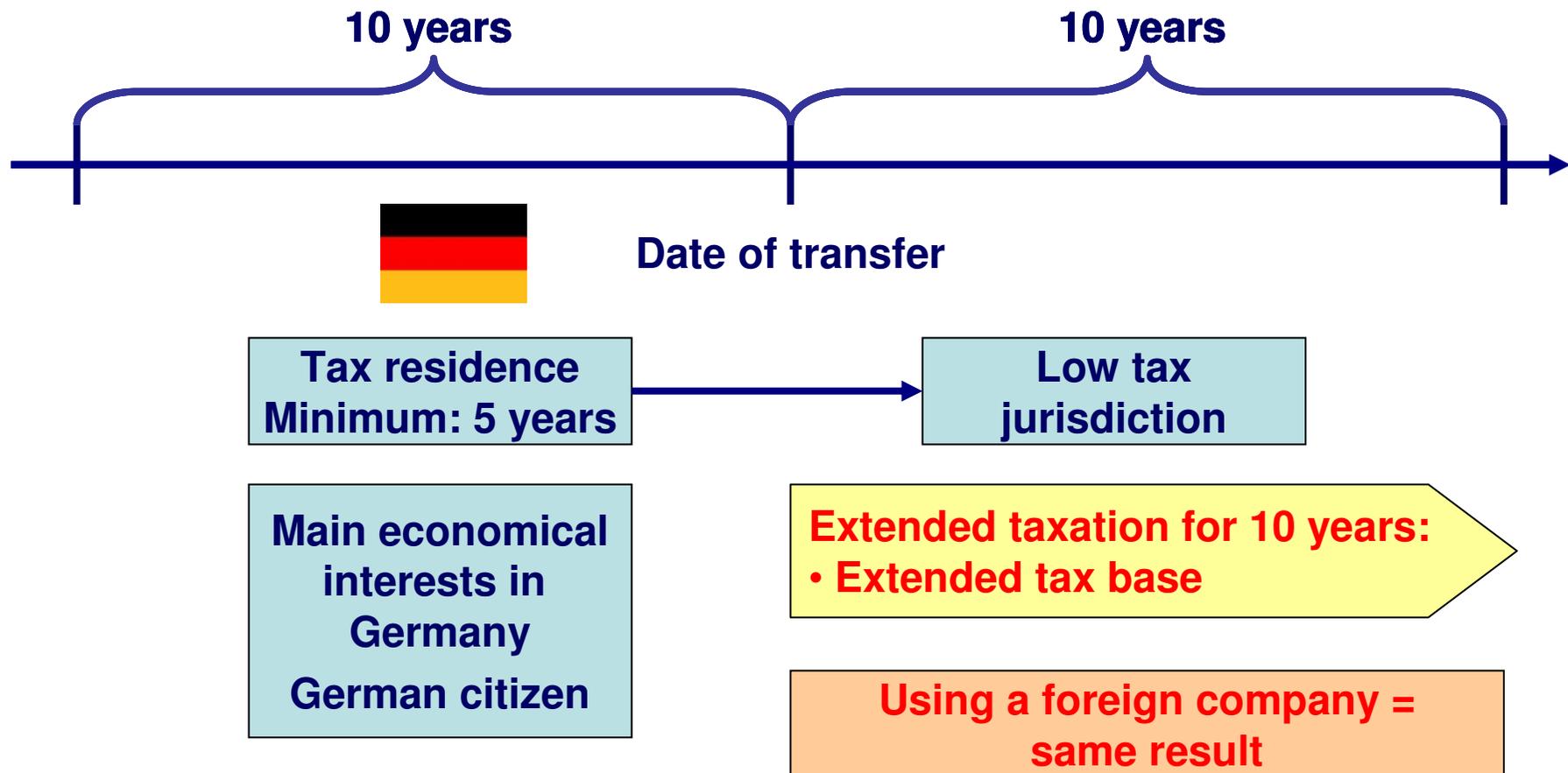
Inheritance and Gift Taxation of Individuals

