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The Business Commitment of a Norwegian Company in Germany

An Examination from a Tax Perspective

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Abstract

The German market is large and of great economic importance for Norway. A detailed understanding of the German tax system and the cross-national regulations between Germany and Norway are necessary for Norwegian companies who assess investment projects in Germany. This thesis aims to provide this information. It may also serve as an introduction to the topic for civil servants in the Norwegian Tax Administration who deal with companies that have German affiliates.

The results are achieved by conducting a comparative examination of the different investment alternatives from a tax perspective. The underlying analysis is initially defining significant tax aspects of investment decision as a common frame of references. Subsequently, the thesis provides an overview of the various legal forms. Given this framework, a legal model is applied that allows the comparison of the different investment alternatives. In this way, the tax consequences within the significant aspects are highlighted for different investment approaches.

The findings of this analysis indicate that in case a Norwegian individual person is planning a long-term investment in Germany and expects positive returns which shall be reinvested in Germany, a subsidiary in form of a corporation has advantages in regard to current taxation. If a Norwegian corporation intends to generate a capital gain through the subsequent disposal of its German operations, the investment alternative of a corporation leads to zero taxation. Yet, the examination shows also that the choice of the investment alternative has in some instances no significant tax effects. Thus, also aspects other than taxation should be considered.

This thesis provides valuable insights for the choice of an appropriate investment alternative in Germany. However, due to the different characteristics of a Norwegian company and its German business venture, the results are not universal applicable and should be evaluated in consideration of the individual situation.

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List of Abbreviations

§	Paragraf (article)
AG	Aktiengesellschaft (public limited company)
AO	Abgabenordnung (fiscal code)
Art.	Article
AStG	Außensteuergesetz (foreign transaction tax act)
DTA	Double taxation agreement
DTA GerNo	Double taxation agreement between Germany and Norway
EC	Treaty of the European Community
ECJ	European Court of Justice
EEA	European Economic Area
EStG	Einkommensteuergesetz (personal income tax act)
Ger	Germany
GewStG	Gewerbesteuergesetz (municipal trade tax act)
GewStR	Gewerbesteuer-Richtlinien (municipal trade tax directives)
GmbH	Gesellschaft mit beschränkter Haftung (private limited company)
GmbH & Co. KG	Gesellschaft mit beschränkter Haftung & Co. Kommanditgesellschaft (limited partnership with a corporation as general partner)
HGB	Handelsgesetzbuch (code of commercial law)
incl.	Inclusive
KG	Kommanditgesellschaft (limited partnership)
KStG	Körperschaftsteuergesetz (corporate tax act)
M&S	Marks and Spencer
No	Norway
Nr.	Nummer (number)
OECD-MC	Organisation for Economic Co-operation and Development – Model Convention
OHG	Offene Handelsgesellschaft (general partnership)
p.	Page
pp.	Pages
S.	Satz (sentence)
SolZG	Solidaritätszuschlaggesetz (solidarity surcharge act)
UmwStG	Umwandlungssteuergesetz (reorganisation tax act)

1. Introduction

The well management of Norway's natural resources and sound economic policies contribute to one of the world's highest standards of living. The export of crude oil and natural gas constitutes the largest share in foreign trade and led to an enormous accumulation of wealth.[1] Even though these aspects create a very potent market, the domestic growth opportunities are limited to its absolute size. In order to increase the sales potential, an expansion to foreign markets represents an obvious solution. Since the European Union is the receiver of 80 % of the Norwegian exports, it constitutes the most essential market abroad. Besides of Sweden, Great Britain and the Netherlands, Germany is especially recognized as one of Norway's most important trading partners. Over 10 % of the Norwegian exports go to Germany and the relationship between both countries is characterized by broad political, cultural and economic cooperation.[2]

On the base of this well-established partnership, the German market provides great opportunities for Norwegian companies. Less affected by the recent worldwide economic turmoil, Germany has not been facing a serious recession and its financial stability is beyond all doubts. The return to new growth opens up once again great business opportunities in Europe's biggest market.[3] In order to seize these opportunities without exposing oneself to the risk of the unknown, a profound knowledge about the country's legal and political structure is essential. Especially a fundamental understanding of the German tax system is crucial in order to make sound investment decisions. In this regard, a Norwegian company with the intention to enter the German market should be aware that the legal form of its German operation is determining the type of taxation and affects the total tax burden.

With the aim to shed light on this highly complex part of German and international legislation, the thesis conducts a comparative examination of the different investment alternatives from a tax perspective. The underlying analysis is in a first step defining significant tax aspects of investment decision as a common frame of references. These factors consist of current taxation, the use of losses and the termination of engagement. Subsequently, the thesis provides an overview of the various legal forms and identifies the

[1] OECD, 2012, p. 3.
[2] Statistisk sentralbyrå, 2011, http://www.ssb.no/ur_okonomi/.
[3] Germany Trade & Invest, 2012, http://www.gtai.de/GTAI/Navigation/EN/Invest/Business-location-germany/economic-profile.html.

permanent establishment, the business partnership and the corporation as most relevant. Given this framework, a legal model is applied that allows the comparison of the different investment alternatives. In this way, the tax consequences within the significant aspects are highlighted for different investment approaches.

However, the German tax legislation comprises a broad field of different aspects and is known for being quite complex. In an international context, the variety of subjects becomes even more extensive and a comprehensive illustration of all characteristics is rather impossible. As a consequence, the examination of a topic should focus on the aspects that are crucial to address the problem. It might be necessary to analyse some context in great detail while other issues must be disregarded. In this respect, the author of the thesis intends to provide all necessary information in order to understand the coherences of the topic and examine the problem. A simplification of certain aspect can facilitate the understanding and draw the attention to the most important points. Thus, the author takes the following assumptions and sets certain limitations:

The applied German and international legislation is based on the 2012 versions. When presenting the personal income, corporate and municipal trade tax, the explanations are limited to the main points and the church tax is not considered. The example calculations disregard the progressive scale of the personal income tax and apply generally the maximal tax rate. Since a consideration of the progressive scale leads to a changing tax rate depending on the income, it would be impossible to provide universal valid results. In contrast to this, findings on the base of a marginal analysis in the highest progressive zone deliver general results and provide a meaningful indication for most companies. However, companies with a very low income are advised to conduct an examination in consideration of the progressive scale. Furthermore it is assumed that the personal income, corporate and municipal trade tax have the same taxable base and all example calculations start at a profit of € 100 with an invested capital of € 1,000. The municipal trade tax is presented in a simplified way and since the tax rate depends on the business location in Germany, a rounded average of 14 % is applied.

The application of the presented analysis under the just described condition delivers deep insights into the taxation of a Norwegian company in Germany. Among others, the results indicate that in case a Norwegian individual person is planning a long-term investment in

Germany and expects positive returns which shall be reinvested in Germany, a subsidiary in form of a corporation has advantages in regard to current taxation. However, if the main objective is to repatriate the profit instead of reinvesting it, an alternative without the foundation of a corporation might be the better choice. If a Norwegian corporation intends to establish a business in Germany in order to generate a capital gain through the subsequent disposal of its operations, the investment alternative of a corporation leads to zero taxation on the level of the Norwegian company and is thus superior to other forms of investment. Yet, the examination shows also that the choice of the investment alternative has in some instances, no significant tax effects. This is the case for a Norwegian company, in form of corporation with regards to current taxation and the use of losses. However, since the choice of an appropriate investment alternative depends on the individual characteristics of the Norwegian company and its German business venture, the results should rather be viewed as supportive guidelines instead of a universal truth for every situation. Thus, the purpose of the thesis is mainly to provide a Norwegian company with the necessary information in order to support sound investment decisions for its individual situation. In addition, the paper is not exclusively addressed to Norwegian companies, but also intended to equip the Norwegian tax authorities with new insights that could help them to facilitate internationally operating Norwegian companies.

In order to cover the topic of this thesis, an examination of German, international and Norwegian tax legislation is required. Since the topic of this thesis addresses a market entrance of a Norwegian company in Germany, the focus is, however, on the German tax aspects. Thus, this thesis provides well-founded explanations of German tax regulations. In comparison to this, the Norwegian tax legislation is presented briefly and in a ‘results-driven’ manner and should be considered as additional information that increases the value of the main findings.

During the work on this topic, the author experienced that many legal terms in German lack a clearly defined translation. In order to support the objectives of this thesis, a small ‘dictionary’ about the vocabulary of the thesis is provided. In this way, terminological misunderstandings are avoided. In addition, a vocabulary list might be helpful for interested readers who would like to deepen their knowledge in the addressed topic. Especially, because the translation of German tax legislation is still rather incomplete or outdated.

In regard to the quotation of legal text, the author is following as far as possible the system of the respective legislation. Thus, the quotation of German, international and Norwegian legislation can differ in their form. This is done in order to simplify the detection of the corresponding paragraphs in the various legal codes. When quoting German legislation, the commonly used symbol of '§' is used for 'articles'. Furthermore, the number in the bracket is indicating the paragraph while the number of the sentence in a continuous text is labelled with 'S.' for 'sentence'. In case of a numeration, the abbreviation 'Nr.' is used for the number.

Last but not least, since this thesis examines the business commitment of a Norwegian company in Germany, it is crucial to define 'a Norwegian company'. For the purpose of this thesis, the term 'Norwegian company' shall refer to a Norwegian business that is operating in form of a corporation or an individual person (sole proprietor). It is also possible that the Norwegian company is operating as a business partnership. However, since a Norwegian business partnership is not an own legal entity and since the Norwegian legislation is applying the transparency principle[4] (a detailed explanation follows), this thesis is recognising the partners in their original form. In this respect, the reference to an individual person or a corporation implies that both businesses could also operate via a business partnership.

The rest of this thesis is organised as follows. Section 2 describes the relevant principles of the German tax system for foreign investors and includes the double taxation agreement between Germany and Norway. Section 3 presents significant tax aspects of investment decision and Section 4 introduces the different investment alternatives. The following Section 5 examines the investment alternatives from a tax perspective. The results of this section are compared and evaluated in Section 6. The thesis ends with a summary and a conclusion in Section 7.

[4] Mörsdorf, 2011, p. 135.

2. Relevant principles of the German tax system

2.1. Relevant types of taxes for foreign investors

Benjamin Franklin said once: ‘In this world nothing can be said to be certain, except death and taxes.’[5] For most parts of the world this seems to be true. Taxes are part of our everyday lives and a considerable amount of our actions implicate tax consequences. The German tax system, generally known to be rather complex, consist of a variety of different kinds of taxes. The value added tax (“Umsatzsteuer”) and the income taxes (“Ertragsteuern”) constitute the base of the German taxation system and generate the major part of the state’s revenue.[6] While the value added tax is taxing the end-consumer of goods and services, the income taxes are generally levied on income of individuals and businesses. Even though a Norwegian company must obviously also deal with the value added tax, the topic of this thesis is addressing the taxation of business income. In this respect, the three most relevant types of taxes are the personal income tax (“Einkommensteuer”), the corporate tax (“Körperschaftsteuer”) and the municipal trade tax (“Gewerbesteuer”).[7] Following paragraph explains the principles of the three most relevant income taxes and provides answers to the crucial questions of *who* is liable and *what* is subject to taxation as well as *how* the tax is levied and in what way the *actual amount* is formed.

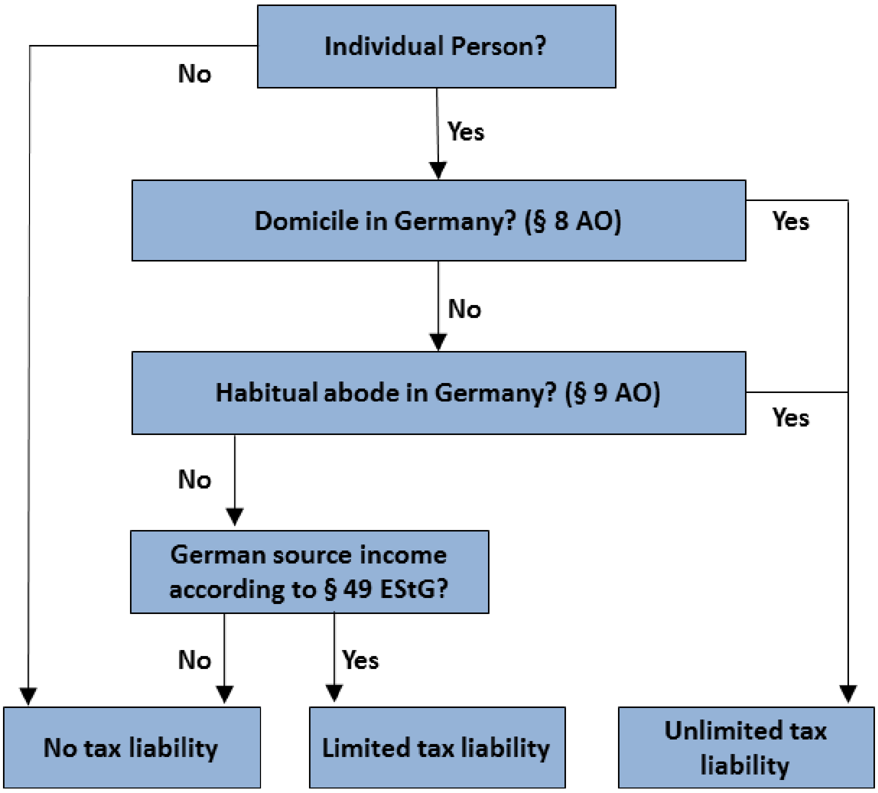
2.1.1. Personal income tax (“Einkommensteuer“)

The personal income tax is taxing the income of individual persons and is primary regulated by the German income tax act (“Einkommensteuergesetz”, EStG). The legislation of the EStG differentiates between an unlimited and limited tax liability (§ 1 EStG), whereas the nature of the tax liability is especially determining the extent of taxation. All individual persons who are domiciled or have their habitual abode in Germany are unlimited liable for taxation (§ 1 (1) EStG). A domicile is presumed if the individual person has its permanent accommodation in Germany (§ 8 AO), while a habitual abode is established by a physically presence in Germany for more than six month (§ 9 AO). If these requirements are fulfilled, the individual person is liable for personal income tax on its worldwide income (world

[5] Gerhart, 1998, pp. 263.
[6] Bundesministerium der Finanzen, 2012a, http://www.bundesfinanzministerium.de/Content/DE/Standardartikel/Themen/Steuern/Steuerschaetzungen_und_Steuereinnahmen/2012-05-29-steuereinnahmen-nach-steuerarten-2010-2011.html.
[7] Beeck, 2012, p. 11.

income principle) (§ 2 (1) EStG).[8] Individual persons with certain German income but without their domicile or habitual abode in Germany are limited liable for taxation with their German source income according to § 49 EStG (territorial principle).[9] The just described system of personal income tax liability is illustrated in the following graph:

Figure 1: Personal income tax liability



Source: Own illustration, based on Tanski, 2009, p. 11.

Subject to the personal income tax is the generated income of an individual person in the tax assessment period. According to § 2 (7) EStG the assessment period is a calendar year. The taxable base is the so called 'taxable income' ("zu versteuerndes Einkommen") which includes generally all relevant income from domestic and foreign sources. The relevant income is based on seven different sources of income which are specified as a conclusive list in § 2 (1) EStG:

- Income from agriculture and forestry (§ 13 EStG),
- Income from trade and business (§ 15 EStG),
- Income from independent personal services (§ 18 EStG),

[8] Beeck, 2012, pp. 11–12.
[9] Schneeloch, 2011, p. 52.

- Income from employment (§ 19 EStG),
- Income from capital investment (§ 20 EStG),
- Income from rentals and leases (§ 21 EStG),
- Other income from incidental activities (§ 22 EStG).

These seven types of income have among others considerable differences in regard to the scope of the tax, the determination technique and the use of losses. Therefore is it crucial to allocate the income to the appropriate category.[10] Since income has regularly common characteristics, a clear allocation is often not possible. In such a case, it may primarily be allocated to the first three categories.[11] For example, income from dividends from shares, purchased in a business context, may rather be allocated to ‘income from trade and business’ than ‘income from capital investment’. Within the different sources of income, business expenses, if correctly documented and necessarily incurred, can be deducted. Only the resulting net income is subject to taxation. In this way, the German regulations to personal income taxation follow the so called ‘net principle’ (“Nettoprinzip”). The net sum of the seven types of income forms the ‘total income’ (“Summe der Einkünfte”), which is the general base of the taxable income.[12]

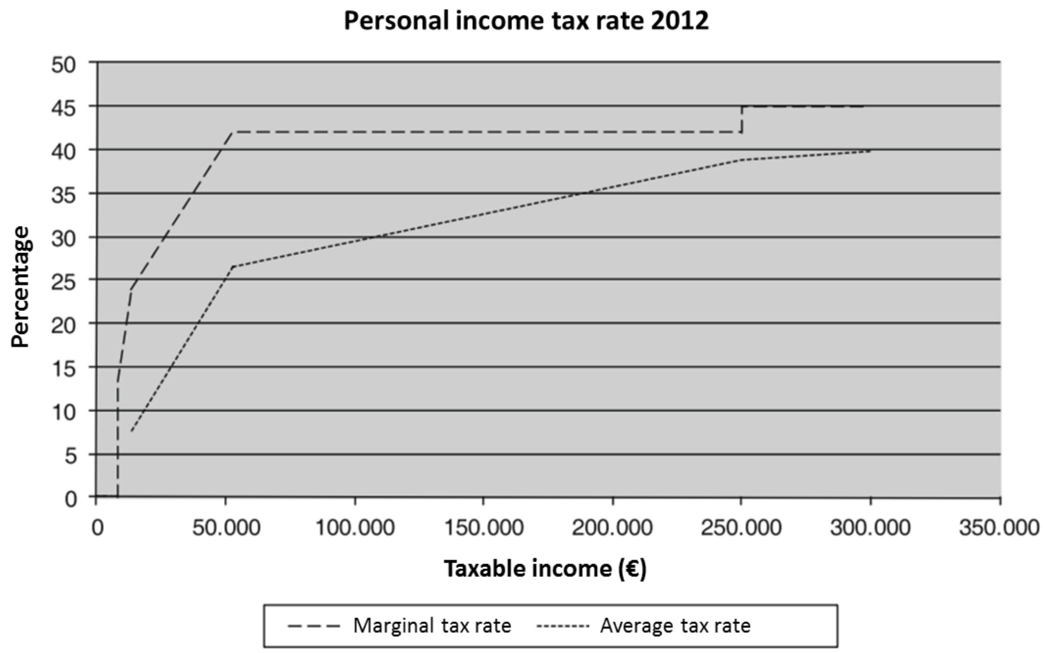
Beside the business expenses, the German income tax legislation allows the deduction of certain non-business expenses (§ 10 EStG). These special non-business expenses are considered as especially meaningful by the tax authorities and can be deducted from the cumulated net incomes. Typical examples for such non-business expenses are social security contributions, costs of professional training or contributions to charity. The deduction of the private expenses is subject to explicit rules and their reliefs are often limited to certain amounts.[13]

The deduction of the allowable non-business expenses results eventually in the taxable base of the personal income tax. In order to compute the individual tax burden, the taxable income is multiplied by an individual tax rate. In order to adjust the individual tax burden to the economic capacity of the individual person, the tax rate is based on a progressive scale.[14]

[10] Beeck, 2012, p. 12.
[11] Jäschke, 2012a, recital 78.
[12] Schneeloch, 2011, p. 89.
[13] Beeck, 2012, pp. 30–32.
[14] Schreiber, 2008, pp. 6–7.

