

# Transfer Pricing Country Summary

## Germany

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## 1. Introduction

German TP regulations are spread among multiple clauses in various legislative acts rather than being contained in a single section of the German tax code.

## 2. Laws & Regulations

### a) References to OECD/EU/Local Rules

The German tax legislation has no special section for a transfer pricing regime, but rules on transfer pricing are established in different sections of the German tax laws, decrees and administration principles. The most important is Section 1 of the Foreign Tax Code (“Aussensteuergesetz”) which defines related party transactions. Section 8 Paragraph 3 of the corporate income tax law (“Körperschaftsteuergesetz”) defines hidden profit distributions. Furthermore, various regulations published by the German Ministry of Finance (BMF) and relevant provisions of the German Double Tax Treaties deal with transfer pricing issues. The documentation requirements on transfer pricing are enacted in Section 90 Paragraph 3 of the General Tax Code.

The Base Erosion and Profit Shifting (BEPS) Action Plan adopted by the OECD and G20 countries in 2013 and implemented into German law in December 2016 has as its main purpose enhancing transparency for tax administrations by providing them with adequate information for a high-level risk assessment to tackle BEPS. In order to implement the three-tiered transfer pricing documentation approach into German law, amendments to the existing section 90, paragraph 3 of the General Tax Code (“Abgabenordnung” or “AO”) and the introduction of a new section 138a of the AO have been made. This effectively requires German resident companies under certain circumstances to prepare the following documentation: Master File and country-specific company-related documentation, i.e. Local File as well as a CbC report.

The German tax administration uses this data especially for ICAP, risk analysis, statistical analysis, and for the determination of focus areas for a tax audit. In the explanations provided to the law, the use of the CbC report for purposes of applying global formulary apportionment was explicitly rejected, as the type of information included therein is not seen to be sufficient to test the arm’s length nature of intercompany transactions. In this respect, in case the receiving country misuses the information for purposes of formulary apportionment, the exchange of CbC reports can be temporally stopped.

The CbC reporting requirements under BEPS Action 13 form one of the four BEPS minimum standards. Each of these minimum standards is subject to peer review in order to ensure timely and accurate implementation. All members of the Inclusive Framework on BEPS,[42] including Germany, commit to

implementing the Action 13 minimum standard on CbC reporting, and to participating in the peer review. According to the phase 1[43] and 2[44] annual peer review reports, Germany's implementation of the Action 13 minimum standard meets all applicable terms of reference.

### b) Definition of Related Party

The definition of related parties is established in Section 1 of the Foreign Tax Act, which states that parties are regarded as related if one party participates directly or indirectly in the management, control or capital of the other, or where a third party participates directly or indirectly in the management, control or capital of both of them, or where the same persons or their close relatives participate in management or control of the other. A minimum direct or indirect participation of 25% is required in order to create an affiliate.

### c) Nature of Transfer Pricing Documentation

On January 1, 2008, detailed TP requirements covering cross-border transfer of functions were integrated into 1 Foreign Tax Act. From 2008, an Executive Order Law detailing how the new TP regulations apply to firm restructurings and function transfers is in effect.

The authorized OECD approach (AOA) on the allocation of earnings to permanent establishments has been incorporated into German legislation as of 1 January 2013 by a statute amending 1 Foreign Tax Act.

An Executive Order Law was issued in October 2014 regarding the application of the arm's-length principle to permanent establishments. For fiscal years (FYs) commencing after December 31, 2014, the Executive Order Law applies.<sup>1</sup>

### d) Tax Havens & Blacklists

Germany is stepping up its efforts to combat tax havens. Olaf Scholz, the Finance Minister, has stated that he intends to "dry up" tax havens.<sup>2</sup>

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<sup>1</sup> [ey-worldwide-transfer-pricing-guide-10-september-2020 \(2\).pdf](#), p.233.

<sup>2</sup> [Germany is taking stronger action against tax havens - Teller Report](#)

### e) Advance Pricing Agreement (APA)

On 5 October 2006, the German tax authorities published Administrative principles on APAs in order to give tax authorities and the taxpayer better guidance for the handling of APAs. APA agreements are valid between 3 and 5 years.

Section 178a of the General Tax code contains a fee of generally €20,000 for an APA request, €15,000 fee for the renewal of APAs and a €10,000 fee for the modifications during the term of the APA. Reduced fees for SMEs are possible.

