April 29, 2022

BY EXPRESS DELIVERY AND EMAIL

Bundeskanzleramt
Bundeskanzler
Olaf Scholz
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Herrn Bundesminister Christian Lindner
Bundesministerium der Finanzen
11016 Berlin
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Subject: Extraterritorial application of Sec. 49 German Income Tax Act

Dear Chancellor Scholz and Minister Lindner,

The undersigned associations have serious concerns about how the German government applies its domestic withholding tax and capital gains rules to income from intellectual property (IP) registered in a German public book. We kindly ask you to review the currently contemplated German tax position and reconsider the retroactive repeal of this old and obsolete provision of the German tax law. The law has been in place since 1925 and has never been applied to extraterritorial cases, i.e., no involvement of a German party to either a license agreement or sale transaction and no payment made out of Germany. It was a huge surprise when our members heard from their advisors that Germany planned, after so many years, to extend the rule to purely non-German agreements. This extraterritorial reach would be a violation of international tax norms, as well as inconsistent with the original intent of this law. We respectfully request this topic to be addressed at the highest ranks of German government.

Our members are multinational groups resident in our countries and active in all kinds of industry segments. These multinational groups face huge administrative burdens in cases where we rely on treaty protection and serious financial impact if there is no treaty protection. We address our arguments as follows:

1) The new approach to this very old law is not in line with existing international norms. The OECD transfer pricing guidelines refer to so-called DEMPE-functions which require substance in a respective country to align with taxation of IP-related profits. These rules were designed and agreed to align taxation with value creation and functions that develop that IP.
2) Pure registration of IP is not sufficient to create nexus or a right for taxation, as it does not meet the threshold set out as described in internationally recognized permanent

establishment principles or agreed international sourcing rules (common in tax treaties) for royalty payments. As far as we can see, there is not a single tax treaty in the world that refers to income from a registered right. It is clear that no tax authority has historically considered this a sufficient basis for taxation.

3) Even when it is entirely clear that the licensor is treaty protected and no German tax is due, the tax administration asks for a large number of documents, translated into German, and for tax returns in IP sale transactions. All of this is requested for the last 7 years for which obviously nothing had been prepared, as this approach was rightly unexpected. The time and resources required are absolutely unnecessary, but substantial. This compliance burden makes the protection provided by the treaty ineffective.

4) These rules, as considered, are also impossible to comply with, given that obligations of withholding agents require very detailed knowledge of third-party partners' business data. It is impractical to expect these partner companies to share that data, and such data may be considered confidential. In this respect, these rules are unprecedented in how impractical and infeasible they are to apply.

5) The entire new process has been based on voluntary disclosure. While in western countries many multinationals invest substantial resources to be compliant, this is certainly not the case everywhere. This leads to unequal treatment, and such a tax cannot be legitimate unless it applies consistently to all similar cases. It produces a very perverse outcome that the most compliant companies are the ones most likely at risk of adjustment by tax authorities.

6) In November 2020, the German Ministry of Finance published draft legislation explicitly stating that this old section of German law was never intended to be applied as it is now being considered, and that it requires an inappropriate administrative burden in view of most cases being treaty-cases without German revenue. We agree!

7) This inconsistent and new application of this rule is also not in line with OECD policy goals – which Germany shares and wishes to be applied internationally, in particular with Pillar 1. Pillar 1 defines how a profit share for a market country will be calculated. A tax based solely on registration of IP in that market is deeply inconsistent with Pillar 1 and needs to be stopped immediately in order to prevent other countries from introducing similar rules which makes all current efforts to ensure fair allocation of taxes obsolete. The proliferation of such rules would create trade barriers, hamper international business, and change business behavior (particularly with respect to activity in Germany) and harm German and non-German businesses alike. Thank you very much for looking into this.

We appreciate the opportunity to provide our views on this issue. For any additional questions or communications regarding this letter, please contact Jake Colvin, President, National Foreign Trade Council (jcolvin@nftc.org) who will coordinate on behalf of the undersigned organizations.

Sincerely,

AFEP
AmCham Europe
Bitkom
Information Technology Industry Council
National Foreign Trade Council
Swiss Holdings
techUK
US Chamber of Commerce
US Council for International Business
Verband Forschender Arzneimittelhersteller e.V. (vfa)