The use of a progressive scale leads to rising tax rates by rising income. The German income tax rate for 2012 is, as defined in § 32a (1) EStG, constructed in the following manner: Income within the basic allowance of € 8,004 is exempt from taxation. The tax rate for income exceeding € 8,004 is rising in two linear-progressive zones from an initial tax rate of 14 % to a maximum tax rate of 42 %. Income of € 52,882 or above is taxed by a constant tax rate of rate of 42 % (proportional zone). Since 2007, particular high income is subject to an increased tax rate of 45 %. The additional 3 % tax applies to income from € 250,731. The marginal tax rate in the two linear-progressive zones is increasing linear with different slopes. In the upper proportional zones, the marginal tax rate is constant. The average tax rate consists of only three linear progressive zones and is generated by dividing the total tax burden by the taxable income. The marginal tax burden increases with rising income and approaches for very high income the maximal tax rate.[15] Following graph is illustrating the marginal and average tax rate of the personal income tax:

Figure 2: Marginal and average tax rate of the personal income tax



Source: Own translation of Beeck, 2012, p. 36.

All income that is included in the catalogue of § 2 (1) EStG is generally liable to personal income tax. However, income from capital investment is treated in a special way. The tax on this type of income is levied via the so called 'withholding tax on capital investment'

[15] Bundesministerium der Finanzen, 2012b, pp. 56–57.

("Kapitalertragsteuer"). In contrast to the other income categories, income from capital investment is not included in the sum of the taxable income and is not taxed with the above explained tax rate. Instead, it is taxed by a flat rate withholding tax of 25 % (§ 43 EStG). As the name implies, the tax has to be withheld at source by the distributer of the income and a deduction of any expenses is not possible (§ 44 EStG). Later paragraphs of the thesis will provided more detailed information about the withholding tax on capital investment which is also referred to as 'flat rate tax' ("Abgeltungssteuer") in Germany.

In addition to the personal income tax, a so called 'solidarity surcharge' ("Solidaritätszuschlag") of 5.5 % is levied on the tax burden of the personal income tax. Due to its surcharge characteristics, it seems to increase the personal income tax. However, the solidarity surcharge is a legally separate tax and has its regulatory base in the 'solidarity surcharge act' ("Solidaritätszuschlaggesetz", SolZG). The solidarity surcharge has it origin in the German reunification and the declared political purpose of financing economic development in East Germany.[16]

In the Germany system of personal income tax, the income of a married couple is joined together. In such a case, the assessment of the combined income is handled in a way as though each spouse had earned half of the total (§ 32a (5) EStG). This so-called 'splitting' system enables a married couple to optimize the use of allowances and thereby benefit from the lowest possible progressive tax rate.[17] For persons with only limited tax liability in Germany, the splitting system is generally not relevant.

Since 2008, the German tax authorities provide in the regulations of § 34a EStG the possibility of a preferential tax treatment of retained profits from agriculture and forestry, trade and business as well as independent work. Up on request, the undistributed profit is subject to a reduced tax rate of 28.25 % plus solidarity surcharge instead of the individual tax rate of the taxpayer.[18] In this regard, it must be noted that it is not possible that the whole profit is taxed with the preferential tax rate. The reason for this is that the tax burden itself is considered as distributed and not reinvested. In case the individual person is operating via a business partnership, an application to the preferential tax rate is only possible if the profit

[16] Schreiber, 2008, p. 71.
[17] Horlemann, 2012, recital 93.
[18] Gragert/ Wißborn, 2007, pp. 2551–2554.

share is greater than € 10,000 or exceeds 10 % of the total profit. If the retained profit is distributed in later years, a subsequent taxation of 25 % is levied.[19] The preferential tax treatment serves the purpose to equalise the tax burden of retained profits for individual persons and corporations. However, the rather new regulation is due to its considerable complexity and other aspects very controversial among experts.[20] It is very questionable to which degree the regulation of § 34a EStG is attractive for foreign investors. Nevertheless, the author of this thesis decided to include the preferential tax treatment of retained profits in order to provide a complete picture and will later on give some brief comments on its limitations.

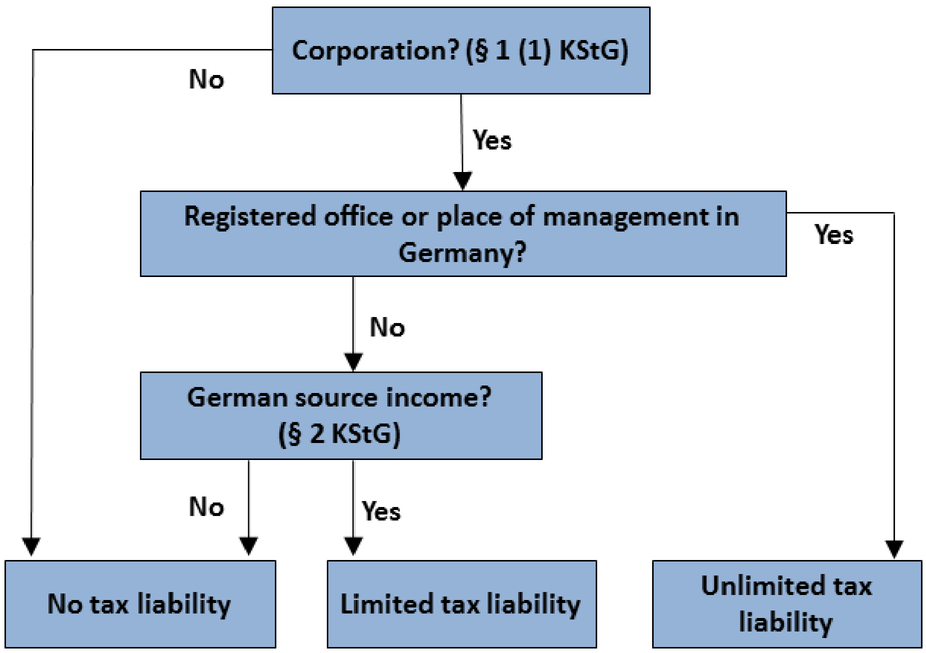
2.1.2. Corporate tax ("Körperschaftsteuer")

All corporations with their registered office or place of management in Germany are considered to be resident in Germany. As in the case of personal income taxation, the status as a resident is resulting in a tax liability on their worldwide income (unlimited tax liability) (§ 1 KStG). Foreign corporations without their registered office or place of management in Germany are deemed to be non-residents. Non-resident companies are only taxable with their German source income (limited tax liability) (§ 2 KStG). Since the corporation itself is subject to taxation, there is a strict fiscal separation between the corporation and the shareholder.[21]

[19] Gragert/ Wißborn, 2007, p. 2566.
[20] Van Heek, 2010, p. 508.
[21] Schreiber, 2008, p. 76.

Following graph is illustrating the determination of the corporate tax liability:

Figure 3: Corporate tax liability



Source: Own illustration, based on Tanski, 2009, p. 69.

As already seen in the similarities regarding residence and taxability, the corporate tax act ("Körperschaftsteuergesetz", KStG) is generally based on the regulations of the personal income tax. Thus, the corporate tax is sometimes referred to as the 'personal income tax for legal persons.' However, in addition to the basic principle of the personal income tax, the legislation of the corporate tax is supplemented by special rules that serve the purpose to tax legal persons.[22]

The taxable base for the corporate tax is the taxable income (§ 7 (1) KStG). The determination of the taxable income has to be done in accordance to the regulations of the EStG and the KStG and follows the net principle. A corporation can generally achieve all kinds of incomes in the meaning of § 2 (1) EStG despite of income from employment. However, income from business corporations which are subject to an unlimited tax liability is always considered as income from trade and business (§ 8 (2) & § 1 (1) Nr. 1 KStG).

In contrast to the personal income tax, the corporate tax rate does not depend on the amount of the taxable income and is 15 % (§ 23 KStG). As with the income tax, a 5.5 %

[22] Tanski, 2009, p. 69.

solidarity surcharge is levied on the tax (§ 1 (1) SolZG), which results in a total tax burden of 15.8 %. At a first sight, the corporate tax rate seems to be very low. However, the after tax income after corporate tax is still on a company level and not yet available to the shareholders. When distributed from company to shareholder level, the profit is again subject to taxation.[23]

2.1.3. Municipal trade tax ("Gewerbesteuer")

The municipal trade tax is levied by the municipalities in parallel to the individual income and corporate tax (§ 1 GewStG). The purpose of the municipal trade tax is to compensate for the burden of the local businesses and constitutes the main source of income for the municipalities. Subject to taxation are not individual persons or corporate bodies, but the business establishment (business object) regardless of their legal form (§ 2 GewStG). Since the assessment base is derived from the pre-tax accounting profit, the municipal trade tax is considered as an income tax (§ 6 GewStG). [24]

Taxable base of the municipal trade tax are the 'trading profits' ("Gewerbeertrag") multiplied by the 'basic federal rate' ("Steuermesszahl"). The calculation of the trading profits is based on the regulations of the EStG (§ 7 GewStG). However, in order to fulfil its purpose to tax the business object and not the individual person or corporate body, several income adjustments apply in accordance to § 8 and 9 GewStG.[25] The basic federal rate is determined by § 11 (2) GewStG and is uniform nationwide 3.5 %.[26]

The municipal trade tax rate is set by the municipalities with a mandatory minimum rate of 200 % (§ 16 (4) S. 2 GewStG). The tax rate between the communities can vary significant. In towns with a population larger than 50,000 citizens, the tax rate ranges usually between 350 % and 490 %. Some smaller communities set a rate lower than 350 % in order to raise the attractiveness of their location and attract businesses. The national average amounts, however, to 387 % (2010 levels).[27] When combining the basic federal rate with the tax rate set by the municipalities, we arrive at an average of 13.545 %. For reasons of simplification, a

[23] Schreiber, 2008, p. 76.
[24] Beeck, 2012, pp. 57–59.
[25] Tanski, 2009, pp. 92–93.
[26] Braun, 2012, p. 153.
[27] Schneeloch, 2011, p. 177.

rounded average of 14 % is used as an effective municipal trade tax rate in the following parts of this thesis.

Individual persons and business partnerships are tax exempt up to an assessment basis of € 24.500 (§ 11 (1) S. 3 Nr. 1 GewStG). Other types of business entities, as corporations, are not eligible to the basic allowance. In case of a positive return, the municipal trade tax is a further burden in addition to the individual income and corporate tax. In order to set off this additional burden, individual persons can deduct the incurred trade tax from the personal income tax. The respective legislation to the deduction can be found in § 35 EStG and states that the allowance is calculated by multiplying the taxable base with the basic federal rate and 3.8. Consequently, in case the municipal trade tax rate is lower or equally 380 % a full compensation is possible. If the tax rate is higher than 380 %, the municipal trade tax constitutes an additional tax burden.

2.2. Double tax agreement between Germany and Norway

An economic engagement of a Norwegian company in Germany results (at least) in a limited tax liability on its German source income in Germany. At the same time, the worldwide income of the Norwegian company is subject to Norwegian taxation. In this way, the economic activities in Germany could lead to an undesired double taxation. Since double taxation hinders international trade and is in all respects undesired, national states enter into bilateral treaties with the purpose to prevent double taxation. These so-called double taxation agreements (DTA) avoid double taxation by granting generally only one contracting state the taxation rights for certain incomes. The other contracting state has then to renounce the exercise of its domestic taxation right. In case more than one country has a right of taxation, the DTA tries to mitigate the excessive tax burden by setting taxation limits or crediting rules.[28]

An important aspect of a double taxation agreement is that it cannot constitute a tax claim, but only restricts existing national tax laws. Whether or to what extent a state exercises its DTA sustained tax claim depends exclusively on its national law. In case the provisions of the national law are broader than the regulations of the DBA, the state may only tax within the limits set by the DBA. If the DBA regulations are, however, broader than the national

[28] Uwe Ritzkat, 2012a, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f114%2f000114016_0001_index.xml&aktion=DokumentAnzeigen.

provisions, the state may only exercise its taxation right in the scale of its national legislation.[29]

Also Germany and Norway have entered into such an agreement. Contractual base for the agreement is, as in most other countries, the OECD Model Convention (OECD-MC). The objective of the OECD-MC is a greater harmonization of bilateral tax agreements between member states. This is achieved by offering a contractual base with common definitions, classification, principles and interpretation of the DTA.[30] The OECD-MC is also providing a contractual structure that divides the treaty into seven main chapters. Also the DTA between Germany and Norway (DTA GerNo) is following this structure, including the following, for the topic relevant parts.

2.2.1. Scope and definitions

The first chapter (Art. 1 and 2) defines the scope of the convention by regulating which persons and taxes are covered. In this regard, Article 1 of the DTA between Germany and Norway states that 'this convention shall apply to persons who are residents of one or both of the Contracting States'. Thus, in order to find out whether the convention is applicable or not, the definition of a residency in chapter two must be examined:

'For the purpose of this Convention, the term "resident of a Contracting State" means any person who, under the laws of that State, is liable to tax therein by reason of his domicile, residence, place of management or any other criterion of a similar nature […]' (Art. 4 (1) DTA GerNo).

Since the topic of this thesis is discussing the entrance of a Norwegian company in the German market, we can assume a residency and thus a tax liability of the Norwegian company in Norway. As a result, the convention is applicable for the issue addressed in this thesis.

Besides of the determination of residency, chapter two of the convention is providing general definitions and clarifies the concept of a permanent establishment. According to Article 5 DTA GerNo, 'the term "permanent establishment" means a fixed place of business

[29] Brähler, 2012, p. 103.
[30] Ibid., p. 97.

through which the business of an enterprise is wholly or partly carried on'.[31] This definition is in later sections especially important in order to allocate the taxation right of business profits.

In regard to the coverage of the various taxes, Article 2 DTA GerNo states that the 'Convention shall apply to taxes on income and on capital imposed on behalf of a Contracting State […]'. On the German side, the personal income tax, the corporate tax and the municipal trade tax are explicitly mentioned. Thus, the DTA between Germany and Norway applies to all relevant taxes.

2.2.2. Allocation of income

Chapter three, the main part of the DTA, regulates in Article 6 to 21 the allocation of the taxation right of the various types of income. In other words, it regulates which contracting state(s) has the right to tax the profits from the different income categories. The three income types of business profits, dividends and capital gains are most relevant in order to address the topic of the thesis.

2.2.2.1. Article 7 Business profits

Since the vast majority of international economic activities falls under the income type of business profits, Article 7 is from significant importance.[32] According to its regulations, business activities are subject to taxation in the source country if a sufficiently close link with its economy exists. Such a sufficiently close link to the economy of the source country is assumed if the foreign company is maintaining a permanent establishment in the meaning of Article 5 DTA GerNo. In other words, if the Norwegian company is maintaining a permanent establishment in Germany, the taxation right of the income, generated by the permanent establishment is allocated to Germany.[33] Whether a permanent establishment is maintained or not can influence the tax burden. In case the foreign tax level is lower than the national, the formation of a permanent establishment abroad will be advantageous.

2.2.2.2. Article 10 Dividends

Article 10 is regulating the taxation right of 'dividends paid by a company which is resident of a Contracting State to a resident of the other Contracting State' (Art. 10 (1) DTA GerNo). The

[31] Günkel, 2011, recital 71.
[32] Brähler, 2012, p. 145.
[33] Kroppen/ Lieber, 2011, recital 6.

Article is distinguishing itself by allocating a taxation right to the country of residency as well as the country of source. However, in order to avoid an excessive tax burden, the regulations of Article 10 in combination with Article 23 are limiting the taxation right of both countries. Additionally, both mentioned Articles provide special regulations for a corporation holding shares in another foreign corporation. Such a constellation can extend to multiple levels of corporations participating in other corporations. A taxation of the distributed dividends on every level would lead to an extensive tax burden and double taxation. The regulation of Article 10 (3) DTA GerNo is solving or at least mitigating the problem by implementing the so called 'intercorporate privilege'.[34] Later on, the issue will be taken up again in other sections of the thesis.

2.2.2.3. Article 13 Capital gains

Within the DTA, a profit generated through the disposition of an asset is called capital gain and regulated in Article 13 GerNo. The purpose of this income category is the determination and taxation of hidden reserves.[35] Even though most countries consider capital gains as current income, it is not uncommon that some countries allocate the income to a special category. In this regard, Article 13 avoids a conflict of handling capital gains differently from the beginning on.[36] The allocation of the taxation right is carried out separately for the alienation of the different types of assets and can lead to different results.

2.2.3. Methods for elimination of double taxation

The OECD-MC is using two different formulations to allocate taxation rights. The first formulation 'shall be taxable only' is already limiting the taxation right for one of the both states and avoids double taxation. In contrast, the second formulation 'may also be taxed' is not excluding a country from the right to tax. In these cases, Article 23 is supplementing the articles in chapter three and limits the taxation rights and prevents thereby an excessive tax burden.[37] Article 23 of the OECD-MC (and also of the DTA GerNo) constitutes Chapter V and presents two different methods for the elimination of double taxation. The first alternative is the 'exemption method'. This method states that the country of residency has to tax exempt income from the source country. Applied to our topic, this means that taxable income,

[34] Grützner, 2011, recital 1–2.
[35] Brähler, 2012, p. 186.
[36] Gosch, 2011, recital 1.
[37] Brähler, 2012, p. 206.

generated by a Norwegian company in Germany is tax-exempt in Norway. However, the German source income might be considered in the Norwegian tax rate. In such a case we speak of a progression clause. The credit method, on the other hand, is not exempting the state of residency from taxation. Instead the state of residency calculates the tax according to the company's total income. This includes also income that is generated and taxed in the other state as long it is not already clearly exempt. Yet, as the name suggest, the state of residency allows a deduction of the tax that was paid in the other country. In other words, the German income of the Norwegian company is included in the tax calculation in Norway, but the tax paid in Germany can be subtracted from the Norwegian tax. Thus, the main different between the two methods is that the exemption method avoids double taxation by adjusting the income, while the credit method modifies the actually tax.[38]

[38] Grotherr, 2011, recital 12–17.

3. Significant tax aspects of investment decision

Tax considerations can be recognised as an especially important factor when taking decision on investments in other countries. The fiscal framework can have different effects in different situations. Depending on the nature (or focus) of the activity, some investment alternatives may be beneficial over others. In this regard, the next section is discussing significant aspects of decisions for investment alternatives.

3.1. Current taxation

Current taxation is generally the most important factor. This is especially the case when investments have a long-term character and positive returns are expected. Current taxation regulates the taxation of net income and determines the tax burden of profit repatriation to Norway. The latter aspect is of less importance, if long-term reinvestments are planned and no early profit repatriation is intended.

3.2. Use of losses

If a company's activities generate a loss, usually no income tax is levied. In this case, the crucial question is, if the losses have a tax-reducing effect in subsequent years in Germany or even in Norway. This aspect is especially important when high initial losses are expected or if no positive returns are anticipated in the near future (e.g. market development activities).

