Deloitte.

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German Tax and Legal News

Ministry of Finance publishes updated legislation to start the process of implementing the EU Pillar Two global minimum taxation directive into German domestic law

Updated draft bill includes amendments to German CFC rules and would abolish royalty barrier rule

On 10 July 2023, the German Ministry of Finance (MOF) published an updated version of the official draft legislation on the domestic implementation of Council directive (EU) 2022/2523 on ensuring a global minimum level of taxation for multinational enterprise (MNE) groups and large-scale domestic groups (the "Pillar Two directive"). The updated draft legislation is the second discussion draft after a first discussion draft was published for comments on 20 March 2023 (see GTLN, 22 March 2023) and incorporates some of the public comments received, together with a number of changes and clarifications proposed in the OECD administrative guidance published on 2 February 2023 that were not reflected in the first draft. In addition to provisions introducing the global anti-base erosion rules into German law, existing German tax legislation would also be amended.

In line with all other EU member states, Germany must implement the rules regarding global minimum taxation into domestic law during 2023, with the rules applying to in-scope MNEs for fiscal years starting on or after 31 December 2023.
With the newly published draft implementation legislation, the MOF has started the official legislative process. In addition to the new "minimum tax act" (Mindeststeuergesetz, MinStG), the updated draft legislation proposes changes to tax law outside of the Pillar Two implementation act. Two of these proposed changes would provide a welcome relaxation of the compliance burden for German multinational companies:

- The updated draft proposes to reduce the low taxation threshold of the German controlled foreign company (CFC) rules from the current 25% to 15%, in line with the global minimum taxation rules, and would abolish the trade tax burden on any CFC income attributed to German shareholders.
- The so-called "royalty barrier" rule, which provides for the (partial) non-deductibility of royalty expenses paid to a related party benefitting from a low-tax, non-nexus compliant preferential tax regime, would be abolished as from 2024.

In terms of minimum taxation rules, the updated draft legislation includes changes reflecting some of the items discussed since the issue of the original draft. It includes new rules to implement the OECD administrative guidance, most significantly the rules on portfolio dividends and on income from qualifying debt releases, the changes and clarifications to the transition rules (articles 9.1.1 to 9.1.3 of the OECD model rules and article 4 of the administrative guidance), and the rules on blended CFC regimes as part of the temporary safe harbor rules. The updated draft still includes a German-specific element around so-called "minimum taxation groups" where the tax payment is concentrated within the German members of an MNE group, but now includes a tax allocation mechanism within that group to provide legal certainty.

The MOF has asked for final comments by 21 July 2023. It is expected that the updated draft legislation will be approved by the government shortly afterwards, and then officially introduced into the legislative process so that the rules can be finalized and be approved by the upper and lower houses of parliament prior to the end of 2023.