### f) Audit Practice

Transfer pricing has been an area of high interest for tax administration in the last years in Germany. The risk of transfer pricing audits has increased lately, as the German tax authorities consider transfer pricing as part of a taxpayer's tax audit or risk assessment. Looking at past audits, companies that have received particular attention are entities that incur losses or that earn relatively low margins. Also, a special focus has been offered to scrutinize transfer and licensing of Intellectual property (IP) between related parties. Tax authorities have strict requirements regarding transfer pricing documentation and in compliance to the requirements entities the tax authorities to perform transfer pricing adjustments to the less favorable end of the range for the taxpayer or assess penalties. Financial transactions are also under high scrutiny, looking at examples of exit taxation, cash pool synergy profits and umbrella brand names licensing.

## 3. Transfer Pricing Documentation

### a) Level of Documentation

The German documentation rules oblige taxpayers to document the nature, content and extent of cross-border transactions with related parties, as well as the economic and legal basis for the determination of prices, which are in line with the arm's length principle. The taxpayer has to prepare the documentation contemporaneously for extraordinary transactions, such as restructuring or a shift of functionality.

The taxpayer has to document if the outcome of those transactions follows the arm's length standard, including a detailed analysis of business functions performed, assets used and risks assumed, selection and application of the most appropriate transfer pricing methodology.

Germany follows generally the BEPS approach and has implemented a three-tier approach consisting of Masterfile, Local file and Country-by-Country-Reporting (CbCR).

According to section 4, paragraph 2 of the Decree Law on Transfer Pricing Documentation, a local file needs to provide the following information:

1) general information about ownership structure, operations and organizational structure:

- representation of ownership structure between the taxable person and related persons in terms of section 1, subparagraphs 2(1) and 2(2) of the AStG, with whom the taxpayer maintains business relations (whether directly or through intermediate persons) at the beginning of the audited period, as well as relevant changes up to the end of such period;
- representation of other circumstances which may justify “associated” in terms of section 1, subparagraph 2(3) of the AStG;
- representation of the organizational and operational structure of the group, as well as relevant changes, including permanent establishments and shares in private partnerships;
- description of management structure, as well as organizational structure (organization chart) of the domestic business of the taxpayer; and
- description of the areas of activities of the taxable person and the business strategy at the beginning of the audit period, as well as relevant changes within the audit period.

2) taxpayer’s business relations:

- representation of the taxpayer’s business relations, overview of the type and scope of these business relations (e.g. purchase of goods, services, loan contracts and other cessions of rights of use, cost allocations) and executive summary of the contracts underlying business relations and relevant amendments; and
- executive summary (list) of the essential intangible assets owned and used by the taxpayer in his business relations or assignment of rights of use;

3) functional and risk analysis:

- information on the functions performed by the taxpayer and the related parties within their relations and assumed risks as well as relevant changes in these functions and risks, information on the essential assets, on agreed contractual terms and conditions, selected business strategies and the significant market and competitive conditions; and
- description of the value chain and representation of contributions made by the taxpayer to the value chain;

4) transfer pricing analysis:

- time of setting transfer prices;
- records of the significant information available and used at the time of setting the transfer price;
- representation of the applied transfer pricing method;
- rationale of the applied method as for choice and suitability;
- documents about the calculations for the application of the preferred transfer pricing method; and
- executive summary and description of the comparable (internal or external) transactions applied.

In addition, section 4, paragraph 2 of the Decree Law on Transfer Pricing Documentation specifies that – for certain cases – in addition to the above-mentioned information, the following information has to be provided:

- information about special circumstances such as benefit-sharing measures, as far as they may affect the taxpayer's transfer pricing calculation;
- in the case of cost sharing: contracts, where appropriate in conjunction with annexes, exhibits and supplementary agreements, documents about the application of the allocations and the expected benefits for all the parties involved, as well as (at least) documents about the type and scope of audit, about adapting to changing conditions, access to the documentation of the company which is a services provider, assignment of user rights;
- information about proposed or executed mutual agreements or arbitration proceedings in other countries and unilateral transfer price agreements, as well as other pre-tax deductions for tax purposes prescribed by foreign tax administrations which affect taxpayer's business relations.
- records of price adjustments of the taxable person, even if they are caused by transfer pricing adjustments or obligations imposed by foreign tax authorities on the taxpayer or its affiliated persons;
- records of the reasons for losses and arrangements of the taxpayer or its affiliated persons to rectify such a situation if the taxpayer reported a tax loss for more than three consecutive business years; and
- records of research projects and ongoing research activities, which may be related to a functional change and which occurred or were accomplished within 3 years preceding the functional change in the event of functional or risk changes in terms of section 3, paragraph 2 of the Decree Law on Transfer Pricing Documentation shall include at least information on the exact subject of research and all the related costs. This only applies if a taxable person regularly performs R&D activities and issues relevant documents from which these records can be derived.