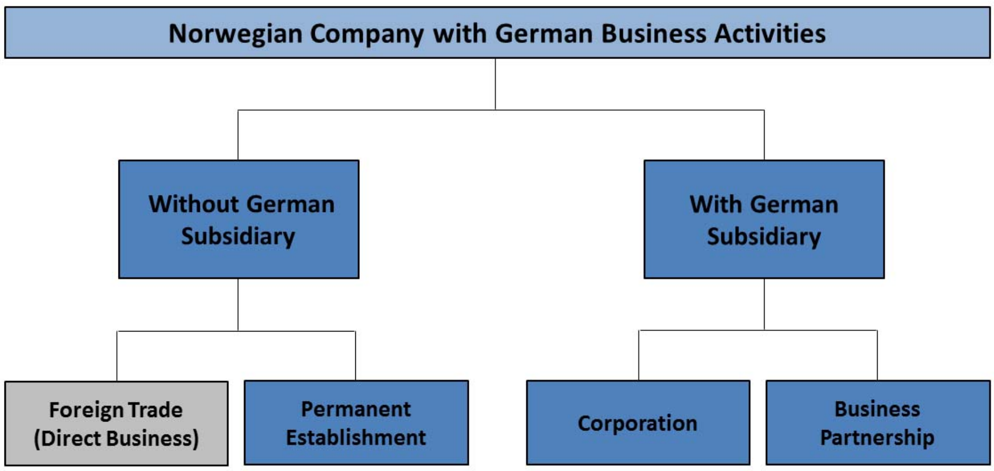
3.3. Termination of engagement in Germany

If the activities are laid out for a limited period of time only, tax consequences as a result of the termination of the engagement have to be taken into consideration. A termination can be performed by the complete disposal of the business in Germany or by simply stopping the foreign activity. As part of the termination process, individual assets might be transferred back to Norway. The consequential tax effects, as result of the asset relocation, should be taken into account when deciding on the investment arrangements. Once again, it should be kept in mind that it makes a difference if the termination results in the realization of a profit or if losses incurred.

4. Investment alternatives

A Norwegian company can decide between various investment alternatives when entering the German marked. It may establish its German operations as a corporation, business partnership or permanent establishment. The first two investment forms involve the establishment of a German company which have a distinct (at least limited) legal capacity.[39] Since we can assume that the Norwegian company has a managerial control over the German company, it is considered as a subsidiary. In case the Norwegian company would prefer to operate in Germany in its Norwegian form, a market entrance without the foundation of a Germany company is possible. In such a case, the Norwegian company can trade directly with the German market or establish a permanent establishment in order to operate from within the borders of the country.[40] Figure 4 is illustrating the different investment alternatives of the Norwegian company. 'Foreign Trade' is for the purpose of this thesis of less importance and only included to provide a complete picture.

Figure 4: Investment alternatives



Source: Own illustration.

The different investment alternatives can result in advantageous and disadvantageous aspects for the business. In order to achieve an optimal outcome, the pros and cons must be balanced in regard to the individual characteristics of the intended business venture. In this

[39] A business partnership is not a legal entity, but may still acquire rights and assume obligations. See paragraph 4.2.1 Business partnership.

[40] Haack, 2012, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f424%2f000424571_0001_index.xml&aktion=DokumentAnzeigen.

respect, the decision for the best possible legal form is dependent on a number of legal and managerial factors:

- Business purpose
- Minimum number of founders
- Seed capital (liable capital)
- Liability of shareholders/partners
- Distribution of profits, losses and liquidation proceeds
- Withdrawal possibilities for the shareholders
- Possibility of legal contracts between the company and the shareholders
- Business succession
- Accounting, auditing and reporting duties
- Tax and social security consequences

Generally, it is not possible to make a universal statement about the most beneficial investment alternative. The choice of a legal form is always a trade-off between the above mentioned factors and therefore highly individual. Thus, when starting a business, the decision shouldn't be based on a single factor. Instead, the founder(s) should choose a legal form which is flexible enough to serve the business in consideration of the predictable changes over time.[41]

Since there isn't a single tax on businesses, the German (and Norwegian) tax legislation affects the question of the optimal legal form. The taxation of a business partnership, corporation and permanent establishment can differ considerably. Two identical annual surpluses may result, depending on the legal form, in a completely different taxation.[42] However, it is not possible to make a general statement about an investment alternative with the lowest tax burden. It is rather necessary to compare the different tax burdens for every particular case. Furthermore, the legal form of the Norwegian company has to be taken into account in order to obtain a complete picture about the final tax burden after profit repatriation. For all these reasons, the Norwegian company should be aware about the

[41] Steinhoff, 2012, pp. 334 – 335.
[42] Ibid.

tax consequences of its choice.[43] The following paragraphs provide more detailed information about the characteristics of the different investment alternatives.

4.1. Without establishment of a subsidiary

In order to get active in the German market, the Norwegian company doesn't necessarily have to found a German company. In other words, the Norwegian company can also operate in its Norwegian formation in the German market. Certain operations might not even require an establishment in Germany. A classic example would be the sale and distribution of goods from Norway to the Germany. In such a case, the contact of the Norwegian business with German legislation would only be very limited. The same applies to taxation, Norwegian business activities without an establishment in Germany cause generally no income tax obligations (§ 1 EStG). Thus, the relevancy of this aspect is very low and will therefore not be further discussed.

If the market presence in Germany requires a physical existence of a facility, the resulting tax consequences might be surprisingly extensive. That occurs when the activities of the Norwegian company create a permanent establishment in Germany. In terms of commercial law, a physically separated and partly independent operating business section is considered as a branch if it's serving the objective of the whole company. A branch implies furthermore that it would be able to operate when separated from the central office and it has to be registered in the German commercial register (§ 13d HGB). The tax concept of a permanent establishment, on the other hand, is defined as 'any fixed place of business or facility that serves the operations of a company' (§ 12 S. 1 AO). In case the requirements are fulfilled, the existence of a permanent establishment results in a limited tax liability of its income from trade and business in Germany (§ 49 (1) Nr. 2a EStG).

The regulations of § 12 AO mention explicitly that branches are one possibility to operate through a permanent establishment in the sense of the German tax legislation. As a result, branches are subject to German taxation. However, the concept of a permanent establishment is generally broader defined and includes for example also warehouses, manufacturing or places of procurement and sales. As a consequence, all branches are

[43] Becker, 2006, pp. 27–30.

permanent establishments, while not all permanent establishments fulfill the requirements of a branch.[44]

The presence of a permanent representative of the Norwegian company in Germany has similar effects in regard to taxation as the existence of a permanent establishment. A permanent representative is defined as ‘any person who conducts the business of an enterprise in a sustained manner and, in so doing, is subject to its instructions’ (§ 13 AO). The regulations of § 49 (1) Nr. 2a EStG establish a limited tax liability for the German income from trade and business that is assignable to the permanent representative.[45]

Since the tax consequences in Germany are generally parallel to the one of a permanent establishment and since the DTA OECD-MC is considering the existence of a permanent representative as a factor establishing a permanent establishment (Art. 5 (5) DTA OECD-MC)[46], the author will for the rest of this thesis not particular refer to a permanent representative. However, in the following paragraphs, it should be noted that the consequences of the permanent establishment apply generally also to a permanent representative.

4.2. Establishment of a subsidiary

When founding a subsidiary in Germany, a Norwegian company can chose between different types of entities. Those regulate the legal relationship between the shareholders (internal relations) as well as the legal relationship between the company and the stakeholders (external relations).[47] Business partnerships and corporations are most relevant to a Norwegian company. Following paragraph describes the most important types of entity within these two major groups.

4.2.1. Business partnership

A business partnership is formed when at least two individual and/or legal persons join together to achieve a common purpose. Even though a partnership itself is not a distinct legal entity, it has similarities to a legal person and may acquire rights and assume

[44] Biechele, 2011, 877–878.
[45] Ritzkat, 2012b, http://www3.nwb-datenbank.de/nwb9/main.aspx?sid=1n21ld3r&kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f262%2f000262853_0001_index.xml&aktion=DokumentAnzeigen.
[46] Rader, 2012, recital 2.
[47] Wöhe/ Döring, 2010, p. 218.

obligations.[48] The structure of a business partnership is very much partner-oriented and (nearly) all of the different types of partnerships have the following common characteristics:

- All partners are personally liable for the company's debts, some even with their personal assets.
- Management and representation is usually carried out by the partners themselves.
- The entire assets of the partnership are collectively available to all partners. Decisions regarding the use of these assets must be reached in mutual consent.[49]

The following paragraphs give detailed information about the general partnership, the limited partnership and the limited partnership with a corporation as general partner. The presentation of the first two types of partnerships has the purpose to provide basic information about the functional principles of a business partnership. The third type of partnerships is considered as especially relevant to a Norwegian company with the intention to enter the German market. However, it should be noted that there exist more forms of business partnership than the three presented.

4.2.1.1. General partnership (OHG)

The general partnership ("offene Handelsgesellschaft", OHG) is in common use in Germany. The OHG pursues commercial goals in its own name and all partners are individual persons with unlimited liability for the partnership's debts. These so-called general partners have the joint right to manage and control the partnership. Since an OHG can acquire rights and assume obligations in its own name, it shows characteristics of a legal person. The legal base for the partnership is the German code of commercial law ("Handelsgesetzbuch", HGB) (§§105-160 HGB). Despite these regulations, many statutory provisions can be replaced by the partnership agreement.[50] Due to its commercial character in the meaning of § 1 HGB, an OHG is obliged to keep books and prepare a financial statement (§ 238 & § 242 HGB).

4.2.1.2. Limited partnership (KG)

Another widely used business partnership is the limited partnership ("Kommanditgesellschaft", KG). As with the OHG, a KG pursues commercial goals in its own

[48] Katla, 2006, p. 9.
[49] Gehrmann, 2012a, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f126%2f000126827_0001_index.xml&aktion=DokumentAnzeigen.
[50] Wöhe/ Döring, 2010, pp. 226–227.

name. According to § 161 (2) HGB, the KG is legally based on the regulation of the OHG. Unless an exception is particularly provided in § 161 to § 177a HGB, the legal framework of the OHG applies. The KG distinguishes itself from the OHG mainly through a second group of partners with a limited liability. These so-called limited partners are, unlike the general partners, only liable with their contractually fixed investment. The daily management of the KG is in principally reserved for the general partners, while the limited partners have the right of control and information only. However, as with the OHG, partners have far-reaching freedom to shape the partnership agreement according to their needs.[51]

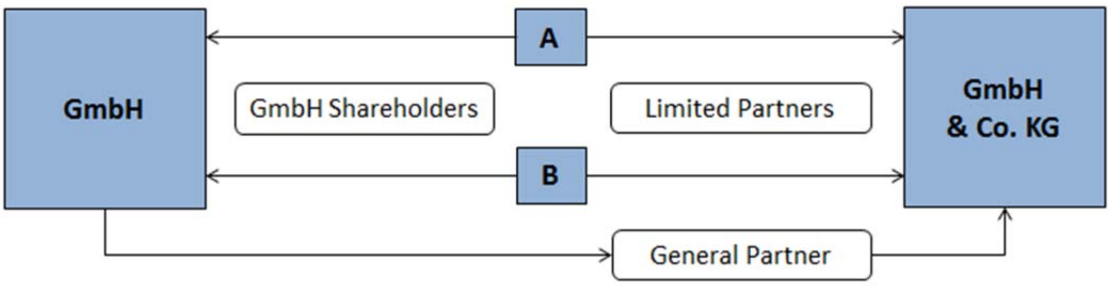
4.2.1.3. Limited partnership with a corporation as general partner (GmbH & Co. KG)

A limited partnership where the general partner is a corporation (usually a GmbH, less frequent an AG) is commonly referred to as a GmbH (or AG) & Co. KG. As a result, the in principal unlimited liability of the general partner is limited to the share capital of the GmbH (AG). In other words, no partner is liable with its personal assets for the partnership's debts.[52] In case the Norwegian company intend to enter the Germany market in form of a business partnership, the GmbH & Co. KG constitutes in many cases the best possibility. In particular, it has to be noted that a GmbH & Co. KG does not require a second individual person. Due to the fact that the Norwegian company can be the only shareholder in the GmbH and the only limited partner in the limited partnership, an establishment of a GmbH & Co. KG is possible without the involvement of a second business partner. Furthermore the GmbH & Co. KG combines the limited liability of a corporation and the characteristics of a business partnership.

[51] Becker, 2006, pp. 23–24.
[52] Katla, 2006, pp. 32–33.

The GmbH itself is usually not involved in separate activities and simply takes the risk of liability.[53] The following figure illustrates the characteristics of a typical GmbH & Co. KG. In the graph, A and B are shareholders of the GmbH and in control over its operations. In turn, the GmbH is the only general, and thus unlimited, partner of the GmbH & Co. KG. In addition, A and B are limited partners of the GmbH & Co. KG.

Figure 5: Typical GmbH & Co. KG



Source: Wöhe/ Döring, 2010, p. 245.

4.2.2. Corporation

A corporation is a separate legal entity with own rights and obligations that are distinct from those of its shareholders. The number of shareholders can vary from only one person to a great number of persons. A corporation is unlimited liable for the company's debts, while the shareholders liability is limited to their invested share. Since shares cannot be returned but only disposed to a third person, a corporation can operate widely independent from its shareholders. In order to enable the corporation to act, the shareholders assign individual persons to act on behalf of the legal entity. The influence of an individual shareholder on the corporation is usually dependent on the amount of its share capital. Most corporations in Germany are public limited companies ("Aktiengesellschaft", AG) or private limited companies ("Gesellschaft mit beschränkter Haftung", GmbH). Both types of entities are briefly presented in following paragraph.[54]

4.2.2.1. Public limited company (AG)

A public limited company ("Aktiengesellschaft", AG) was designed as an entity suitable to be owned by a large number of shareholders. As all corporations, an AG is an own legal person

[53] Wöhe/ Döring, 2010, p. 245.
[54] Wöhe/ Döring, 2010, pp. 229–230.

and its capital stock is divided into shares. These shares can be acquired and disposed in form of publicly tradable stocks. A broad distribution of shares enables the AG to raise a great amount of equity. The minimal share capital is € 50,000, of which at least one quarter has to be deposited on the founding date. The share capital is the product of the nominal value of at least € 1 and the number of shares.[55]

Managerial and supervisory powers of the corporation are distributed in three organs: Management board, supervisory board and shareholders' meeting. The management board is appointed by the supervisory board and consists usually of several persons. The so-called directors of the management board manage and represent the corporation on their own responsibility, but have a reporting duty to the supervisory board. The main purpose of the supervisory board is to control and appoint the management board. In turn, the supervisory board is appointed by the shareholders' meeting. As the name implies, the shareholders' meeting is a gathering of the shareholders with the purpose to form and establish the will of their majority. Among others, the most important rights of the shareholders' meeting are: Appointing the supervisory board, deciding on the use of the profits, changing the articles of association and the liquidation of the corporation. Every shareholder has one vote per share. The AG is subject to disclosure requirements and, depending on size, also auditing duties.[56] Traditionally, the legal form of an AG is chosen by large corporation which are usually listed on the stock exchanges. The effort of establishing an AG is relatively high and its organisational structure is rather complex.[57] Therefore, the choice of an AG as a legal form for a subsidiary is most reasonable for a big Norwegian company with an intention to raise an extensive amount of capital through public offering.

4.2.2.2. Private limited company (GmbH)

A private limited company ("Gesellschaft mit beschränkter Haftung", GmbH) is addressing the needs of smaller and middle-sized businesses, whose equity investors want to limit their liability to their invested share. As already mentioned, the GmbH is a corporation and thus an own legal person. As a consequence, private and company assets are separated. Since the

[55] Gehrmann, 2012b, http://www3.nwb-datenbank.de/nwb9/main.aspx?sid=cl5cru0i&kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f256%2f000256231_0001_index.xml&shigh=aktiengesellschaft&aktion=DokumentAnzeigen.

[56] Wöhe/ Döring, 2010, pp. 230–233.

[57] Gehrmann, 2012b, http://www4.nwb-datenbank.de/nwb9/main.aspx?sid=1et02xjz&kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f256%2f000256231_0001_index.xml&shigh=aktiengesellschaft&aktion=DokumentAnzeigen.

obligations of the company are limited to the company's assets, a personal liability of the shareholder is not possible. The GmbH can be founded by one or more persons that have to provide a share capital of at least € 25,000. [58]

The GmbH consist generally of two organs: The managing director(s) and the shareholders' meeting. Under some conditions, a GmbH can also be required to have a supervisory board. The management of the GmbH is executed by one or more managing directors on their own responsibility. The managing directors are subject to the instruction of the shareholders and have to follow possible limitations of the articles of association. The management must be carried out with care and due diligence of a prudent businessman. In case of a breach of their duties, the managing directors can be made liable for damages.[59] The shareholders' meeting has generally a supervisory right over the activities of the managing board. Furthermore it is taking decision on the financial statement, the profit distribution as well as the appointment and dismissal of the managing board. The voting rights of the shareholders are inextricably linked to their share in the business and cannot be transferred. The profits are generally distributed according to these shares. In regard to disclosure requirements and auditing duties, the same rights as for the AG apply.[60] The required share capital of a GmbH is only half the amount as for the AG and the organisational structure is considerable simpler. In this way, the legal form of a GmbH is also suitable for smaller and middle-sized businesses and especially attractive for Norwegian companies with the desire to hold the Germany subsidiary entirely in group ownership or select the investors themselves.

[58] Wöhe/ Döring, 2010, p. 236.

[59] Gehrmann, 2012c, http://www3.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f126%2f000126825_0001_index.xml&aktion=DokumentAnzeigen.

[60] Becker, 2006, p. 26.

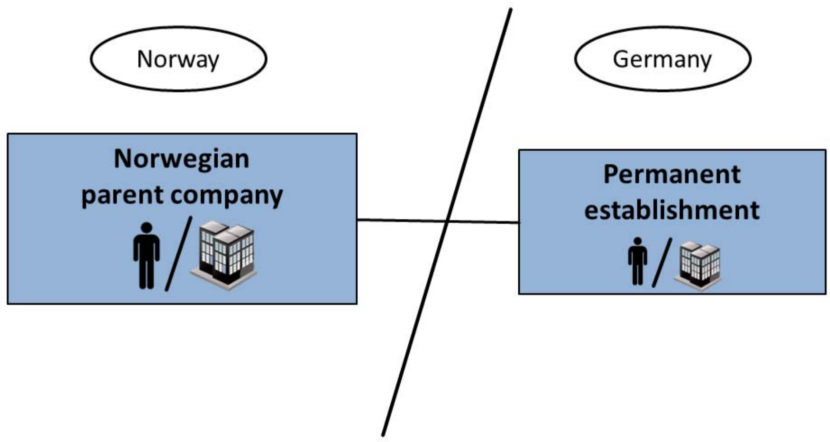
5. Examination of investment alternatives from a tax perspective

5.1. Permanent establishment

The first investment alternative that is examined in regard to significant tax aspects is the permanent establishment. As we already know, a permanent establishment is any fixed place of business or facility that serves the operations of the company (§ 12 S. 1 AO). It must be noted that a permanent establishment is not a German company but rather a concept of tax law that gives rise to taxation and facilitates the allocation of taxation rights.[61]

The following graphic is illustrating the relationship between a permanent establishment and its parent company. In the graph, the oblique stroke is symbolising the border between Norway and Germany. In Norway, the parent company can operate as an individual person (symbolised by the person icon) or as a corporation (symbolised by the corporation icon). The physical presence of the Norwegian company in Germany is the permanent establishment. Since the permanent establishment is an integrated part of the Norwegian company, it is respectively operating as an individual person or a corporation:

Figure 6: Relationship between Norwegian parent company and permanent establishment



Source: Own illustration.

