



Germany

Introduction

A person's liability to German individual income tax is determined by residence status for taxation purposes and the source of income derived by the individual. Income tax is levied at progressive rates on an individual's taxable income for the calendar year. It is calculated by subtracting allowable deductions from the total assessable income.

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Key messages

It is essential that transfer pricing rules be observed, which means that appropriate cost sharing between the home and the host country should be agreed and properly documented.

Extended business travelers are likely to be taxed on employment income relating to their German workdays.

In this respect, withholding obligations may arise for the host company. It should be noted that the tax withholding for nonresident employees follows special rules, which differ from those for resident employees. It is important that the home and host country establish a reporting system that allows them to exchange all the relevant information in a timely manner.

Individuals working in Germany are subject to German social security regulations unless exempted under the applicable EEC Regulation, a totalization agreement, or domestic laws. The home and the host company should carefully review whether there is a social security withholding obligation for inbound business travelers or, if an exemption applies, whether a certificate of coverage has been obtained.

Germany applies a strict regime of immigration laws for non-EU citizens.

A review of the immigration status of your business travelers well in advance of the business trip or assignment is strongly recommended.

Income tax

Liability for income tax

A person's liability to German individual income tax is determined by residence status. A person can be a resident or a nonresident for German tax purposes. A resident of Germany generally refers to an individual who has a domicile in Germany or spends more than six consecutive months in Germany (habitual place of abode). A domicile is a home or dwelling owned by or rented to the taxpayer who has full control over the property. Domicile is determined by fact, not by the intention of the taxpayer.

A nonresident of Germany is generally someone who spends less than six consecutive months in Germany. The general rule is that a person who is a resident of Germany is assessable on the individual's worldwide income. Nonresidents are generally assessable on income derived from German sources. Extended business travelers are likely to be considered nonresidents of Germany for tax purposes unless they stay in Germany for more than six months in a row (brief interruptions such as home trips over the weekend or vacations are disregarded).

Definition of source

Employment income is generally treated as German-sourced compensation where the individual performs the services while physically present in Germany. Additionally, specific rules apply for salary received as a board member, managing director, or other authorized representative (*Prokurist*) of a German company. Double tax treaty provisions may prevent Germany from taxing employment income if certain conditions are met.

Tax trigger points

Technically, there is no threshold/minimum number of days that exempts the employee from the requirements to file and pay tax in Germany. To the extent that the individual qualifies for relief in terms of the dependent personal services article of an applicable double tax treaty, there will be no tax liability. In some cases, treaty relief can be obtained only by submitting a formal application to the German tax authorities. The treaty exemption will not apply if the German entity is the individual's economic employer or if the salary is paid by a direct branch of a foreign employer who has created a permanent establishment for treaty purposes in Germany.

Types of taxable income

For extended business travelers, the types of income that are generally taxed are employment income and German-sourced income and gains from taxable German assets (such as real estate located in Germany); fringe benefits (broadly non-cash employment income also fall into this category).

Tax rates

Taxable income is taxed at graduated income tax rates ranging from 14 percent to 45 percent. In addition to income tax, a solidarity surcharge amounting to 5.5 percent of the assessed income tax is charged. If the taxpayer is a member of a church that is recognized for tax purposes, church tax at 8 or 9 percent of the income tax is levied. Nonresident employees are also subject to income tax at graduated rates as well as a solidarity surcharge. Nonresidents are not subject to church tax.

Social security

Liability for social security

Employees working in Germany are generally subject to German social security payments. Extended business travelers from other EU or EEC member states or Switzerland will typically be exempted from contributing to the German social security system under the applicable EEC regulation. Extended business travelers from other countries may be exempted under a totalization agreement or under Germany's domestic laws.

Contributions to pension insurance and unemployment insurance, as well as health insurance and long-term nursing care insurance, are capped for both the employer and the employee.

Compliance obligations

Employee compliance obligations

Tax returns are due by May 31 following the tax year-end, which is December 31. Where a tax agent is used, there is an automatic extension until December 31. Nonresidents who derive German-sourced employment income and no other income from German sources are required to file an income tax return only if the employment income was not subject to German wage tax withholdings. If the host company is obliged to withhold German wage tax on a nonresident's wages, the nonresident taxpayer generally cannot file a German income tax return. As a consequence, the German wage tax withholding needs to be accurate and precise.

Employer reporting and withholding requirements

If an individual is taxable on employment income, the German employer has a withholding requirement. A company that economically bears an individual's wages is also deemed to be a German employer even if no employment contract exists between the German company and the individual. (This is the economic employer concept.)

A permanent establishment of a foreign employer in Germany is also obliged to withhold German wage tax. It is important to note that a permanent establishment as defined by German domestic law is sufficient to trigger a withholding obligation. It does not necessarily have to qualify as a permanent establishment under an applicable tax treaty.

Other

Work permit/visa requirements

Where a visa is required, it must be applied for before the individual enters Germany. The type of visa required will depend on the individual's country of origin and the purpose of the individual's entry into Germany. Simplified rules exist for business travelers from EU member states and certain other countries in the Western world.

There is a certain risk that an agreement between the home and host company might be classified as a staff loan agreement if certain conditions are met, which can potentially lead to a violation of German labor and civil laws.

Double taxation treaties

In addition to Germany's domestic arrangements that provide relief from international double taxation, Germany has entered into double tax treaties with approximately 80 countries to prevent double taxation and allow cooperation between Germany and other tax authorities in enforcing their respective tax laws.

Permanent establishment implications

There is the potential that a permanent establishment could be created as a result of extended business travel, but this would be dependent on the type of services performed, the duration, and the level of authority the employee has.

The definition of a permanent establishment under Germany's domestic laws differs from the definition of a permanent establishment for treaty purposes. A permanent establishment, as defined by German domestic law, is sufficient to trigger a wage tax withholding obligation.

Indirect taxes

Value-added tax (VAT) is applicable at 19 percent for taxable supplies.

Transfer pricing

Germany has a tough transfer pricing regime. A transfer pricing implication could arise to the extent that the employee is being paid by an entity in one jurisdiction but performing services for the benefit of the entity in another jurisdiction,

in other words, a cross-border benefit is being provided. This would also be dependent on the nature and complexity of the services performed. There is a legal requirement to have comprehensive documentation on cross-border activities (cost and benefit analysis) at hand for a future tax audit.

Local data privacy requirements

Germany has data privacy laws.

Exchange control

Germany does not restrict the flow of German or foreign currency into or out of the country. Certain reporting obligations are imposed, however, to control tax evasion and money laundering.

Nondeductible costs for assignees

The deduction of assignee-related costs may be limited where the salary level of an inbound assignee significantly exceeds the cost of a local individual in the same role. Hence, proper documentation should be kept available.

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