A Masterfile requires specification regarding the following information:

- graphical representation of the organization structure (legal and ownership structure) as well as the location of companies and branches of the MNE group in terms of section 90, paragraph 3 of the AO;
- overview of significant factors for the MNE group's consolidated profit;
- description of supply chains for the five products and/or services of the MNE group which generated the highest revenues (meaningful graphics or a corresponding diagram will suffice);
- description of supply chains for all other products and/or services of the MNE group, the share of which is above 5% of the MNE group's revenues (meaningful graphics or a corresponding diagram will suffice);
- list and summary of important service agreements between members of the MNE group (excluding R&D), including description of the capabilities of the main locations which provide

important services, as well as the pricing policy for the allocation of costs of services and the determination of the transfer prices for MNE group-internal services;

- description of key geographic markets for the products or services of the MNE group (see (3) and (4));
- high-level functional analysis which describes major contributions of each MNE group company to the value chain, i.e. key functions, important risks and material assets;
- executive summary of significant reorganizations of the company's MNE group referring to its activities within the business year, as well as a list and summary of acquisitions and sales of companies within the business year;
- general description of the overall strategy of the company's MNE group pertaining to intangible assets (development, ownership, protection and use), including a list of locations of the main R&D facilities and locations of the management of R&D activities;
- list of the intangible assets or groups of intangible assets of the company's MNE group that are important for transfer pricing purposes, as well as of the companies which are the legal owners or holders of these intangible assets;
- summary of important agreements among MNE group companies relating to intangible assets, including cost sharing agreements, essential contract R&D service agreements and license agreements;
- general description of transfer pricing policies of the MNE group, R&D policies, as well as policies pertaining to intangible assets;
- general description of all important transfers of rights to intangible values within the group, including relevant companies, countries and remunerations;
- general description of how the MNE group is financed, including the representation of major financial relations with third parties;
- description of the MNE group companies which perform central financing, cash or asset management functions with an indication of the law underlying the company's incorporation and actual place of management of the respective company;
- general description of transfer pricing strategy of the MNE group in relation to financing within the MNE group;
- consolidated financial statements of the MNE group for the relevant business year if the financial statements were prepared; and
- list and brief description of the existing unilateral advance transfer price agreements of the group, as well other agreements with the tax authorities in advance as regards the profit allocation between the countries.

## b) Industry Analysis

By identifying value drivers for the relevant industry, a first indication of the level of profitability common in the industry is being given.

### c) Company Analysis

A description of the management structure of the local entity, a local organisation chart, and a description of the individuals to whom local management reports and the country(ies) in which such individuals maintain their principal offices.

A detailed description of the business and business strategy pursued by the local entity including an indication whether the local entity has been involved in or affected by business restructurings or intangibles transfers in the present or immediately past year and an explanation of those aspects of such transactions affecting the local entity.

### d) Functional Analysis

In conducting a functional analysis, an assessment is made of the significant activities and responsibilities that are performed by the related parties relevant to the Intercompany Transactions under review, the tangible and intangible assets that are employed and the risks that are borne in undertaking the business activities. Such an assessment is consistent with the recommendations that have been made in the OECD Guidelines at paragraph 1.51.

### e) Choice of Transfer Pricing Method

Germany is a member of the OECD and follows the guidelines on transfer pricing in general. The transfer pricing methods specified in the German transfer pricing regulations are the same as in the OECD Guidelines: CUP, resale minus method, cost plus method, TNMM and, in special cases, profit split methods. German tax authorities expect the most appropriate method to be applied, but not more than one method has to be applied to confirm that transfer prices are in line with the arm's length principle. Since 2008 the tax authorities have been making available a hypothetical arm's length test in case no other method is applicable. Taxpayers can apply this test especially for cases treating intangibles.