[61] Wedelstädt, 2012, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f114%2f000114004_0001_index.xml&aktion=DokumentAnzeigen.

5.1.1. Current taxation

5.1.1.1. Tax liability in Germany

A permanent establishment of a Norwegian company in Germany has a limited tax liability for its German source income. Since a permanent establishment is in most cases generating income from trade and business, the regulation of § 49 (1) Nr. 2a EStG constitutes the legal base for the taxation. Whether the income is subject to personal income or corporate tax depends on the legal form of the Norwegian company. In case the Norwegian company is an individual person, the permanent establishment is subject to limited personal income tax. If the permanent establishment is part of a Norwegian corporation, the income is respectively limited liable for corporate tax (§ 2 KStG).

In addition to the general requirements of a fixed place of business or facility that serves the business of an enterprise, a permanent establishment must be under the control of the Norwegian company for a not only temporary period of time.[62] In order to clarify the concept, § 12 S. 2 AO provides various examples of what in particular, but not only shall be considered as a permanent establishment. The list includes among others the place of business management, branches, offices, factories and workshops.

In this context, it has particularly to be emphasized that the permanent establishment is not a separate legal entity but rather an integrated part of the Norwegian company. As a result, the achieved income is part of the overall income of the Norwegian company. However, the German income as a result of the German activities of the Norwegian company is allocated to the permanent establishment and constitutes the base for German tax collection.[63] In consideration of all the circumstances, we can assume that a Norwegian company that is active in Germany through a permanent establishment is generally limited liable for taxation in Germany.

5.1.1.2. Allocation of the tax jurisdictions by the DTA

Since there is a limited tax liability in Germany, the next step is to examine whether Germany is also entitled to exercise its right of taxation. A Norwegian company will regularly earn business profits from its activities in Germany. Article 7 of the DTA between Germany and Norway is allocating the right of taxation of business profits as follows: ‘The profits of an

[62] Wilke/ Weber, 2012, pp. 127–129.
[63] Schreiber, 2008, pp. 387–388.

enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein.' Hence, business profits are subject to taxation in the country where the enterprise pursues the economic activity if the activity is exercised through a permanent establishment within the meaning of the DTA. The definitions of a permanent establishment of the DTA GerNo (Art. 5) and the German national law (§ 12 AO) are not completely identical but very similar. The regulations of the DTA define a permanent establishment generally more narrowly than § 12 AO. Unlike German national law, the DTA GerNo includes a catalogue of circumstances that are not covered by the concept of a permanent establishment (Art. 5 (4) DTA GerNo). Through the broader definition of § 12 AO, the German tax authorities make sure that the taxation right that is allocated by the DTA is also covered by national law. As mentioned earlier, a DTA cannot constitute a right of taxation but only limit it. In case the national definition would be narrower than the definition of the DTA, Germany could only tax within the scope of its own national legislation.[64] However, since the definition of a permanent establishment of the DTA is very similar to the national definition, the right of taxation is normally allocated to Germany. As a result, Germany is entitled to exercise its national right of taxation. According to Article 23 (1) of the DTA GerNo, Norway has to exempt the German income from taxation.

5.1.1.3. Tax burden in Germany

As already explained, business profits that can be attributed to the activities of a German permanent establishment are subject to taxation in Germany (Art. 7 DTA GerNo). While Section 1 of Article 7 of the DTA between Germany and Norway is determining the taxation right, Sections 2 to 6 contain the principles of profit allocation between parent company and permanent establishment.[65] According to the so called direct method in Article 7 (2) DTA GerNo, profits are attributed to the permanent establishment 'which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment'. This is resulting in a so-called 'fictive independence' ("wirtschaftliche Selbständigkeitsfiktion") of the permanent establishment,

[64] Brähler, 2012, pp. 150–151.
[65] Ibid., p. 151.

which constitutes the base for the principle of dealing-at-arm's-length ("Fremdvergleich").[66] Independent companies would not allow any other company a benefit at their own expense without a reason. A parent company and its permanent establishment are pursuing, on the other hand, the same interest of maximizing after-tax profits of the whole company. Through the economic exchange of goods and services, profits might be moved between the two parties in a for independent companies unnatural way. The dealing-at-arm's-length principle is addressing this problem by determining the adequacy of performance and consideration.[67] Article 7 (3) DTA GerNo is supplementing the dealing-at-arm's length principle with regard to the expenditures: 'Expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses', are allowable and have to be deducted. In this regard, it does not matter in which country the expenses incurred.[68]

Also German national law regulates transaction between affiliated parties according to the dealing-at-arm's length principle. The corresponding legislation of § 1 (1) AStG is, however, currently only applicable to affiliated companies and not to the income determination of a permanent establishment. Though a proposed revision of § 1 AStG as part of the 'Tax Amendment Act 2013' ("Jahressteuergesetz") is likely to extend the application of the arm's length principle to cross-border transactions with a permanent establishment.[69]

Despite of the just explained direct method, Article 7 (4) DTA GerNo allows, under certain circumstances, another approach of profit allocation. The so-called indirect method is allocating the profits according to a distribution key. Because of the difficulties to determine an accurate distribution key, the direct method is given preference.[70]

Besides the taxable base, the amount of the tax depends significantly on the tax rate and thus on whether the Norwegian company is an individual person or a corporation. The business profit of a Norwegian company in form of an individual person is subject to personal income tax, while corporations are liable to corporate tax. Within the individual income tax, there might be the possibility to apply for a preferential tax treatment for

[66] Kroppen/ Lieber, 2011, recital 92.
[67] Brähler, 2012, p. 155.
[68] Wilke/ Weber, 2012, p. 144.
[69] Wagner, 2012, p. 637.
[70] Kroppen/ Lieber, 2011, recital 133–134.

retained profits according to § 34a EStG. The use of this taxation system has furthermore an influence on the tax burden.

In addition to the individual income and corporate tax, both types of companies are subject to municipal trade tax. However, individual persons are allowed to deduct this additional tax (partly) from their total tax burden (§ 35 EStG).

Since a permanent establishment is a dependent part of the Norwegian company, the taxation in Germany is not affected by whether the income is transferred to Norway or retained in Germany.

5.1.1.4. Tax burden in Norway

The DTA GerNo is allocating the taxation right to Germany. As a result, the business profit of the permanent establishment is only in Germany subject to taxation, while Norway has to exempt the income from taxation. However, according to Article 23 (1) d DTA GerNo, Norway has the right to take the German income into account when determining the progressive tax rate in Norway. That means, even though the German income is not included in the taxable base of the Norwegian taxation (and thus not subject to taxation), it might have an effect on the Norwegian tax rate. This principle is called 'progression clause' ("Progressionsvorbehalt") and while allowed by the DTA GerNo, it is not applied by the Norwegian tax authorities. Yet, according to an interview with Kjetil Bakketun from 'Skatt vest' (Norwegian tax authorities for western Norway), the Norwegian tax authorities consider to apply the progression clause in the near future.[71] Therefore, the provided information should be handled in consideration of the latest developments in the Norwegian tax legislation. Since a permanent establishment is a dependent part of the Norwegian company, the business profits can be transferred to Norway without further taxation.

Even though a German business profit is not subject to taxation in Norway, it might be liable to taxation when transferred from company to shareholder level in Norway. In case the Norwegian company is a corporation, a profit distribution to its shareholders in form of an individual person causes further taxation. In this respect, the Norwegian tax legislation provides a tax allowances of 2 % of the invested capital for profits distributed to an individual persons (§ 10 – 12 Skatteloven). The remaining profit is subject to taxation with a

[71] Bakketun, personal interview of September 26, 2012.

maximal tax rate of 28 %.[72] In case the Norwegian company is already driven by an individual person, no distribution of profits is necessary and therefore no Norwegian taxation applies.

5.1.1.5. Example calculation

The following example illustrates simplified the calculation of the tax burden for a permanent establishment in Germany and Norway. As explained in the paragraphs above, it is necessary to differentiate between the parent company in form of an individual person and a corporation. Within the category of an individual person, we distinguish whether the preferential tax treatment for retained profits is used or not:

Table 1: Calculation of the tax burden of a permanent establishment

	Partner Individual person (a) (without § 34a EStG)	Partner Individual person (b) (with § 34a EStG)	Partner Corporation (c)
Pre-tax profit	€ 100	€ 100	€ 100
(1) Personal income tax (2) Corporate income tax (3) Solidarity surcharge (4) Municipal trade tax (5) Municipal trade tax allowance	€ - 45 - € - 2.475 € - 14 € + 13.3	€ - 34.456 - € - 1.895 € - 14 € + 13.3	- € - 15 € - 0.825 € - 14 -
After tax profit (Ger)	€ 51.825	€ 62.949 *(reinvested)*	€ 70.175
(6) Subsequent taxation by distribution (7) Solidarity surcharge (8) Norwegian taxation	- - -	€ - 11.047 € - 0.608 -	- - -
After tax profit (No)	€ 51.825	€ 51.294 *(distributed)*	€ 70.175 *(company level)*
(9) Norwegian taxation			€ - 14.049
After tax profit (No)			€ 56.126 *(shareholder level)*

[72] Bakketun, personal interview of September 26, 2012 with reference to Stortingsvedtak 25.11.2010 Nr. 1529 om skatt av inntekt of formue mv. for inntektsåret 2011, Kapittel 3.

Calculations:

(1) a) € 100 x 45 % = € 45 b) € 62.949 x 28.25 % + (€ 100 - € 62.949) x 45 % = € 34.456
(2) € 100 x 15 % = € 15
(3) a) € 45 x 5.5 % = € 2.475 b) € 34.456 x 5.5 % = € 1.895 c) € 15 x 5,5 % = € 0.825
(4) € 100 x 14 % = € 14
(5) € 100 x 3.5 % x 3.8 = € 13.3
(6) (€ 62.949 - € 62.949 x 28.25 % x 1.055) x 25 % = € 11.047
(7) € 11.047 x 5.5 % = € 0.608
(8) No taxation, no usage of progressive clause
(9) Norwegian tax burden of the distribution of dividends from a Norwegian corporation to an individual person in Norway:

After-tax profit at company level (Ger)	€ 70.175
Allowance 2 % of invested capital	€ - 20 *(€ 1,000 x 2 %)*
Taxable base	€ 50.175
Norwegian taxation 28 %	€ 14.049 *(€ 50.175 x 28 %)*

Source: Own tables and calculations.

When examining the tables above, we can see the distinction between an individual person and a corporation. Respectively, the profit of € 100 is subject to personal income tax (1) or corporate tax (2). Within the personal income tax, we distinguish between the individual tax rate of a normal income taxation and the preferential tax treatment for retained profits according to § 34a EStG. In case of the latter, a reduced tax rate of 28.25 % is applied on the reinvested profits. However, it must be noted that the tax is considered as distributed and hence itself subject to the usual tax rate of 45 %. In order to determine the maximal amount that can be reinvested and thus taxed by the reduced tax rate, a single variable equation has to be solved. This is because, the result of the after tax profit is needed to calculate the very same. The calculation can be found in Appendix B and is not further discussed. Based on the amounts of these taxes, the solidarity surcharge (3) is levied. In addition, the municipal trade tax (4) has to be subtracted from the profit. In this regard, it has to be emphasized that we assume the same taxable base for the municipal trade tax and use a rounded average of 14 %. Individual persons are allowed to deduct this additional tax load from their tax burden (5). In case the reinvested profit that has been taxed under the regulations of § 34a EStG is distributed in a later year, a subsequent taxation of 25 % is levied (6). In this process, the previously paid preferential tax is deducted from the taxable base. In a next step, the solidarity surcharge is adjusted (7). In this regard, it has to be noted that the comparability of these profits is limited since a distribution and thus a part of the taxation takes place at a later date. This results in an interest and liquidation advantage which is not considered in the calculation. According to the DTA GerNo, Norway has to exempt taxation (8). However, in case the Norwegian company is a corporation and distributes the profit to its shareholders in form of individual persons, a tax of 28 % is levied on the income (9). Two percentage of the invested income is tax allowable (9). For the example calculation we assume an invested capital of € 1,000. When comparing the after tax profit of the two different types of parent companies, we have to consider the difference between company and shareholder level. While the remaining profit is much higher for a corporation after German taxation, the differences are levelled out after the Norwegian taxation of the distributed profit to an individual person.

5.1.2. Use of losses

5.1.2.1. In Germany

As earlier stated, a permanent establishment of a Norwegian company is subject to taxation with its German source income. Businesses with such a limited tax liability have, like unlimited taxpayers, the possibility to offset losses against profits in Germany.[73] This possibility exists for businesses that are limited liable for personal income tax as well as corporate tax. The deduction of losses between periods, in addition to the mandatory balancing of losses within a period (§ 2 (3) EStG), contributes to the net principle and avoids an excessive tax burden.[74] If the Norwegian company has several permanent establishments or other income in Germany, losses and profits can generally be offset with each other between the units. This approach follows the general principle of calculating the total income according to § 2 (3) EStG. German legislation provides different regulations for the different types of taxes. Whether the regulations for personal income or corporate tax apply, depends on the legal form of the Norwegian parent company.

<u>Personal income tax</u>

Positive and negative income that has been generated by different sources within a period has to be balanced with each other. In a first step, profits and losses are balanced within an

[73] Brandt, 2012, recital 31.
[74] Schreiber, 2008, pp. 53–54.

income category. Thereafter, the remaining positive and negative income is balanced between the categories.[75]

As far as losses cannot be compensated within a period by reason of a lack of positive income in a sufficient amount, the remaining losses are deductible in another tax year under the rules of § 10d EStG. Losses can be carried forward and backward in order to achieve a tax reduction.[76] The regulation of a loss carried backwards state that negative income is deductible from the total income of the immediately preceding taxable period up to an amount of € 511,500 (§ 10d (1) EStG). According to § 10d (1) S. 5 EStG, the taxpayer has the possibility to renounce the loss carry back on request. Losses not compensated by the carry back have to be carried forward to the following tax assessment period and are deducted from the total income. The amount carried forward without restriction is, however, limited to € 1 million. An amount exceeding the limitation is only deductible to an amount that ensures that at least 40 % of the profit exceeding € 1 million remains taxable. In other words, a loss that exceeds 60 % of the profit exceeding € 1 million is not deductible. In this way, a ‘minimum taxation’ (“Mindestbesteuerung”) is ensured. In contrast to the carry back, the loss carry forward is mandatory (§ 10d (2) EStG). Losses not fully compensated because of a lack of positive income are carried forward to the following taxable periods. This process is repeated under the regulations of § 10d EStG until all losses are offset.[77]

Special rules apply, among others, for losses generated in the income category of capital investment (§ 20 EStG). Losses which occur in this income group cannot be balanced with positive income that originates from other income groups within a period. It is not possible to either carry the losses backwards or forwards according to § 10d EStG (§ 20 (6) S. 2 EStG). Instead, § 20 (6) S. 3 EStG opens up the possibility to carry forward losses from capital investment separately.[78] However, this issue is generally not crucial for foreign entities with only a permanent establishment in Germany.

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[75] Meier, 2012, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f097%2f000097082_0001_index.xml&aktion=DokumentAnzeigen.
[76] Schneeloch, 2011, p. 195.
[77] Schreiber, 2008, p. 55.
[78] Schneeloch, 2011, p. 196.

Corporate income tax:

According to § 8 (1) KStG, the regulations of the EStG to the determination of the total net income apply generally also to corporations. This includes the rules of balancing losses within a period (§ 2 (3) EStG) as well as the loss deduction in other periods (§ 10d EStG).[79] However, § 8c KStG constitutes an exception for corporations: The right of loss deductions can expire proportional if more than 25 % of the shares or voting rights of the Norwegian corporation are transferred to one purchaser or several purchasers which are affiliated with each other (purchaser group) within a period of five years. In case more than 50 % of the shares are acquired, the right to carry a loss forward is completely lost. Several acquisitions by the same purchaser or the same purchaser group within the period are added together. This legal norm is primarily intended to prevent the purchase of an ailing company with the only purpose of reducing one's own tax burden through the company's deductible losses. The regulation of the forfeiture of losses does not apply if the same person is holding the entire share capital of both companies (§ 8c (1) S. 5 KStG). In this way, an internal group restructuring is not hindered.[80]

Municipal trade tax:

Due to a different tax basis and an independent determination process, a municipal trade tax loss is normally not identical with the individual income or corporate tax loss. Since the municipal trade tax is only taxing the business establishment, it does not allow the balancing of losses and profits between different permanent establishments in Germany.

Moreover the regulations of the municipal trade tax do not allow a carry back of losses. Instead, a possible loss has to be carried forward to the following period in accordance with § 10a GewStG. The deduction has to take place as early as possible and the company cannot choose a year of deduction. As with the individual income and corporate tax, the annual deductible amount is limited to € 1 million. A remaining amount exceeding that limit can only be deducted to 60 % (§ 10a S. 1 & 2 GewStG).

In case the company is a corporation, the regulations of § 8c KStG (loss of losses in case of a transfer of shares or voting rights) apply also in regard to the municipal trade tax

[79] Beeck, 2012, p. 50.
[80] Engelberth, 2012, pp. 1688–1685.

(§ 10a S. 10 GewStG). In this way, the purchase and sale of tax losses is also prevented for this type of tax.[81]

In case the permanent establishment is sold itself, the loss cannot be deducted anymore, no matter the Norwegian company is organised as corporation or is just an individual person (R 10a.3 GewStR).

5.1.2.2. In Norway

Double taxation agreements refer in principal only to positive income. In order to clarify in which country losses are deductible, the German and Norwegian tax authorities apply the so called 'symmetry thesis' ("Symmetriethese"). This commonly used principle implies that the allocation of taxation rights by the DTA comprises not only profits but also losses. Thus, if profits of a permanent establishment are taxable in Germany and at the same time tax exempt in Norway, the losses of the permanent establishment can only be used in Germany. In other words, losses that are generated by a permanent establishment in Germany cannot reduce the taxable base of the parent company in Norway.[82] In respect to this principle, the Norwegian tax legislation does not include any special regulations that would allow the use of German losses in Norway.[83]

At first glance, the system of symmetry thesis seems to be logical and fair. On a closer inspection, however, considerable issues can be recognized. Since a permanent establishment might not only generate initial but permanent losses, a loss deduction might not be possible at all. This could especially be the case if a permanent establishment is terminated because the foreign business venture failed to achieve a profit. The resulting lack of positive income is hindering a loss deduction and a use of losses in the source country is thus not possible. This situation is especially questionable when compared to the tax regulations without a DTA. A system without a DTA is usually taxing the world wide income and would therefor consider foreign losses in the determination process. As a consequence, a DTA, with the declared purpose to protect the taxpayer, could have a significant negative effect on the company's tax burden.[84]

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[81] Schneeloch, 2011, p. 199.
[82] Schella, 2009, p. 13.
[83] Bakketun, personal interview of September 26, 2012.
[84] Kessler, 2010a, http://blog.handelsblatt.com/steuerboard/2010/09/07/symmetrie-mit-leichter-asymmetrie/.

