News International

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Dear Sir or Madam,

In its ruling dated 10/23/2018 (I R 54/16), the German Federal Court of Finance (BFH) made a decision about the issue still outstanding at the highest federal court, on whether the managing director of a foreign corporation can qualify as its permanent representative within the meaning of Sec. 13 German Fiscal Code (AO). Until now, the fiscal courts and literature have disagreed on whether representative bodies could establish a connecting factor in Germany in order to be subject to limited taxation.

The previous instance, the Fiscal Court of Rhineland-Palatinate (FG) rejected such a connecting factor on the grounds that the activities of the managing director and the activities of a permanent representative are mutually exclusive. It held the position that representation requires the representative to act instead of the company, while a managing director's actions are legally classified as their own and not on behalf of the company. The other position argues that this view of civil law is not relevant for tax purposes and a managing director may act as both a representative body and a permanent representative. Contrary to the opinion of the previous instance, the BFH has now adopted the latter position.

Specifically, the case concerned the managing director of a stock company based in Luxembourg, who regularly spent time in Germany for business. The company itself did not set up a permanent establishment in Germany. In the past, the BFH had decided that the owner of a company could not be their own permanent representative at the same time. However, this case-law applies to sole proprietorships. The principles do not cover

Furthermore, according to the wording of the AO – as e.g. Sec. 34 (1) and Sec. 79 (1) No. 3 AO show - the activities of a body are to be considered the activities of the representative. Another argument against the application of the executive body theory is that Sec. 13 AO mainly targets foreign companies and their legal systems often do not know this theory.

The BFH referred the matter back to the FG. First, it had to be clarified whether the representative sustainably worked for the foreign company, which would require activities to be planned and regular to a certain extent. Secondly, the question arose whether, and if so, to what extent the double taxation treaty with Luxembourg limits any existing tax claim in Germany.

The decision is likely to be important particularly in the cases in which a (management's) permanent establishment of the foreign corporation is not established in Germany. This affects all foreign companies which are active in Germany through members of their management board. Luckily, not every single, occasional or temporary activity in Germany is sufficient to trigger a limited tax liability. Sec. 13 AO requires "sustainable" work. Each individual case must be reviewed as to when an activity exceeds the time limit and triggers limited tax liability.

If you have a managing director of a foreign company working in Germany, please contact us. We will be happy to advise and help you!

Best regards

to representation by legal entities. Ultimately, this theory - according to which the activities of the representative bodies of legal entities are to be attributed to them as their own activities - does not prevent the application of the rules governing representation under civil law.

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Company presentation

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