Special provisions (§ 2 (1) No. 1b ErbStG)



Inheritance and Gift Taxation of Individuals

Special provisions (§ 4 AStG)



Inheritance and Gift Taxation of Individuals

Special provisions (§ 4 AStG)

- Restrictions by Double Taxation Treaties
 - Germany has only a very limited network of DTT applicable on inheritance and gift tax
 - and some of these DTT allow extended taxation (e.g. DTT USA)
- European Law
 - Breach of European Freedom Rights (especially freedom of transfer of capital funds)
 - So far no ruling of the European Court of Justice
 - Special information: also applicable on cases with Swiss citizens (Freedom agreement between Switzerland and the EU)
- Day to day problems
 - The same problems as for income taxation
 - Difficulties to identify tax payer (if living abroad)
 - No knowledge of German tax authorities of taxable transfer (death or gift)
 - Difficulties to calculate low taxation in each applicable case

Tax transparency and fight against cross-border tax evasion

- The German Parliament estimates revenue losses from tax evasion at around several billion euros every year
- Most of them are deemed to be losses from cross-border tax evasion
- To fight tax avoidance and tax evasion Germany adopted in July 2009 the Act for combating tax evasion – Steuerhinterziehungsbekämpfungsgesetz - and August 2009 Anti-Tax Evasion Rule - Steuerhinterziehungsbekämpfungsverordnung

Scope of Application/Legal consequences

- The Anti-Tax evasion act applies only, if the involved parties are resident in a so-called uncooperative tax haven
- The Anti-Tax evasion act does not apply, when a Tax Information Exchange agreement has been agreed – with reference to Article 26 OECD MC 2010
- If the conditions of the Tax Evasion Act are met the German tax authority is authorized not to apply certain provisions of German tax law and tax reliefs
- Additionally stricter obligations to provide information and record-keeping obligations (German Tax Code – Abgabenordnung)