In some instances, not to provide the possibility to use losses of an affiliated company in another member state of the European Economic Area (EEA) might even violate the treaty of the European Community (EC). Article 43 EC regulates that 'restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be prohibited.' This includes also the establishment of branches and subsidiaries (Article 43 EC). Since Article 48 EC regulates that companies of member states shall in this regard be treated in the same way as natural persons, the regulations apply also to legal persons with the intention of a cross border establishment.

In this context, the European Court of Justice (ECJ) had to address the issue and passed various judgments in recent years. Among experts, the court decision in the case of the British retailer 'Marks and Spencer' (M&S) (Case C-446/03) from 2005 became particular famous. The dispute was mainly about the question whether M&S was allowed to offset the losses of its subsidiaries in other EU member states against its profits in the UK.[85] The ECJ decided on this point that Article 43 EC and 48 EC do not preclude general provisions that prevent a parent company from deducting losses incurred by its subsidiary in another member state. Hence, the ECJ is generally approving the legitimacy of the symmetry thesis. However, the member state has to provide the possibility to offset the losses, if the non-resident subsidiary has exhausted all possibilities of loss deduction in its state of residency. This is the case if there is neither at present nor in the future a sufficient amount of profits available in order to deduct the losses.[86]

The court decision in the M&S case is based on the fact that a general prohibition is restricting the freedom of establishment. However, this restriction can be justified by overriding reasons in public interest. The court refers in this regard to the necessity of interstate allocation of tax powers and the risk of double usage of such losses.[87]

While the case of Marks and Spencer is dealing with losses of subsidiaries, the case of 'Lidl Belgium' (Case C-414/06) is addressing the issue of weather losses of a permanent establishment can be deducted from its parent company's profits.[88] In the court decision from May 15, 2008, the ECJ is taking up the case of Marks and Spencer and underlines again

[85] ECJ, decision of December 13, 2005, C-446/03, Marks & Spencer.
[86] von Brocke/ Auer, 2010, p. 755.
[87] ECJ, decision of December 13, 2005, C-446/03, Marks & Spencer.
[88] ECJ, decision of May 15, 2008, C-414/06, Lidl Belgium.

that losses must be deductible in the resident state of the parent company if there is no possibility to offset the losses against profits in the residence state of the permanent establishment.[89] Yet, a transfer from losses from the source state to the state of residency of the parent company has to be considered as the ultimo ratio.[90]

The transfer of losses between affiliated companies in the EEA is a complex topic and contains still a certain uncertainty. A further discussion of this issue is out of the scope of this thesis and the paragraphs above served primarily the purpose to provide a quick overview of the influence of European legislation on national taxation rules. Since Norway is a member of the EEA, the presented jurisdictions apply also to the Norwegian tax regulations. Thus, even though Norway's tax legislation provides no possibility to deduct losses from a permanent establishment in Germany, a general provision might in some instances not be in accordance to the treaty of the European Community. As a result, a Norwegian company should consider appealing on European law if its permanent establishment in Germany is unable to deduct its losses from profits in Germany. With regard to the presented decisions of the ECJ, a deduction of the German losses from Norwegian profits might be permitted as an ultimo ratio.

5.1.3. Termination of engagement in Germany

In case a Norwegian company would like to quit its engagement in the German market, the permanent establishment can be terminated by alienation or liquidation. These two methods results generally in a capital gain or capital loss. The following paragraph examines the tax effects of the termination process.

5.1.3.1. Tax liability in Germany

<u>Alienation</u>

If the permanent establishment is disposed as a whole unit, the Norwegian company is usually generating a capital gain or loss. In case the permanent establishment is sold for a higher price than its book value, the parent company achieves a capital gain. In a reverse situation, the Norwegian company is respectively making a capital loss. Since the German tax legislation does not provide special rules for capital gains, the profit or loss is in such

[89] Fehling/ Wichert, 2010, p. 1837.

[90] Kessler, 2010b, http://blog.handelsblatt.com/steuerboard/2010/06/22/die-rechtsachen-lidl-belgium-und-kra nkenheim-wannsee-verschiedene-systeme-verschiedene-ergebnisse/.

instances considered as income from trade and business (§ 16 (1) S. 1 EStG). As a consequence, the Norwegian company is limited liable for taxation with its capital gain of disposing a permanent establishment in Germany (§49 (1) Nr 2a EStG). Depending on the legal form of the parent company, either personal income or corporate tax is levied. In case the Norwegian company is an individual person, § 34 (1) EStG provides the possibility of a reduced tax rate.[91]

If the Norwegian company is an individual person, the capital gain is generally not subject to municipal trade tax. Even though there are exemptions to this regulation, the municipal trade tax is charged against the individual income tax and a possible remaining burden is normally insignificant low. In case the Norwegian company operates in form of a corporation, municipal trade tax is levied (§ 7 (1) S.2 GewStG). As a result, the tax burden of a capital gain does not differ considerable from the current taxation.

Liquidation

A permanent establishment is liquidated by disposing its individual assets or by transferring them back to the parent company in Norway. The disposal of individual assets has the same effects as the alienation of the entire permanent establishment and leads to a taxation of the capital gains under the regulations of § 49 (1) Nr. 2a EStG. In case individual assets are transferred abroad and thus out of the tax jurisdiction of Germany, an evaluation under the principle of fair value has to be conducted. A possible difference between the fair value and the book value of the items are called hidden reserves. The disclosure of such hidden reserves is considered as a capital gain and results also in a taxation under § 49 (1) Nr. 2a EStG.[92] If the individual assets would be transferred at book value, already generated but not yet realized profits would be reallocated from the permanent establishment in Germany to the parent company in Norway without taxation. From a fiscal point of view, the taxation of hidden reserves is therefore absolute necessary if a future taxation is not secured. This taxation approach covers not only recognized, tangible assets, but also unrecognized and possible intangible assets as for example patents.[93]

[91] Höhn/ Höring, 2010, p. 92.
[92] Ibid., p. 92.
[93] Schreiber, 2008, pp. 469–470.

If an entire field of activity (e.g. sales, production) is relocated from Germany rather than only individual assessable assets, the regulations of the 'transfer of functions' ("Funktionsverlagerung") apply according to § 1 (3) S. 9 AStG. In such a case, the assessment of the so called 'function' is based on the total value of the entire field of activity. This includes the fair value of the assets as well as future risk and chances (§ 1 (3) S. 10 AStG). In this regard, future profits that are expected to be generated by the function are the crucial base of valuation.[94] This overall assessment of the function facilitates the attempt to disclose hidden reserves and prevents a transfer without taxation. In this way, the German regulations erect transfer barriers in order to avoid the loss of future tax revenues or at least compensate them through immediate taxation.[95]

Presupposition for the application of the regulations for the transfer of functions is an existing 'business relationship' according to § 1 (1) AStG. The German tax authorities assume already the applicability for business partnerships but see a limitation for permanent establishments on the base of Article 7 DTA GerNo. In order to clarify this uncertainty and establish an undisputable applicability, a revision of the regulation is expected in the 'Tax Amendment Act 2013'.[96]

5.1.3.2. Allocation of the tax jurisdictions by the DTA

Both possibilities of terminating the engagement of the Norwegian company in Germany result usually in a capital gain or loss. As just described, a capital gain is either liable to personal income or corporate income tax. In addition to the national tax liability in Germany, Article 13 (2) of the DTA between Germany and Norway is allocating a taxation right for capital gains to German:

> 'Gains from the alienation of movable property forming part of the business property of a permanent establishment which an enterprise of a Contracting State has in the other Contracting State, […], including such gains from the alienation of such a permanent establishment (alone or with the whole enterprise) […], may be taxed in that other State.'

However, the formulation 'may be taxed' allocates Germany a taxation right, without disallowing Norway to claim its right of taxation. In order to clarify Norway's tax jurisdiction, it is necessary to examine the exemption method in the DTA GerNo. In this respect, Article

[94] Wagner, 2012, p. 637.
[95] Schreiber, 2008, pp. 470–471.
[96] Wagner, 2012, p. 637.

23 (1) a) states that 'where a resident of the Kingdom of Norway derives income or owns capital which, […], may be taxed in the Federal Republic of Germany, the Kingdom of Norway shall, […] exempt such income or capital from tax.'

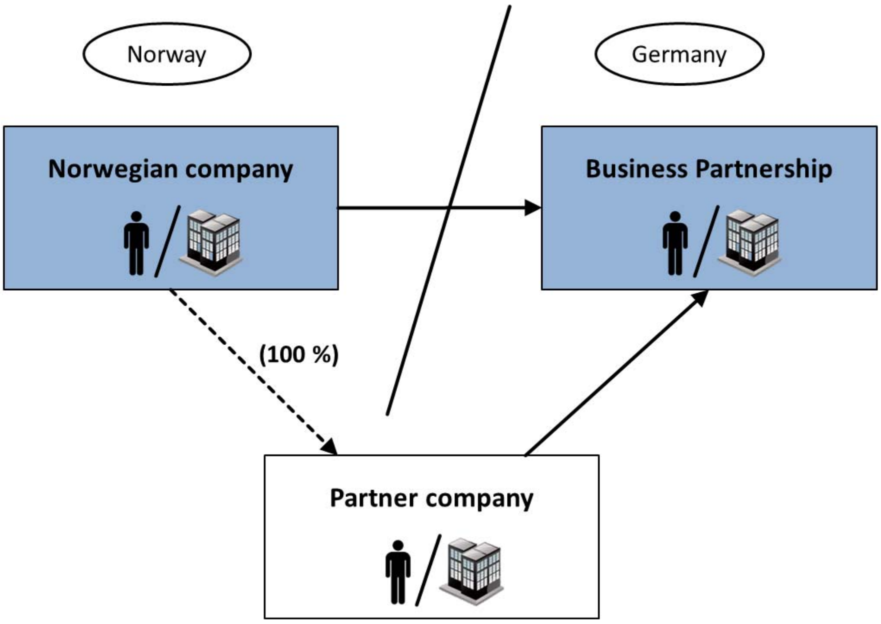
Taking both articles of the DTA GerNo into consideration, we can clearly assume a taxation right for Germany while Norway has to exempt capital gains from taxation. In this regard, it does generally not matter if the capital gain is generated by alienation or liquidation.

5.2. Business partnership

The second investment alternative that is examined in regard to significant tax aspects is the business partnership. As already explained, a business partnership is formed when at least two individual and/or legal persons join together to achieve a common purpose.

Figure 7 is illustrating the structure of a business partnership. The oblique stroke is once more symbolising the border between Germany and Norway and the icons visualise an individual person and a corporation. The German business partnership consists of the Norwegian company and at least one other company. The partners can be individual persons as well as corporations. At least one of the partners has to be unlimited liable for the obligations of the partnership. In the special case of the GmbH & Co. KG, the Norwegian company can establish a business partnership without another independent person or company. Instead of searching for a fitting and willing partner, the Norwegian company is founding an own corporation (in this case a GmbH) in which it is holding 100 % of the shares. In this way, the Norwegian company has the sole control over the business partnership. In addition, it is possible to limit the liability for the partnership debts to the share capital of the corporation.

Figure 7: Relationship between a Norwegian company and a business partnership



Source: Own illustration.

5.2.1. Current taxation

5.2.1.1. Tax liability in Germany

Even though a business partnership has similarities to a legal person and is considered as an own company, it is not a distinct legal entity and has only limited tax autonomy.[97] As a result, the German legislation considers the partners themselves as liable for income taxation instead of the business partnership. In this regard, a partner of a business partnership is normally viewed as a 'co-entrepreneur' ("Mitunternehmer") in the meaning of § 15 (1) S. 1 Nr. 2 EStG, who achieves income from trade and business. Depending on the legal form of the partner, personal income or corporate tax is levied.[98]

Although each partner is liable for income taxation itself, the taxable income is in a first step collectively identified for all partners on a company level. In a next step, the resulting income is allocated to the different partners. Due to this profit allocation, the income of a business partnership is rather taxed at shareholder than at company level.[99] This system of taxation is

[97] Katla, 2006, p. 9.
[98] Gehrmann, 2012d, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f266%2f000266232_0001_index.xml&aktion=DokumentAnzeigen.
[99] Ibid.

commonly known as the 'transparency principle' ("Transparenzprinzip") and is done regardless of whether the income is reinvested or distributed to the shareholder.[100]

In case a partner is non-resident in Germany, § 49 (1) Nr. 2a EStG constitutes the legal base for a taxation in Germany. According to this regulation, income from trade and business is limited liable for taxation in Germany if it was generated through a permanent establishment. Since the income of a business partnership is generally considered as income from trade and business, a tax liability depends on whether the partnership maintains a permanent establishment in Germany. Due to the characteristics of an investment via a business partnership, a permanent establishment can generally be assumed.[101]

Based on these circumstances, the personal income tax treatment of an investment in form of a business partnership corresponds generally to the treatment of a permanent establishment. As earlier explained, a permanent establishment is a dependent part of its parent company. Therefore, the permanent establishment is not itself liable for taxation. Instead, the parent company is subject to taxation with the income of the permanent establishment. The same applies for a business partnership, which is taxed on a shareholder level.[102] As a result, it is in many respects irrelevant for the Norwegian company whether it is maintaining a permanent establishment or participating in a business partnership.

Nevertheless, in some instances, the business partnership itself is liable for taxation. Especially the value added and the municipal trade tax lead to a direct taxation at company level. According to § 5 (1) S. 3 GewStG, the business partnership is itself subject to municipal trade tax.[103]

5.2.1.2. Allocation of the tax jurisdictions by the DTA

Business partnerships in Norway are, similar to the German system, taxed under the principle of transparency.[104] Due to the lack of a tax liability in both countries, the partnership is not considered as 'resident of a Contracting State' within the meaning of Article 4 (1) S. 1 DTA GerNo. As a result, the DTA between Germany and Norway does not apply for business partnerships. However, partners of a business partnership that are

[100] Schneeloch, 2011, p. 316.
[101] Höhn/ Höring, 2010, p. 94.
[102] Brähler, 2012, p. 305.
[103] Schneeloch, 2011, p. 170.
[104] Mörsdorf, 2011, p. 135.

considered as residents in Germany or Norway are covered by the DTA GerNo.[105] These partners achieve income through their involvement in the partnership. Such income is generally considered as business profits according to Article 7 DTA GerNo. As previously explained, the allocation of taxation rights depends in such a case on whether the business operation of the partners is considered as a permanent establishment within the meaning of Article 5 DTA GerNo. From a fiscal point of view, the share of the Norwegian partner in the German business partnership is regarded as a permanent establishment, while the partner himself is considered as the parent company. In other words, each individual partner is operating an independent company with a permanent establishment at the place of management of the Germany business partnership. As a result, Germany has the taxation right whereas Norway has to exempt such income from tax.[106]

5.2.1.3. Tax burden in Germany

As we already know, the income of a business partnership is subject to taxation at a shareholder level. Since a business partnership consists of at least two companies, the income has to be allocated to the different partners. The profit allocation follows usually the previously determined rules of the partnership agreement. If the partnership agreement does not provide any specifications, the allocation follows the regulations of §§ 121 or 168 HGB.[107] After the income is allocated, the partners are liable for taxation with their individual profit share. Depending on the legal form of the partner, either personal income or corporate tax is levied. In addition, the income is subject to municipal trade tax on company level. The tax burden of the individual partners is generally identical to the tax burden of a permanent establishment.

While the final tax burden of a business partnership and a permanent establishment is generally equal, there are some major differences regarding the income attribution. Unlike a permanent establishment, a business partnership is a separate company and legally bound to produce an annual financial statement.[108] Therefore, a separate attribution of income from German operations is not necessary. However, it should be noted that prices for goods and services between the Norwegian parent company and the German business partnership

[105] Brähler, 2012, pp. 136–137.
[106] Ibid.
[107] Becker, 2006, p. 23.
[108] Wöhe/ Döring, 2010, p. 227.

cannot be set arbitrary. In order to address the previously explained problem of profit shifting between affiliated businesses, German legislation has strict restrictions on internal pricing. According to § 1 AStG, internal pricing has to follow the dealing-at-arm's-length principle as explained in chapter 5.1.1.3. Since the German tax authorities examine these transfers very carefully, a profit shift to Norway is hardly possible.

5.2.1.4. Tax burden in Norway

As already explained, due to the transparency principle, the share of a Norwegian partner in a German business partnership is, in regard to taxes, considered as a permanent establishment. Thus, Germany has the taxation right on the business profits while Norway has to exempt taxation (see 5.1.1.2). As with a permanent establishment, there is no further taxation of the German profits when transferred back to Norway. However, as mentioned in paragraph 5.1.1.4, Norway has the right to apply the progressive clause, although it is not exercised at the moment.[109]

Even though a German business profit is not subject to taxation in Norway, it might be liable to taxation when transferred from company level of the Norwegian partner company to the shareholder level. In case the partner of the German business partnership is a corporation, a profit distribution to its Norwegian shareholders in form of an individual person causes further taxation in Norway.[110] More detailed information about the assessment base and tax rate has already been given in paragraph 5.1.1.4 and can be seen in the following calculation.

5.2.1.5. Example calculation

Table 2 illustrates the calculation of the tax burden of a business partnership. For reasons of simplification and comparability, we assume that a single partner is holding 100 % of the shares of the business partnership. As explained earlier, the tax burden of a business partnership will be identical with the tax burden of a permanent establishment. Also in the case of a business partnership, we have to distinguish between partners in form of an individual person and a corporation as well as whether the preferential tax treatment for retained profits is applied or not.

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[109] Bakketun, personal interview of September 26, 2012.

[110] Ibid.

Table 2: Calculation of the tax burden of a business partnership

	Partner Individual person (a) (without § 34a EStG)	Partner Individual person (b) (with § 34a EStG)	Partner Corporation (c)
Pre-tax profit	€ 100	€ 100	€ 100
(1) Municipal trade tax	€ - 14	€ - 14	€ - 14
(2) Personal income tax (3) Corporate tax (4) Solidarity surcharge (5) Municipal trade tax allowance	€ - 45 - € - 2.475 € + 13.3	€ - 34.456 - € - 1.895 € + 13.3	- € - 15 € - 0.825 -
After tax profit (Ger)	€ 51.825	€ 62.949 *(reinvested)*	€ 70.175
(6) Subsequent taxation by distribution (7) Solidarity surcharge (8) Norwegian taxation	- - -	€ - 11.047 € - 0.608 -	- - -
After tax profit (No)	€ 51.825	€ 51.294 *(distributed)*	€ 70.175 *(company level)*
(9) Norwegian taxation			€ - 14.049
After tax profit (No)			€ 56.126 *(shareholder level)*

Calculations:

(1) € 100 x 14 % = € 14
(2) a) € 100 x 45 % = € 45 b) € 62.949 x 28.25 % + (€ 100 - € 62.949) x 45 % = € 34.456
(3) € 100 x 15 % = € 15
(4) a) € 45 x 5.5 % = € 2.475 b) € 34.456 x 5.5 % = € 1.895 c) € 15 x 5,5 % = € 0.825
(5) € 100 x 3.5 % x 3.8 = € 13.3
(6) (€ 62.949 - € 62.949 x 28.25 % x 1.055) x 25 % = € 11.047
(7) € 11.047 x 5.5 % = € 0.608
(8) No taxation, no usage of progressive clause
(9) Norwegian tax burden of the distribution of dividends from a Norwegian corporation to an individual person in Norway:

After-tax profit at company level (Ger)	€ 70.175
Allowance 2 % of invested capital	€ - 20 *(€ 1,000 x 2 %)*
Taxable base	€ 50.175
Norwegian taxation 28 %	€ 14.049 *(€ 50.175 x 28 %)*

Source: Own tables and calculations.

