Corporate tax in Germany

Tax liabilities for companies in Germany

Anyone carrying on a trade or business is subject to business tax and municipal business tax. Within German company law, businesses fall into two categories:

- Companies (incorporated businesses)
- Partnerships (unincorporated businesses)

There are several main differences between companies and partnerships:

- Companies provide for limited liability of their shareholders, while partnerships generally require unlimited liability of the partners.
- Companies are required to have a certain minimum share capital due to their limited liability. This is not necessary for partnerships as the creditors can be satisfied with the property of the partner who has unlimited liability.
- Companies have a distinct legal personality and are taxed, whereas partnerships have only a ‘partial legal personality'. Partnerships may, for example, acquire immovable property, conclude contracts, etc. Partnerships, however, are transparent, i.e. their profits and losses are attributed directly to the partners for both civil law and tax law purposes.

The basics of German company law are laid down in the Civil Code (*Bürgerliches Gesetzbuch*, BGB) and completed by special statutes for the different types of entities, such as:

- **Stock Company Law (Aktiengesetz, AktG) for stock companies (AG)**
- **Limited Liability Company Law (Gesetz betreffend die Gesellschaften mit beschränkter Haftung, GmbHG) for limited liability companies (GmbH**)

  and

- **Commercial Code (Handelsgesetzbuch, HGB) for partnerships.**

Except for civil law partnerships, new businesses must apply for entry in the Commercial Register (*Handelsregister*) and register with the local trade office and the tax authorities, irrespective of its business form.

Taxable profit

Resident companies are subject to corporate income tax on their worldwide income. Foreign-source income, such as income from foreign permanent establishments, is usually excluded from the German taxable base under tax treaties. If a treaty does not exist or its provisions do not apply, unilateral relief provisions allow a foreign tax credit under certain conditions.

All types of income realised by a company are deemed business income, whether they stem from the actual business activities or from investments (dividends, interest, rental income). Business income is subject to both the corporate income tax and the business tax.

Under both commercial and tax law, a company must keep its books on the accrual basis. The profits are determined using the net worth comparison method. According to this method, profits are the difference between net assets at the end of the previous year and net assets at the end of the current year.

For tax purposes, this net asset difference is reduced by capital contributions (because they are tax free) and increased by withdrawals (because they must be financed out of taxed income).

The financial statements of a company must be drawn up on the basis of the generally accepted accounting principles of commercial law. The commercial accounts are also binding for tax purposes unless specific tax rules provide otherwise. This means the commercial balance sheet and the tax balance sheet are identical in most cases. If there are deviations, companies must prepare both a commercial balance sheet (*Handelsbilanz*) and a tax balance sheet (*Steuerbilanz*). This can be done either by preparing two different sets of financial statements or simply by explaining the tax deviations in an appendix to the corporate income tax return.

Exempt income

The most important types of exempt income include:

At the company level – capital contributions upon formation or capital increase, whether or not in return for shares, other membership rights or simply in connection with an increase in the capital reserves.

At the shareholder level – capital repayments from the company if they do not contain dividend distributions. They are taxable, however, to the extent they exceed the book value of the shareholder's investment, e.g. as a result of former depreciation of the investment.

95 percent of domestic and foreign dividends.

95 percent of capital gains derived from the sale of shares in a company.

Investment grants for investments in the new federal states.

Taxable period

The tax year in Germany is equal to the calendar year. A taxpayer may adopt a financial year that deviates from the calendar year once their business is registered in the Commercial Register (*Handelsregister*), which is mandatory for companies.
The profit of a business is subject to tax in the year in which the financial year ends,

i.e. the profit of a company whose financial year ends on 31 January 2013 is subject to tax in the tax year 2013, even if most of the profit was derived in 2012. As a practical matter, this leads to postponement of the filing obligation.

Solidarity surcharge

Both resident and non-resident companies are subject to a solidarity surcharge of 5.5 percent. The assessment base for the solidarity surcharge is the total corporate income tax due by the taxpayer after deducting tax credits. If non-residents who benefit from a tax treaty are subject to a solidarity surcharge, the total tax including the surcharge may not exceed the maximum treaty rate that Germany is allowed to charge.

Inno:va tax advisory firm will be pleased to assist you in all stages of your new business activities in Germany and provides individual advice. Just contact us:

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