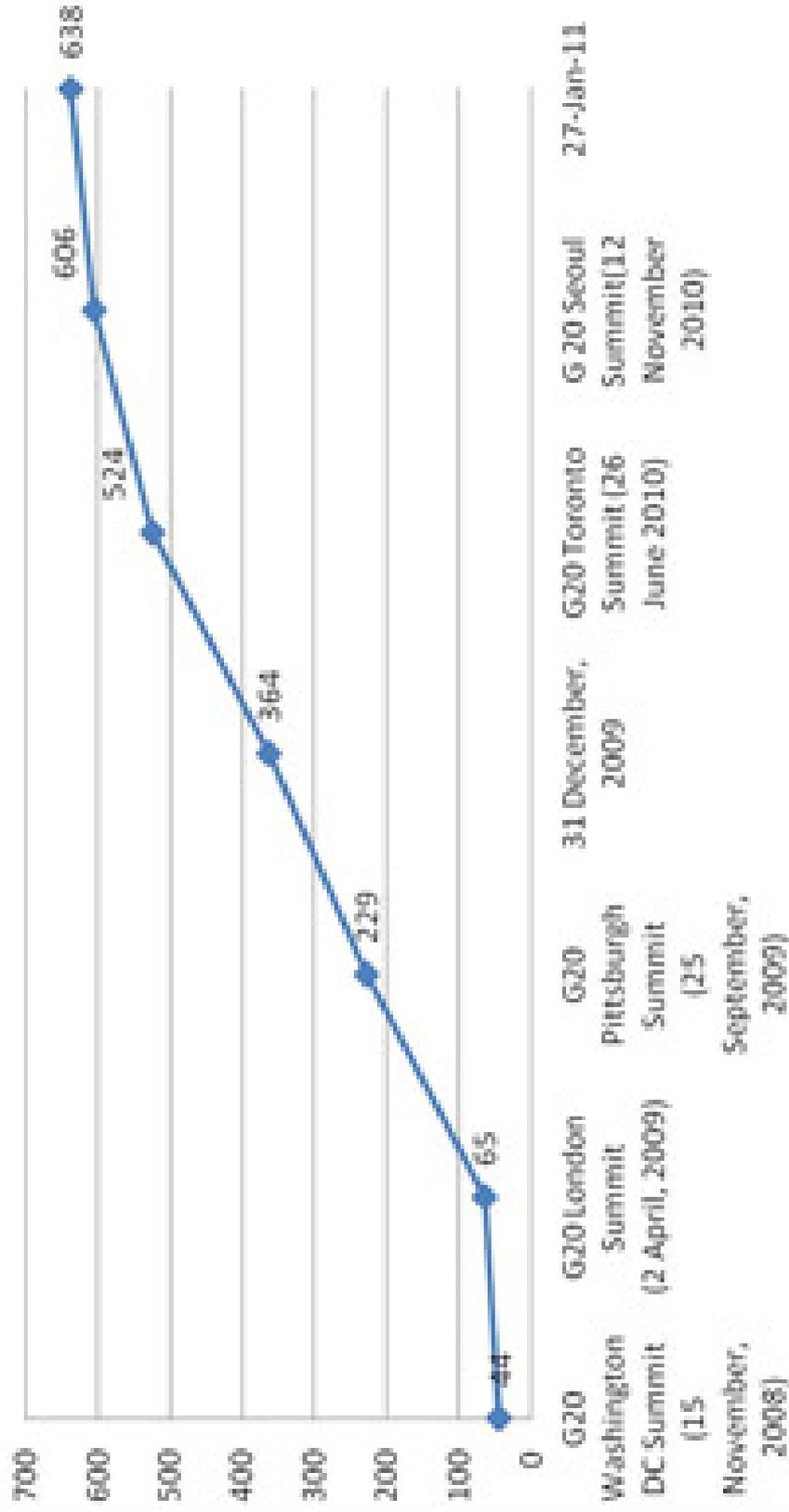
Amendments to German tax law

- Amendments were made to the German Income Tax Law (Einkommensteuergesetz), Corporate Income Tax Law (Körperschaftsteuergesetz) and German Tax Code (Abgabenordnung)
- If the Tax Evasion Act is applicable, the following consequences may occur:
 - Denial of deduction of operating expenses/income-related expenses
 - Denial of withholding exemption on capital income
 - Denial of application of Flat tax on capital income (25%)
 - Denial of partial income taxation method (40% tax exempt)

Status Quo – Application of the German Tax Evasion Act

- In May 2009, the OECD decided to remove all three remaining jurisdictions (Andorra, the Principality of Liechtenstein and the Principality of Monaco) from the list of uncooperative tax havens
- No jurisdiction is currently listed as an uncooperative tax haven by the Committee on Fiscal Affairs
- As a result, the German Tax Evasion Act is currently not applied

TIEAs/DTCs Signed between G20 Summits



TIEAs recently signed by Germany

- Germany – Switzerland (Revised DTA – Art. 26 OECD MC)
- Germany - Principality of Andorra (25 Novembre 2010)
- Germany – Antigua and Barbuda (19 October 2010)
- Germany – British Virgin Islands (5 October 2010)
- Germany – Dominica (21 September 2010)
- Germany - Monaco (27 July 2010)
- Germany - San Marino (21 June 2010)
- Germany – Saint Lucia (7 June 2010)
- Germany – Turks and Caicos Islands (4 June 2010)
- Germany – Cayman Islands (27 May 2010)
- Germany - Bahamas (9 April 2010)
- Germany – St. Vincent and the Grenadines (30 March 2010)
- Germany - Anguilla (19 March 2010)
- Germany - Liechtenstein (2 September 2009)
- Germany - Gibraltar (13 August 2009)
- Germany - Bermuda (3 July 2009)
- Germany - Guernsey (26 March 2009)
- Germany – Isle of Man (02 March 2009)
- Germany – Jersey (4 July 2008 / Date of entry into force: 28 August 2009)

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