When examining the tables above, we can see that most parts of the calculations are identical to the calculations of a permanent establishment and result in the same tax burden. However, in case of a business partnership the approach is different. In a first step, the municipal trade tax is paid directly by the company (1). In a second step, the partners are liable for their income tax. Apart from that, the calculations are identical to a permanent establishment and we distinguish again between individual persons and corporations. Respectively, the profit of € 100 is subject to personal income tax (2) or corporate tax (3). If the individual person is applying the regulations of § 34a EStG, a preferential tax rate is applied on the retained profits (2). In this regard, it must be noted that the tax is considered as distributed and is itself subject to the usual tax rate of 45 %. As earlier mentioned, in order to calculate the maximal amount that can be reinvested, a single variable equation has to be solved and can be found in Appendix B. Based on the amounts of these taxes, the solidarity surcharge (4) is levied. Even though the municipal trade tax is levied on a company level, individual partners are allowed to deduct their proportionate share of the tax from their individual income (5). Previously reinvested profit that is distributed at a later date is subject to subsequent taxation of 25 % (6). In this process, the previously paid preferential tax is deducted from the taxable base. In a next step, the solidarity surcharge is adjusted (7). As already mentioned in paragraph 5.1.1.5, a possible interest and liquidity advantage is limiting the comparability of the results. According to the DTA GerNo, Norway has to exempt taxation for income generated in a permanent establishment in Germany (8). However, if the Norwegian company is a corporation and distributes the profit to its shareholders that are individual persons, a tax of 28 % is levied on the income (9). Two percentage of the invested income is tax allowable (9). For the example calculation we assume an invested capital of € 1,000. When comparing the outcomes (after tax profit) of the two different types of partners, we have to consider the difference between company and shareholder level. While the remaining profit is much higher for a corporation after German taxation, the differences are levelled out after the Norwegian taxation of the distributed profit to an individual person.

5.2.2. Use of losses

5.2.2.1. In Germany

Personal income tax & corporate tax

Losses of a business partnership are directly allocated to the different partners as part of the income distribution. In such a case, the partners of a business partnership obtain negative income from their participation. The allocated loss is accumulated with other income from trade and business within the meaning of § 15 (1) S. 1 Nr. 2 EStG. Any remaining loss can be balanced with other types of income within a period (§ 2 (3) EStG). If there is still a loss that could not yet be offset, § 10d EStG provides the possibility to deduct losses from profits in other periods.[111] In this regard, different rules apply for partners that are individual persons or corporations. A detailed explanation to the use of losses has previously been given in paragraph 5.1.2.

Special rules apply for a business partnership with limited liable partners. The previously described KG and the, in Germany very popular, GmbH & Co. KG are typical examples. The limited liable partners can only balance losses with other German income at an amount up to their liable investment in the partnership (§ 15a (1) EStG). Remaining losses are not transferable to other partners (e.g. an unlimited liable partner), but can be carried forward in order to balance them with future profits from the same investment (§ 15a (2) EStG).[112]

Municipal trade tax

A municipal trade tax loss has to be determined independently and reduces the taxable base of the municipal trade tax in the following year(s). In case of a business partnership, the loss remains on the company level and is not usable for the partners to charge against other income that is subject to the municipal trade tax. Yet, the loss has to be allocated to the different partners according to the partnership's income distribution key virtually for the following reason: The possibility to deduct the loss from the municipal trade tax assessment base of the subsequent year(s) (§ 10a S. 4 & § 5 GewStG) is connected to the distribution of shares to the partners. A deduction is, however, just possible as far as the ownership structure hasn't changed in comparison to the year of the loss incurrence. In order to be deductible, the loss must have occurred personally to the partner. That means that the right

[111] Schreiber, 2008, p. 220.
[112] Schneeloch, 2011, pp. 323–324.

of loss deduction expires partial in the event of a partner change (e.g. retirement of a partner or sale of a holding).[113] More general information to the regulations regarding the use of municipal trade tax losses can be found under 5.1.2.

5.2.2.2. In Norway

As explained in paragraph 5.1.2.2, the Norwegian tax legislation is following the principle of the symmetry thesis. Since the DTA is allocating the taxation right of business partnerships to Germany, it is generally not possible to use losses in Norway.[114] However, within the EEA there exists an exemption. According to the ECJ decision in the case of M&S, the member state of the parent company has to provide the possibility to offset losses, if the non-resident subsidiary has exhausted all possibilities of loss deduction in its state of residency.[115] Thus, in case the Norwegian partner of the German business partnership has no possibility to offset the losses with German profits, the partner should consider appealing on European law. With regard to former decisions of the ECJ, a deduction of the German losses from Norwegian profits might be possible as an ultimo ration.

5.2.3. Termination of engagement in Germany

5.2.3.1. Tax liability in Germany

In case a partner would like to terminate its engagement in Germany, the holding in the business partnership can be alienated or liquidated. If the whole unit is disposed and the sales price is higher than the book value, the outgoing partner is achieving a capital gain. The same applies for individual assets that are sold in the course of a liquidation of the partner's participation. In this regard, also the disclosure of hidden reserves, when transferred back to Norway constitutes a capital gain. If an entire function is relocated back to Norway, the regulations of the 'transfer of function' apply for a business partnership in the same way as for a permanent establishment. The capital gains that are generated by the various forms of termination are generally considered as income from trade and business (§ 16 (1) S. 1 EStG).[116] Thus, the Norwegian company is limited liable to taxation according to § 49 (1) Nr. 2a EStG and respectively subject to individual income or corporate tax. As we can see, the termination of a business partnership results generally in the same tax

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[113] Schreiber, 2008, p. 221.
[114] Bakketun, personal interview of September 26, 2012.
[115] von Brocke/ Auer, 2010, p. 755.
[116] Schreiber, 2008, p. 243.

consequences as the termination of a permanent establishment. More detailed information can therefore be found in the previous paragraph of 5.1.3.

5.2.3.2. Allocation of the tax jurisdiction by the DTA

Germany and Norway are both following the ‘transparency principle’. As a result and previously explained, the DTA between Norway and Germany does not cover a business partnership. However, the participation in a business partnership is considered as a permanent establishment, while the Norwegian partner is regarded as the parent company.[117] On the base of this legal circumstance, capital gains that are generated by the termination of engagement are handled in the same way as for a permanent establishment. Therefore, the findings of 6.1.3 apply generally also for a business partnership. As a result, Germany has the taxation right for capital gains (Article 13 (2) DTA GerNo), while Norway has to exempt the taxation (Article 23 (1) a) GerNo).

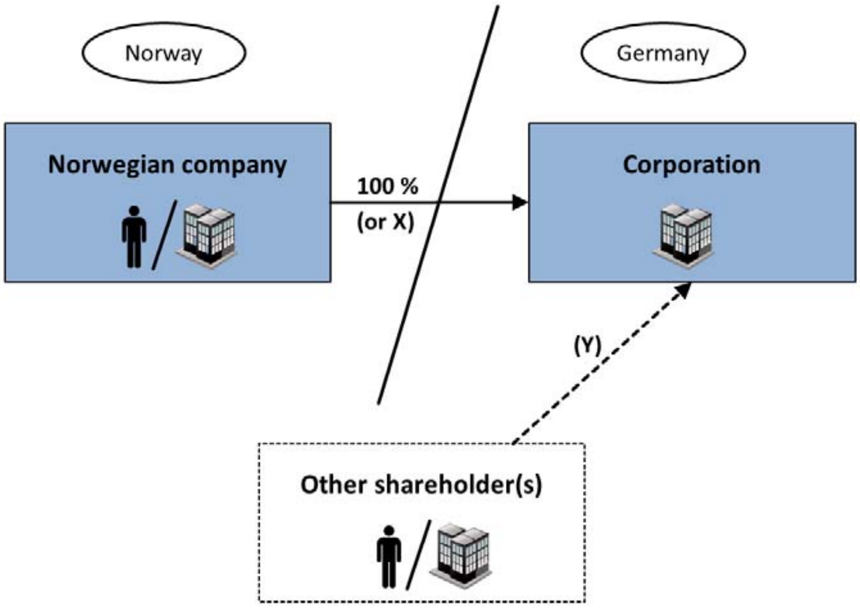
5.3. Corporations

The third and last investment alternative that is examined in regard to significant tax aspects is the corporation. As already presented, a corporation is a separate legal entity with own rights and obligations that are distinct from those of its shareholders. A corporation can consist of one to multiple shareholders.[118]

Figure 8 is illustrating the structure of a corporation and the relationship to its shareholders. The symbolisation equalise the previous illustrations and the respective explanations can be found in paragraph 5.1 and 5.2. In case of a corporation, the Norwegian company can be the sole shareholder or one of many. Since a Norwegian company is usually pursuing specific goals, it is likely to hold the majority of the shares (X) in order to operate independently. Thus, the distribution of the shares can generally be assumed to be $X + Y = 100\ \%$ and $X \geq 51\ \%$. The Norwegian company as well as other shareholders can be themselves corporations or individual persons.

[117] Brähler, 2012, pp. 136–137.
[118] Gehrmann, 2012c, http://www3.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f126%2f000126825_0001_index.xml&aktion=DokumentAnzeigen.

Figure 8: Relationship between Norwegian parent company and an affiliated corporation



Source: Own illustration.

5.3.1. Current taxation

5.3.1.1. Tax liability in Germany

A corporation is a distinct legal entity and therefore itself subject to taxation. The resulting tax separation between the corporation and its shareholders is called ‘separation principle’ (“Trennungsprinzip”) and implies that the income is taxed at company level.[119] In contrast to a business partnership, the profit is not directly allocated to the shareholders in order to levy taxes. As a consequence, the participation of a Norwegian company has initially no influence on the taxation of the German corporation and we have to distinguish between a tax liability on company and shareholder level.

Company level

A corporation with its place of business or management in Germany is according to § 1 (1) KStG unlimited liable for corporate tax in Germany. Since this can generally be expected of a German corporation although it is controlled by a Norwegian company, we can assume an unlimited tax liability. In this regard, the corporate tax extends to all income and

[119] Schreiber, 2008, p. 76.

could be considered as the personal income tax for legal persons (§ 1 (2) KStG).[120] This level of taxation takes places regardless of whether profits are distributed or retained.

In addition to the corporate tax, a corporation is subject to municipal trade tax (§ 2 GewStG).

Shareholder level

The distribution of a corporation's profits to its shareholders results in a second level of taxation. At this next level, the shareholder of the corporation becomes subject to taxation. According to § 1 (4) EStG, a foreign shareholder in form of an individual person and without a residency in Germany becomes limited liable to taxation if it receives income in the meaning of § 49 EStG. The same regulation applies to a shareholder in form of a corporation without its place of management or business in Germany (§ 2 Nr. 1 KStG).

Profit that is distributed from a corporation to its shareholders constitutes income from capital investment according to 20 (1) Nr. 1 S. 1 EStG. Since the catalogue of § 49 EStG includes such income when received from a German corporation, a limited tax liability in German is established for a Norwegian company (§ 49 (1) Nr. 5a EStG). Depending on whether the shareholder is an individual person or a corporation, personal income tax or respectively corporate tax is levied.[121] A profit distribution is only in very special cases subject to municipal trade tax, which is generally not relevant for foreign shareholders.

5.3.1.2. Allocation of the tax jurisdictions by the DTA

As long as the German corporation is itself only active in Germany, the regulations of double tax agreements are not applicable at company level. In contrast to this, the taxation of cross-border profit distribution between corporations and shareholders in Germany or Norway is governed by Article 10 DTA GerNo. The DTA refers to such and similar income as dividends and defines the term in Article 10 (6) DTA GerNo.

The DTA between Germany and Norway is generally allocating the taxation right of dividends from a German corporation to a Norwegian shareholder to Norway: 'Dividends paid by a company which is a resident of a Contracting State to a resident of the other Contracting State may be taxed in that other State' (Article 10 (1) DTA GerNo). However, according to Article 10 (2) DTA GerNo 'such dividends may also be taxed in the Contracting State of which

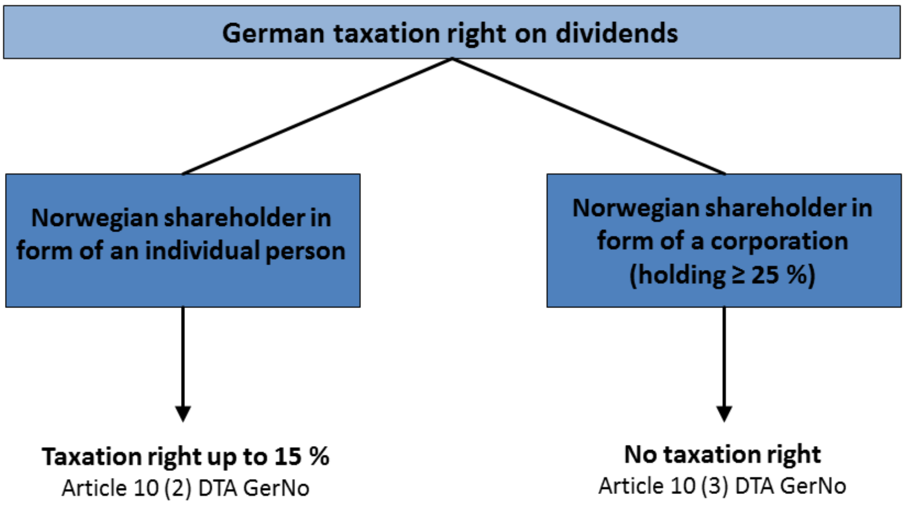
[120] Braun, 2008, p. 123.
[121] Brähler, 2012, pp. 78–79.

the company paying the dividends is a resident […]'. As a result, also Germany has a right to tax dividends paid by German corporation to a Norwegian shareholder. This right is, however, limited by Article 10 (2) DTA GerNo to a maximum charge of 15 %. Article 10 (3) DTA GerNo is furthermore restricting a German taxation by excluding Norwegian shareholders in form of a corporation that holds at least 25 % of the shares of the distributing German corporation. This regulation is an implementation of the internationally commonly used 'intercorporate privilege' ("Schachtelprivileg"). The principle of an international intercorporate privilege describes the favourable tax treatment of dividends from a qualified holding, distributed by a foreign corporation to a national shareholder. The general aim of the intercorporate privilege is to mitigate or eliminate double taxation as a result of taxing the distribution of dividends on multiple levels. The OECD-MA limits the taxation rates of the so called intercompany dividends to 5 % in the source state.[122] However, some DTAs set a higher tax rate while others, as the DTA between Germany and Norway, totally disallow the taxation in the state of source under certain conditions. Thus, a German taxation of dividends is only granted for individual persons or corporations holding a share of under 25 %. Due to the characteristics of a Norwegian market entrance in Germany, an investment share of fewer than 25 % is of minor importance in order to address the topic of the thesis.

[122] Gehrmann, 2012e, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f230%2f000230561_0001_index.xml&aktion=DokumentAnzeigen.

The following figure is illustrating the German taxation right on dividends, distributed to an individual person or a corporation holding at least 25 % of the shares:

Figure 9: German taxation right on dividends



Source: Own illustration.

Even though both states have a certain right to tax dividends paid to the Norwegian shareholder, a double taxation and hence a doubled tax burden for the shareholder should be avoided. Thus, Article 23 (1) b DTA GerNo states that 'the first-mentioned State shall allow as a deduction from the tax on the income of that residence an amount equal to the tax paid in that other State.' On this legal base, the Norwegian shareholder can deduct the German tax burden from the Norwegian tax on the dividends paid. In this way a double taxation is avoided.

In case dividends are distributed from a German to a Norwegian corporation, Article 23 of the DTA GerNo includes further restrictions. As we already know, Germany has no taxation rights on such dividends if the shareholder holds at least 25 % of the shares. In contrast to this, the DTA GerNo is not generally disallowing Norway the taxation of German dividends. However, Article 23 (1) c DTA GerNo is referring to Norway's national legislation and states that the dividends have to be exempted from taxation in the same way as if both corporations would be resident in Norway. In other words, the same regulations have to apply for German dividends as for dividends distributed by a Norwegian corporation to another Norwegian corporation. In this way, it is assured that also dividends from a German corporation enjoy the protection of the Norwegian national intercorporate privilege.

In case the tax on dividends is levied by a withholding tax, the DTA GerNo is according to Article 28 (1) GerNo not limiting the national right to do so. As a result, even though a country's taxation right on dividends is limited by the DTA GerNo, there is no limitation regarding an initial tax deduction at source. This regulation is crucial for the German withholding tax on capital investment as already presented in the paragraph 3.1.1. Even though Article 10 DTA GerNo is limiting a German taxation of dividends that are distributed to a Norwegian shareholder, the withholding tax on capital investment has to be deducted and transferred by the German corporation (§ 50d (1) EStG).

5.3.1.3. Tax burden and collection in Germany

Following paragraph is discussing the tax burden and collection of a Norwegian company that is operating in form of a German corporation. In this respect, it is again meaningful to distinguish between a company and a shareholder level.

Company level

On a company level, the German corporation is subject to corporate tax. As we already know, the corporate tax rate is 15 % plus the solidarity surcharge of 5.5 %. In combination with the municipal trade tax, the total tax burden amounts to around 30 %. Since the municipal trade tax rate is set by the municipalities themself, the total tax burden depends on the location of the business. A detailed explanation of the determination of the municipal trade tax can be found in paragraph 2.1.3.

Shareholder level

As already described, distributed income is subject to taxation at shareholder level once again. In case the shareholder is an individual person, the dividends are generally considered as income from capital investment in the meaning of § 20 (1) Nr. 1 & 2 EStG. As earlier mentioned, this type of income is subject to the special regulations of the withholding tax on capital investment under the German personal income tax act (§ 43 (1) EStG). Instead of the general progressive income tax rate, the shareholder is paying a flat rate tax of 25 % ("Abgeltungsteuer") plus solidarity surcharge (§ 43a (1) S. 1 Nr. 1 EStG). As the name already implies, the tax is levied in form of a withholding tax (§ 44 S. 3 EStG). That means that the distributer of the income is obliged to withhold and deduct the tax from the payment and subsequently transfer the amount to the financial authorities.[123] Applied to our topic, the German corporation withholds and transfers the tax of the Norwegian shareholder to the German tax authorities. Even though the tax is withheld and transferred by the German corporation, it should be noted that the Norwegian shareholder is subject to taxation.