### f) Economic Analysis – Benchmark Study

If the tested party is located in Germany, comparables should ideally come from the German market, but Pan-European comparables are accepted. The administrative principles on procedures contain a special section with requirements for database searches. Detailed information and data on German companies is available from a number of databases such as the Amadeus and other databases.

### g) Inter-company (IC) Legal Agreement

Although an Inter-company legal agreement formalizes the business and financial relationship between group entities, the legal agreements have a lower ranking since the OECD 2017 Guidelines made the “conduct of parties” the prevailing concept.

### h) Financial Statements

As previously stated, the CbC report’s required material is in accordance with OECD recommendations. There are no legal requirements in general for the underlying currency or accounts to be utilized, but the OECD’s recommendations must be followed. In particular, the reporting MNE should complete the template using the same sources of data year after year. Data from the reporting MNE’s consolidation reporting packages, distinct entity statutory financial statements, regulatory financial statements, or internal management accounts may be used in the first year. However, consistency of source must be observed in the coming years. For CbC reporting, the majority of German MNEs have employed the group operational currency and group accounting.<sup>3</sup>

There is no specific guidance on the financials to be used, according to section 138a of the AO. The legislator demanded the use of the group’s financials when the bill was first introduced, but this portion was later eliminated to allow for more freedom.<sup>4</sup>

### i) Production Process for TP Relevant Returns, Documents, Forms and Financials

In the chart below, the existence of the filing requirements with the details of which format is used, the latest filing date, notification requirement and its deadline, thresholds to be applied in case it exists, and the required languages are demonstrated. This information can be seen respectively for CIT, master file, local file, CbCR, local forms, annual accounts and segmented P&L documentations.

	Prepare or File?	Format	Deadline	Notification Deadline*	Threshold* (Yes/No)	Local Language (Yes/No)*(If “No”, it can be filed in English)

<sup>3</sup> [Document - Germany - Transfer Pricing - 13. Documentation Requirements - Tax Research Platform - IBFD](#), para. 13.2.3.

<sup>4</sup> Document - Germany - Transfer Pricing - 13. Documentation Requirements - Tax Research Platform - IBFD, Para. 13.2.10.

<b>Corporate Income Tax</b>	File	Local requirements	31 July	No	Yes	No
<b>Master File</b>	Prepare	OECD Guidelines 2017	The submission of records must be completed within 60 days, after the tax authority's request	No	Yes	No
<b>Local File</b>	Prepare	OECD Guidelines 2017	The submission of records must be completed within 60 days, after the tax authority's request	No	Yes	No
<b>CbCR</b>	File	Electronically	1 year after the end of the relevant fiscal year	31 July	Yes	No
<b>Local form</b>	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.

<b>Annual Accounts</b>	File	Electronic format	12 months after the last closing date	No	Yes	No
<b>Segmented P&amp;L</b>	GAAP	Excel/Other	Ready upon filing CIT/TP documents	No	No	No
* Germany has signed the MCAA agreement for the filing of CBCR.						
* Germany does not request as much and detailed information from smaller and less complex enterprises (SME's included) than it does from large and complex enterprises.						

### j) Mandatory Language

In general, documentation must be prepared in German language, but documents in English are accepted by the tax inspector. Taxpayers need to be prepared to provide a translation of the documentation, upon request.

### k) Notification Requirement

Not applicable.

### l) Record Keeping

Taxpayers have in general to keep records for ten years (Section 147 General Tax Code). The Administrative Principles on Procedures follow this general rule and require that relevant transfer pricing documents have to be stored in this manner – therefore, transfer pricing documentation has to be stored in electronic or written form in general for ten years. For the use of electronic records, there exists a separate administrative regulation: Grundsätze ordnungsmäßiger DV-gestützter Buchführungssysteme (GoBS) last amended in 2015.

### m) Penalties and Interest Charges

Germany has established a penalty regime in 2003 in Section 162 of the General Tax Code, with effect from 2004. Penalties must be raised as a surcharge of 5 to 10% of a profit adjustment with a minimum of €5,000. In cases where a taxpayer presents documentation which is in general usable for a tax

auditor, but presented after a set deadline, penalties of up to €1 million are possible, with a minimum of €100 for each day the 60-day time limit is exceeded.