If the investment is, however, part of the business assets of the shareholder, income distributed from a corporation is taxed as part of the personal income tax. In applying this so called 'partial income method' ("Teileinkünfteverfahren"), only 60 % of the income is subject to taxation (§ 3 Nr. 40 S. 1 d & e EStG). Since the withholding tax on capital investment is still initially deducted, the Germany tax authorities credit the whole amount on the tax burden of the personal income tax (§ 36 (2) Nr. 2 EStG).[124] In case the investment is part of the private assets of the shareholder and therefore generally subject to the regime of the flat rate tax, there exists the possibility to apply for the partial income method if the shareholder holds at least 25 % of the corporations assets or at least 1 % in combination with a regular employment in the same corporation (§ 32d (2) Nr. 3 EStG).[125]

The opportunity of the partial income method is especially attractive if the investment in the German corporation implies expenditures for the Norwegian shareholder. A typical example for such expenses would be the cost of debt through external financing. In contrast to the withholding tax on capital investment, the partial income method opens up the possibility to deduct expenditures from the distributed income and reduces in this way the taxable base. However, according to § 50 (2) S. 1 EStG, the initially deducted withholding tax on capital investments is generally considered as final for limited liable persons. Hence, a Norwegian shareholder in form of an individual person with only limited tax liability in Germany is normally not entitled to opt for the partial income method.[126] Yet, in the special case that the investment of such a person is part of the business assets of a permanent establishment, the partial income method applies regardless of this regulation.[127] Since this situation would include a third level of participation in the analysis, the thesis will disregard this particular

[123] Roning, 2012, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f097%2f000097065_0001_index.xml&aktion=DokumentAnzeigen.

[124] Gehrmann, 2012f, http://www4.nwb-datenbank.de/nwb9/main.aspx?kaufschritt=Default&dokurl=content%2fdms%2finfoCenter%2fdata%2f000%2f114%2f000114780_0001_index.xml&aktion=DokumentAnzeigen.

[125] Gunsenheimer, 2012, p. 409.

[126] Brähler, 2012, p. 280.

[127] Höhn/ Höring, 2010, p. 98.

case in order to keep the comparison of the investment alternatives easily understandable. Moreover, the variation of the results would be marginal in the applied model. The reason for this lies in the simplification that disregards allowable business expenditures on shareholder level and assumes a maximal individual tax rate. As a result of these preconditions, the eventual tax rate of the partial income method is 27 % (100 x 60 % x 45 %) and thus even 2 % higher than the withholding tax on capital investment.

In case the shareholder is a corporation itself, 95 % of the dividends in the meaning of § 20 (1) Nr. 1 EStG are exempt from taxation (§ 8b KStG). Despite this tax exemption, the withholding tax on capital investment is initially deducting 25 % from the dividends (§ 43 (1) EStG) which is later fully refunded. However, § 32 (1) KStG is excluding income from corporations with limited tax liability from this regulation. Thereby, particularly the exclusion of foreign corporations that reside in the EEA is against the backdrop of the European integration, a controversial topic. In this regard, the ECJ addressed the issue and declared in 2011 the German taxation of dividends by a final withholding tax as contrary to European community law (Case C-284/09).[128] As a response, the German authorities are discussing a new law that implements the court decision and complies with European legislation. Since the draft law includes not only the possibility of a future tax relief for foreign corporations but also a retroactive refund, the German authorities face in the next two years a considerable financial burden through the pay back.[129]

In consideration of these just explained regulations, we arrive at the conclusion that regardless of whether the shareholder is an individual person or a corporation, 25 % withholding tax on capital investments is initially deducted and transferred to the German financial authorities. Furthermore, a limited liable Norwegian company has at the moment not the possibility to opt for an individual tax assessment or benefit from the extensive tax exemptions for corporations. However, the DTA GerNo limits the German right of taxation for individual persons to 15 % and exempts corporations (holding ≥ 25 %) entirely. Thus, Germany is, upon request, refunding the difference between the deducted withholding tax and the permitted amount by the DTA GerNo to the Norwegian company (§ 50d (1) S. 2 & 3

[128] Schönhaus/ Broekmann, 2012, p. 623.
[129] Haufe, 2012, http://www.haufe.de/steuern/gesetzgebung -politik/milliarden-an-kapitalertragsteuer-erstatten_168_144418.html.

EStG).[130] The refund application has to include a tax residence certificate from the foreign tax authorities (§ 50d (4) S. 1 EStG). In this way, the German tax authorities can assure that the DTA is applicable to the foreign shareholder. Another reason for the requisition of a residence certificate is the desire to avoid a 'double non-taxation'. Through the process of issuing a certificate, the Norwegian tax authorities are getting informed about the payment and can themselves initiate the taxation of the dividends.[131] Since the withheld and later refunded tax is temporarily not available for the Norwegian company, the German regulation causes interest and liquidation disadvantages. However, this issue is discussed in more detail in the evaluation paragraph of 6.1.1.

5.3.1.4. Taxation in Norway

As explained in the paragraph 5.3.1.2, Norway has a general taxation right on dividends distributed by a German corporation to a Norwegian shareholder. Since the Norwegian taxation depends on the legal form of the shareholder, we distinguish between an individual person and a corporation.

Dividends distributed from a German corporation to an individual Norwegian shareholder are taxed with a maximal tax rate of 28 %. As already mentioned in paragraph 5.1.1.4, the Norwegian lax authorities provide a tax allowances of 2 % of the invested capital (§ 10 – 12 Skatteloven). Since Germany has also a taxation right, the DTA between German and Norway avoids double taxation through the application of the credit method. According to Article 23 (1) b DTA GerNo, a Norwegian shareholder can deduct the effective German tax burden of 15 % from its tax burden in Norway.[132]

In case the Norwegian shareholder is a corporation, the DTA GerNo is generally allowing Norway the taxation of dividends. However, Article 23 (1) c DTA GerNo is referring to Norway's national law and states that the dividends have to be treated in the same way as if both corporations would be resident in Norway. In other words, the same regulations have to apply for German dividends as for dividends distributed by a Norwegian corporation to another Norwegian corporation. When examining the Norwegian tax legislation, it appears

[130] Oberfinanzdirektion Frankfurt am Main, direction of June 6, 2012, Erstattung der Kapitalertragsteuer bei Steuerausländern.

[131] Nieland, 2012, recital 301.

[132] Bakketun, personal interview of September 26, 2012 with reference to Stortingsvedtak 25.11.2010 Nr. 1529 om skatt av inntekt of formue mv. for inntektsåret 2011, Kapittel 3.

that Norway too is following the intercorporate privilege. In this respect, Norway is more or less tax exempting the dividend flow between corporations. Only 3 % of the distributed dividends are subject to taxations with a tax rate of 28 %. This is resulting in an effective tax rate of 0.84 %.[133]

5.3.1.5. *Example calculation*

Table 3 illustrates the calculation of the tax burden of a Norwegian subsidiary in form of a German corporation. As explained in the paragraphs above, it is necessary to distinguish between a Norwegian shareholder as an individual person and a corporation. In case the Norwegian shareholder is a corporation, we further differentiate between a holding of more and less than 25 % of the shares in the German corporation. As already mentioned, the characteristics of a market entrance of a Norwegian company in Germany implicate generally a majority holding in the subsidiary. Thus, the illustration of the tax burden of a corporation holding less than 25 % of the shares serves primary the purpose to present a complete picture. For reasons of simplification, we assume that the whole profit is distributed to one single shareholder:

Table 3: Calculation of the tax burden of a corporation

	Shareholder Individual person	Shareholder Corporation (b) (holding ≥ 25 %)	Shareholder Corporation (a) (holding < 25 %)
Pre-tax profit	€ 100	€ 100	€ 100
(1) Corporate tax (2) Solidarity surcharge (3) Municipal trade tax	€ - 15 € - 0.825 € - 14	€ - 15 € - 0.825 € - 14	€ - 15 € - 0.825 € - 14
After tax profit at company level (Ger)	€ 70.175	€ 70.175	€ 70.175
(4) Withholding tax on capital investments (5) Solidarity surcharge (6) Refund of withholding tax & Solidarity surcharge	€ - 17.544 € - 0.965 € + 7.983	€ - 17.544 € - 0.965 € + 18.509	€ - 17.544 € - 0.965 € + 7.983
After tax profit at shareholder level (Ger)	€ 59.649	€ 70.175	€ 59.649
(7) Norwegian taxation	€ - 3.523	€ - 0.589	€ - 0.589
After tax profit at shareholder level 1 (No)	€ 56.126	€ 69.586 *(company level)*	€ 59.060 *(company level)*
(8) Norwegian taxation		€ - 13.884	€ - 10.937
After tax profit at shareholder level 2 (No)		€ 55.702 *(shareholder level)*	€ 48.123 *(shareholder level)*

[133] Zielke, 2012, p. 563; Bakketun, personal interview of September 26, 2012.

Calculations:

(1) € 100 x 15 % = € 15
(2) € 15 x 5,5 % = € 0.825
(3) € 100 x 14 % = € 14
(4) € 70.175 x 25 % = € 17.544
(5) € 17.544 x 5,5 % = € 0.965
(6) Calculation of the withholding tax & solidarity surcharge refund:

	Individual person/ Corporation holding < 25 %	Corporation holding ≥ 25 %
Actual tax value after German taxation:	*Withholding tax (25 %) plus solidarity surcharge (5.5 %)* € 17.544 + € 0.965 = € 18.509	*Withholding tax (25 %) plus solidarity surcharge (5.5 %)* € 17.544 + € 0.965 = € 18.509
Permitted tax value according to DTA GerNo:	*Maximal tax according to DTA (15 %) -> no solidarity surcharge* € 10.526 + € 0 = € 10.526	*Maximal tax according to DTA (0 %) -> no solidarity surcharge* € 0 + € 0 = € 0
Refund of withholding tax:	*Actual value minus desired value* € 18.509 - € 10.526 = € 7.983	*Actual value minus desired value* € 18.509 - € 0 = € 18.509

(7) Norwegian tax burden for an individual person:

After tax profit at company level (Ger)	€ 70.175
Allowance 2 % of invested capital Assumption: Invested capital = € 1,000	€ - 20 *(€ 1,000 x 2 %)*
Taxable base	€ 50.175

Norwegian taxation 28 %	€ 14.049 *(€ 50.175 x 28 %)*
German taxation	€ - 10.526 *(€ 10.526 + € 0)*
Actual Norwegian tax load	€ 3.523

Norwegian tax burden for a corporation:

After tax profit at company level (Ger)	€ 70.175
Taxable base 3 % of distributed dividend	€ 2.105 *(€ 70.175 x 3 %)*
Norwegian taxation 28 %	€ 0.589 *(€ 2.105 x 28 %)*

(8) a) € 69.586 - (€ 1,000 x 2 %) x 28 % = € 13.884 b) € 59.060 - (€ 1,000 x 2 %) x 28 % = € 10.937

Source: Own tables and calculations.

As already mentioned, the tables above distinguish between three types of shareholders: An individual person, a corporation with a shareholding of at least 25 % and a corporation with a shareholding below 25 %. For each type, we assume a profit of € 100. The taxation at company level is not affected by the different types of shareholders. As a first step, the profit is subject to the corporate tax (1), the solidarity surcharge (2) and the municipal trade tax

(3). Again, we assume the same taxable base for the municipal trade tax and use a rounded average of 14 %.

After the subtraction of these three German taxes, we arrive at the after tax profit at company level. In a next step, we assume that 100 % of the profit is distributed to one shareholder. Irrespectively of the type of shareholder and the resulting DTA allocation of taxation rights, the distributing corporation has to withhold 25 % withholding tax on capital investments (4). Based on this amount, a second solidarity surcharge (5) is levied. As earlier explained, the DTA GerNo is restricting the taxation right of Germany. Depending on the type of shareholder, the withholding tax has to be fully or partly refunded (6). If the shareholder is an individual person or a corporation holding less than 25 %, the German taxation right is limited to 15 %. Thus, the deducted excess amount of 10 % plus the solidarity surcharge has to be refunded. In case the shareholder receives a dividend from a holding of at least 25 %, Germany has no taxation right at all and the full amount is refunded. After these deductions and refunds, we arrive at the profit after German taxation at shareholder level (Ger). At this level, we can identify a lower tax burden for shareholders in form of a corporation with a holding of at least 25 % in the German corporation. In this regard, it has to be noted that the results of this calculation does not include the interest disadvantages of the initially deducted and later refunded excessive tax burden. In order to arrive at the true after tax profits, an individual defined discount rate has to be applied on the refunded tax. However, for the purpose of this thesis, the accuracy of the current results is sufficient.

Despite of the German taxation, also Norway has the right to tax the distributed dividends (7). In this situation, we distinguish between individual persons and corporations in general. When calculating the tax burden for individual persons, we have to subtract the allowance of 2 % of the invested capital from the taxable base. The tax rate for the dividends is 28 %. Since a double taxation of dividends should be avoided, the German tax is deducted from the Norwegian tax burden. In case the Norwegian shareholder is a corporation, only 3 % of the distributed dividends are subject to taxation with a tax rate of 28 %.

After this taxation, we arrive at the profit after Norwegian and German taxation at the first shareholder level (No). When comparing the different outcomes, we can recognize that the tax burden of the corporation with a holding of at least 25 % is still considerable lower than for the other two types of shareholders. The differences between the shareholder in form of an individual person and a corporation with a holding lesser than 25 % is in comparison considerable lower. However, if the Norwegian company is a corporation itself, the dividends are distributed to the company level of the Norwegian corporation. In other words, the dividends are not yet at a shareholder level of an individual person. Thus, when distributed to an individual person in Norway, the dividend is once more subject to taxation (8). The Norwegian tax authorities levy 28 % tax and grant an allowance of 2 % of the invested capital. As a result, a corporation that holds at least 25 % can distribute a profit of € 55.702 while a corporation with less than 25 % can only pay a dividend of € 48.123. As a remainder, the Norwegian company in form of an individual person remains with an after tax profit of € 56.126. When comparing the results it can be seen that the individual person and a corporation holding at least 25 % are subject to a fairly similar tax burden, while a corporation with less than 25 % is taxed more. The reason for the unequal treatment lies in the German taxation through the withholding tax on capital investment and its 'finality' for limited liable companies. In combination with the 'protection' of corporations with a holding of at least 25 % by DTA GerNo, it creates a situation of a prohibitive taxation of participations under 25 %. Since persons that are unlimited liable to taxation in German are not facing this discrimination, the regulation has been identified as contrary to European community law (see paragraph 5.3.1.3).

5.3.2. Use of losses

5.3.2.1. In Germany

As previously described, corporations are separate legal entities and the taxation of shareholders and the corporation is disconnected. Since the income of a corporation is taxed at company level, the losses can only be used on company level. A 'distribution' of the losses to the shareholders of a corporation is therefore not possible.

At company level, the corporation is liable to corporate taxation (§ 1 (1) KStG). However, since § 8 (1) KStG refers to the EStG in regard to the determination of the total net income, the regulation of § 10d EStG applies also for corporation. In addition to § 10d EStG, there are certain special rules for corporations. In this regard, § 8c KStG states that the right of loss deduction can expire if more than 25 % of the shares or voting rights of the Norwegian corporation are transferred to one purchaser or to several persons affiliated with each other within a period of five years. This legal norm shall prevent the purchase of an ailing company with the only purpose of reducing one's own tax burden through the company's deductible losses. Since a corporation is additionally subject to municipal trade tax (§ 2 (2) GewStG), the regulations of § 10a GewStG, regarding the use of a municipal trade lax loss, are also applicable for corporations. In contrast to the use of a corporate tax loss, the rules of § 10a GewStG allow only a carry forward. The earlier paragraph of 6.1.2.1 covers the regulations of § 10d EStG, § 8c KStG and § 10a GewStG in greater detail and can be reviewed for further information about the possibilities of corporations to set off losses.

Even though the losses of a corporation cannot be distributed to its shareholders, German legislation allows generally the use of capital losses as a result of terminating the participation. In case the shareholder is disposing a holding in the meaning of § 17 EStG and incurs a capital loss, the income can be balanced within a period (§ 2 (3) EStG) and deducted from profits in other periods according to the regulations of § 10d EStG.[134] However, the DTA between German and Norway is allocating the taxation right for capital gains to Norway (Article 13 (6) GerNo). As a general rule, losses can only be used in the country with a taxation right on the profits. As a consequence of the symmetry thesis, capital losses of a limited liable person cannot be used in Germany.[135]

5.3.2.2. In Norway

The Norwegian tax legislation does not provide regulations that allow a Norwegian parent company to deduct losses that are generated by its German subsidiary from its profits in Norway.[136] As explained in paragraph 6.1.2.2, the Norwegian tax authorities, in this regard, follow the principle of the symmetry thesis.[137] However, Norway is part of the EEA and thus bounded to the Treaty of the European Community. On the base of this multilateral agreement, the ECJ decided that losses from a German subsidiary must be deductible from Norwegian profits if there is no possibility to offset the losses in Germany. Hence, in respect to European law, a loss deduction in Norway cannot be ruled out for certain situation.[138]

[134] Jäschke, 2012b, recital 324.
[135] Diller/ Kittl, 2012, p. 271.
[136] Bakketun, personal interview of September 26, 2012.
[137] Schella, 2009, p. 13.
[138] von Brocke/ Auer, 2010, p. 755.

A termination of the participation in the German corporation by the Norwegian shareholder might result in a capital loss. Depending on the legal type of the shareholder, a loss deduction in Norway might be possible. In case the shareholder is an individual person, the loss can be offset with profits in Norway. If the shareholder is a corporation, it is not possible to use the losses in Norway.[139]

5.3.3. Termination of engagement in Germany

5.3.3.1. Tax effects in Germany

The operations of a corporation in Germany can be terminated by alienation or liquidation of the business. In order to analyse the tax affects, we distinguish again between company and shareholder level. Starting with the company level, the disposal of a corporation has besides the expiration of the use of losses (§ 8c KStG) no direct tax effects. Is the corporation not just disposed but liquidated, § 11 KStG sets the legal base for the taxation of profits resulting from the disclosure of hidden reserves. The objective of liquidation is to finish up current business and the collection of all company assets. These assets are converted to cash, which is used to pay back creditors and distribute (if available) remaining profits to the shareholders.[140] The profit in form of a capital gain is subject to corporate taxation which is determined by subtracting the 'liquidation-start-capital' from the 'liquidation-end-capital'.[141] Besides of corporate tax, capital gains from liquidation are also subject to municipal trade tax according to § 7 S. 1 GewStG.

At the shareholder level, the disposal of a holding in a corporation leads to income from trade and business according § 17 EStG. The precondition is, however, that the disposing shareholder has been participating in the corporation with a share of at least 1 percentage within the last 5 years. If this requirement is not fulfilled, the capital gain is liable to the withholding tax on capital investment according to § 43 EStG. Since the characteristics of an investment by a Norwegian business with the intention to get active in the German market is usually fulfilling these requirements, we can assume income in the meaning of § 17 EStG. In case the shareholder is not disposing its holding, but the corporation is liquidated, § 17 (4) EStG states that capital gains from a liquidation are also considered as income from trade and business in the meaning of § 17 EStG. Thus, such income is considered as a sale of shares

[139] Bakketun, personal interview of September 26, 2012.
[140] Klaus Stein, 2012, recital 1.
[141] Ibid., recital 42.

rather than a profit distribution. In addition, § 49 (1) Nr. 2 e EStG is including income in the meaning of § 17 EStG to the catalogue of limited tax liable income. Hence a limited tax liability is established for a Norwegian shareholder, disposing its holding in a German corporation. Nevertheless, taxation in Germany is only possible if the DTA between Germany and Norway is also allocating the taxation right to Germany. In the case of income from capital gains, this is not the case. Article 13 (6) GerNo is allocation the taxation right to Norway: 'Gains from the alienation of any property, other than that referred to in the previous paragraphs shall be taxable only in the Contracting State of which the alienator is a resident.' Hence, at shareholder level, Germany has to refrain from the taxation of capital gains as a result of disposing or liquidating a corporation.

5.3.3.2. Tax effects in Norway

As mentioned before, corporations are own legal entities and themselves liable for taxation. Because of this, the taxation of shareholders and the corporation is separated. Against this background, the German subsidiary has, on company level, no tax relations to Norway. Therefore, a termination of the engagement has no tax effects in Norway.

However, since a Norwegian company is participating in the German corporation, a termination of the engagement can have a Norwegian tax effect on a shareholder level. In case the corporation is disposed or liquidated, the Norwegian shareholder might achieve a capital gain, leading to a tax liability in Germany. Yet, since Germany has according to Article 13 (6) GerNo no taxation right on capital gains, taxation depends merely on Norwegian regulations. In this regard, Norwegian national law distinguish between shareholders in form of individual persons and corporations. In case the Norwegian shareholder is an individual person, capital gains as a result of the disposal or liquidation of the corporation are subject to taxation in Norway. The capital gains are taxed in the same way as dividends. Thus, 2 % of the invested capital is deducted as an allowance and the resulting taxable base is multiplied by a tax rate of 28 %. If the shareholder is not an individual person but itself a corporation, capital gains are free from taxation in Norway.[142]

[142] Bakketun, personal interview of September 26, 2012.

6. Evaluation of investment alternatives

The following section is evaluating the three different investment alternatives in regard to the significant aspects of taxation. In order to illustrate the results, the author creates two tables that summarize the main findings of the conducted analysis. The first table shows the results for an investor in form of an individual person, while the second table assumes a Norwegian company in form of a corporation. The separation into two types of Norwegian investors is based on the fact that it constitutes the most constant variable. In other words, the Norwegian company is, most likely, already an individual person or a corporation when it intends to start business operations in Germany. In this way, the appropriate table can be chosen for further investigation on the base of the initial situation.

Within the tables, the three investment alternatives of a permanent establishment, a business partnership and a corporation are examined in the frame of references. Due to the characteristics of a market entrance in Germany, it is assumed that the Norwegian company is holding at least 25 % of the shares in the German corporation. As already known, the frame of references consists of the significant tax aspects of current taxation, use of losses and termination of engagement. The application of these three aspects is furthermore divided into the relevant countries of Germany and Norway. In this context, the column of the tables defines the different investment alternatives while the lines represent the significant aspects of taxation. The resulting matrix presents the main points of the tax analysis.

On the base of this matrix, the results of the different investment alternatives are compared and variations are evaluated. In this way, it is possible to point out situations for which one or another investment alternative entails a tax advantage. However, the tax outcome of the different investment alternatives might frequently be identical. In these cases, tax aspects do not constitute a crucial factor of decision and are not further discussed.

6.1. Norwegian company in form of an individual person

Table 4 summarises the results of the conducted analysis for a Norwegian company in form of an individual person. Since a detailed explanation or calculation can be found in the respective parts of the thesis, the author focuses merely on the presentation of the main findings. The matrix follows the structure as just described in the introduction of this section. The three paragraphs subsequent to the comparative table present an evaluation of the results.

Table 4: Tabular comparison of investment alternatives for an individual person

	Permanent establishment	**Business partnership**	**Corporation (holding ≥ 25 %)**
Current taxation in Germany	Business profit € 100 German tax € - 48.175 After tax profit € 51.825 *Preferential tax for retained profits:* Business profit € 100 German tax I € - 37.051 After tax profit reinvestment € 62.949 German tax II € - 11.655 After tax profit distribution € 51.294	Business profit € 100 German tax € - 48.175 After tax profit € 51.825 *Preferential tax for retained profits:* Business profit € 100 German tax I € - 37.051 After tax profit reinvestment € 62.949 German tax II € - 11.655 After tax profit distribution € 51.294	Business profit € 100 German tax I € - 29.825 After tax profit company level € 70.175 German tax II € - 10.526 *Withheld € - 18.509* *Refunded € 7.983* After tax profit shareholder level € 59.649
Current taxation in Norway	According to DTA no taxation right for Norway	According to DTA no taxation right for Norway	After tax profit company level € 59.649 Norwegian tax € - 3.523 After tax profit shareholder level € 56.126
Use of losses in Germany	<u>Individual income tax</u> Unlimited within a period Carry backwards up to € 511,500 Carry forward up to € 1 million without restrictions, exceeding amount to 60 % <u>Municipal trade tax</u> Only carry forward, without restrictions € 1 million, exceeding amount to 60 %	<u>Individual income tax</u> Loss directly allocated to the partners Use of losses ← See left column <u>Municipal trade tax</u> ← See left column	**Company level** <u>Corporate tax</u> Use of losses generally the same as individual income tax ← See left column <u>Municipal trade tax</u> ← See left column **Shareholder level** Only a capital loss after disposal/liquidation can be deducted, but no taxation right for Germany according to DTA → No loss deduction (symmetry thesis)

Use of losses in Norway	Norwegian legislation Loss deduction generally not possible (symmetry thesis) European community law Loss deduction must be possible if no possibility exist to offset losses in Germany (freedom of establishment)	Norwegian legislation Loss deduction generally not possible (symmetry thesis) European community law Loss deduction must be possible if no possibility exist to offset losses in Germany (freedom of establishment)	Norwegian legislation Loss deduction generally not possible (symmetry thesis) European community law Loss deduction must be possible if no possibility exist to offset losses in Germany (freedom of establishment) Capital loss Deductible with profits in Norway
Termination of engagement - German tax consequences	Business disposal Capital gain liable to personal income tax in Germany Liquidation & asset transfer to Norway Disclosed hidden reserves taxed as capital gains in Germany	Business disposal Capital gain liable to personal income tax in Germany Liquidation & asset transfer to Norway Disclosed hidden reserves taxed as capital gains in Germany	**Company level** Disposal of shares No tax effect, besides regulations to expiration of loss deduction Liquidation Capital gain (after disclosure of hidden reserves) is subject to corporate & municipal trade tax **Shareholder level** Business disposal/Liquidation Capital gain liable to personal income tax, but no taxation right for Germany according to DTA.
Termination of engagement - Norwegian tax consequences	Capital gain According to DTA, taxation right is allocated to Germany → no taxation in Norway	Capital gain Business partnership is according to DTA considered as permanent establishment → no taxation in Norway	Capital gain Liable to tax in Norway, DTA allocates taxation right to Norway → taxation in Norway

Source: Own table and calculations.

6.1.1. Current taxation

In case a Norwegian individual person is planning a long-term investment in Germany and expects positive returns which shall be reinvested in Germany, a subsidiary in form of a corporation has advantages in regard to current taxation. The after tax profit at company level amounts to € 70.175 for a corporation while a permanent establishment or a business partnership remains with a profit of only € 51.825. In other words, the overall taxation rate for the two last mentioned types of entities is 48.175 % whereas corporations pay only

29.825 %. As a result, a corporation can reinvest additionally € 18.350 into the German business operation. Since this would mean a significant disadvantage for an individual person and a business partnership, the German tax authorities introduced in 2008 the regulations to the preferential tax treatment for retained profits according to § 34a EStG. In case this regulation is applied, the profit which is available for reinvestment in Germany increases to € 62.949. As a result, the difference between the investment forms minimizes to an amount of € 7.226. However, the regulation of § 34a EStG is very complex and creates a significant administration effort. In order to optimal utilize the regulation, an in-depth analysis of the operating and financial structure of the company is necessary. Especially for a foreign company, the additional tax planning effort and consultancy costs are considerable constraints.[143] In addition, the preferential tax treatment for retained profits is not applying a progressive tax rate. The total tax burden after subsequent taxation amounts to a fixed rate of 48.706 %. In comparison to the total maximal tax rate of 48.175 %, which is assumed for the example calculations, the additional tax burden is rather small. However, in case the Norwegian company is not liable to the maximal tax rate, the additional tax burden increases with the decrease of the individual tax rate. Thus, as lower the company's profits are, as such less attractive is the regulation of § 34a EStG. Table 5 is illustrating the correlation between the individual tax rate and the advantages and disadvantages of the preferential tax treatment for retained profits. As we already know, the preferential tax rate is 28.25 % while the subsequent tax rate amounts to 25 %. An example calculation for the disadvantages after subsequent taxation can be found below the table:

Table 5: Tax advantages and disadvantages of § 34a EStG in regard to the individual tax rate

Individual tax rate	Preferential tax rate for retained profits	Advantages through preferential tax rate	Disadvantages after subsequent taxation
ESt 45 %	28.25 %	16.75 %	- 1.1875 %
ESt 42 %	28.25 %	13.75 %	- 4.1875 %
ESt 40 %	28.25 %	11.75 %	- 6.1875 %
ESt 30 %	28.25 %	1.75 %	- 16.1875 %
ESt 28.25 %	28.25 %	0 %	- 17.9375 %

Example calculation: 45 % - ((100 – 28.25 %) x 25 % + 28.25 %) = - 1.1875 %

Source: Own translation of van Heek, 2012, p. 505.

[143] van Heek, 2010, pp. 507–508.

As we can see in Table 5, the tax disadvantage after subsequent taxation is increasing with a decrease of the individual tax rate. Even though the additional tax burden after subsequent taxation is reduced by the interest profits as a result of the tax deferral, the disadvantages in case of lower individual tax rates can be quite significant. This factor is even more severe, since subsequent taxation takes place in later years and a prediction of the company's profits and thus a prediction of the individual tax rate might be very difficult. Taking all these aspects into consideration, a meaningful application of § 34a EStG is most likely for companies with relatively large profits, high planning certainty and the capability to cope with an extensive administrative effort. These characteristics might rather be allocated to larger companies which are also suitable to establish and maintain a corporation in Germany. In case an individual person has not the appropriate structure to set up a corporation in Germany, a meaningful application of the preferential tax treatment for retained profits might be very doubtful. In a reversed situation, where the company and its business venture have the characteristics that are appropriate for the establishment of a corporation or the application of § 34a EStG, a corporation might be the better choice anyway. Based on these findings, the author sees generally an advantage in a subsidiary in form of a corporation if the Norwegian company is an individual persons and intents to reinvest its positive returns in Germany.

If the corporation is planning to repatriate and distribute the profit to its shareholders in Norway, the profits are subject to a second German as well as a Norwegian taxation. After these deductions, the profit diminished from € 70.175 to only € 56.126. Even though the after tax profit of the corporation is still € 4.301 higher than for a permanent establishment and a business partnership, the difference is relatively small. This remaining tax benefit of a corporation is furthermore reduced by the interest disadvantage of the initially deducted and excessive tax burden of the German withholding tax on capital investment. As already explained, the DTA GerNo allocates a taxation right of 15 % to Germany. Yet, according to German legislation, an amount of 25 % must initially be deducted and transferred to the national tax authorities. Later on, the difference between the deducted and the permitted tax burden is refunded upon request. With respect to the numbers of our example, a withholding tax on capital investment plus solidarity surcharge of € 18.509 is initially deducted. Since the final tax burden is, according to the DTA GerNo, not allowed to exceed € 10.526, the German tax authorities refund an amount of € 7.983. In other words, more than 12 % of the entitled after tax profit is initially not available to the Norwegian shareholder and constitutes thus a considerable disadvantage with regards to interest and liquidity. That means, in the period between the distribution of the dividends and the receipt of the refund, the Norwegian company has not the possibility to reinvest the inaccessible part of the profit and thus not the possibility to generate a return. In case of a liquidity shortage, the Norwegian company might be required to seek external financing in order to compensate for the withholding of the profit. The actual degree or amount of these disadvantageous aspects depends of course on the individual situation of the shareholder as well as various external factors (e.g. interest level). As a consequence of the interest and liquidity disadvantages, the tax benefit of a corporation is furthermore reduced or might even be completely lost. Thus, if the main objective is to repatriate the profit instead of reinvesting it, an alternative without the foundation of a corporation might be the better choice.

Since tax aspects deliver, in this case, not a clear conclusion about the most advantageous investment alternative, aspects other than taxation might be taken into account. In this regard, an excursus in paragraph 6.2.4 provides a short overview about some other factors that could influence the decision between a corporation and a permanent establishment or business partnership.

6.1.2. Use of losses

In case the Norwegian company is an individual person, the choice of the investment alternative has no significant effects on the use of current losses in Germany and Norway. In Germany, the losses of a permanent establishment and a business partnership can be used according to national regulations as described in paragraph 5.1.2.1 and reduce the taxable base of the individual income as well as municipal trade tax. In case the German business is established in form of a corporation, it has to be distinguished between the company and shareholder level. At a company level, the legislation of the corporate tax applies. Since the regulations of loss deduction are generally the same for corporations as for individual persons, the use of losses on company level constitutes no crucial factor.

Based on the symmetry thesis, the Norwegian tax authorities do not allow a tax deduction of losses that are generated in Germany. Nevertheless, European Community law requires that a member state of the EEA provides the possibility to offset losses that have been generated in another member state if it is not possible to deduct these losses from profits in the source state. However, whether the affiliated company is a permanent establishment, a business partnership or a corporation is generally not influencing this principle and has thus no effects on the use of losses.

In contrast to a permanent establishment and a business partnership, a corporation is divided into a company and shareholder level. Because of the separation principle, losses of a company can only be used on a company level. However, in case the Norwegian individual person is generating a capital loss as a result of the disposal of the shares or a liquidation of the company, the German and the Norwegian tax legislation is allowing a deduction of these losses. Since the DTA GerNo is allocating the taxation right to Norway, the individual person is able to deduct the losses from positive income in Norway. This circumstance is especially interesting for a Norwegian company in form of an individual person that expects the liquidation of its operations in Germany after a certain period of time. In such a situation, the legal certainty to be able to offset possible losses with profits in Norway is a crucial factor. Such a scenario could occur if the Norwegian company is executing a prestige project in Germany which in itself is not profitable but increases the company's reputation. Since the possibility to deduct capital losses is generally depended on the taxation of capital gains, the topic will recur in the next paragraph about the termination of engagement in Germany.

6.1.3. Termination of engagement

When examining the comparative table regarding the termination of engagement, an instant identification of possible tax advantages or disadvantages might be difficult. However, after a close observation it can be recognized that a Norwegian company with the main intention to establish a German business in order to generate a capital gain through a later disposal can achieve a tax benefit by choosing the legal form of a corporation. This result is based on following finding and additional calculations:

The engagement of a Norwegian company in Germany can be terminated by disposing or liquidating the German operations. This results either in a capital gain or a capital loss. Capitals gains from the disposal of a permanent establishment or business partnership result in a personal income liability in Germany. The same applies to hidden reserves in case of an asset reallocation to Norway in the course of business liquidation. The DTA between Germany and Norway is allocating the taxation right to Germany. In case the Norwegian company is a corporation, we have to distinguish between the company and the shareholder level. While the disposal of the shares of a corporation has no tax effect at company level, the liquidation might lead to the disclosure of hidden reserves, which results in capital gains. Such capital gains are subject to corporation and municipal trade tax in Germany. On a company level, the allocation of taxation rights by the DTA GerNo is not relevant. Capital gains that are distributed to the Norwegian company are liable to Norwegian taxation in the same way as dividends. As a consequence, the Norwegian tax authorities grant 2 % of the invested capital as an allowance and levy 28 % tax on the remaining taxable base.

Table 6 is illustrating the taxation of a capital gain as a result of a business termination. In this way, an easier comparison of the different outcomes for the different investment alternatives is provided. The calculations distinguish furthermore between a termination by disposal and a termination by liquidation. Since capital gains are generally taxed as ordinary income, we assume a profit of € 100 and use the respective result of previous calculations. The only factors responsible for the derivation from the results of the calculation of the current taxation are the allocation of the taxation rights by the DTA GerNo and the municipal trade tax exemptions for individual persons. In this regard, a detailed explanation of the calculations can be found in the previous parts of this thesis. At this point, it should be reminded that the following outcomes are only applicable for a Norwegian company in form of an individual person:

Table 6: Taxation of capital gains of an individual person

	Permanent establishment / Business partnership		**Corporation**	
Disposal	Capital gain	€ 100	Capital gain	€ 100
	(1) German taxation	€ - 47.475	German taxation	-
	After tax capital gain	€ 52.525	After tax capital gain company level	€ 100
			(2) Norwegian taxation	€ - 22.4
			After tax capital gain shareholder level	€ 77.6
Liquidation	Capital gain	€ 100	Capital gain	€ 100
	(1) German taxation	€ - 47.475	(3) German taxation	€ - 29.825
	After tax capital gain	€ 52.525	After tax capital gain company level	€ 70.175
			(4) Norwegian taxation	€ - 14.049
			After tax capital gain shareholder level	€ 56.126

Calculations:

(1) € - 45 (Personal income tax) + € - 2.475 (Solidarity surcharge)
(2) [€ 100 - 2 % x € 1,000 (Norwegian tax allowance)] x 28 % (Norwegian tax rate)
(3) € - 15 (Corporate tax) + € - 0,825 (Solidarity surcharge) + € - 14 (Municipal trade tax)
(4) [€ 70.175 - 2 % x € 1,000 (Norwegian tax allowance)] x 28 % (Norwegian tax rate)

Source: Own table and calculations.

The taxation of capital gains from the termination of a permanent establishment leads to an identical result as for a business partnership. In this regard, it is also irrelevant whether the German operation is disposed or liquidated since both ways of termination result in an after tax capital gain of € 52.525. In contrast to this, the amount of the after tax capital gain of a corporation depends on the way of termination. In case of a liquidation, the after tax capital gain for a corporation amounts to € 56.126 and differs thus relatively little from the figure of a permanent establishment and business partnership. If the German corporation is, however, disposed by the shareholder, the tax burden is significant lower. Since the disposal has no tax effects in Germany, the shareholder achieves an after tax capital gain of € 77.6. As already mentioned before, this aspect could be crucial for a Norwegian company that intent to establish a business in Germany in order to sell it after a certain period of time. In such a case, the capital gain after the disposal of the shares is a major factor of the investment and the Norwegian company might be best of by entering the German market with a corporation.

6.2. Norwegian company in form of a corporation

The last preceding paragraphs summarised and evaluated the results for a Norwegian company in form of an individual person. In order to cover the complete scope of the topic, the following part of the thesis is paying attention to a Norwegian company in the legal form of a corporation. In this regard, we apply the same structure as above and start with a summarising table followed by an evalutation:

Table 7: Tabular comparison of investment alternatives for a corporation

	Permanent establishment	Business partnership	Corporation (holding ≥ 25 %)
Current taxation in Germany	Business profit € 100 German tax € - 29.825 After tax profit € 70.175	Business profit € 100 German tax € - 29.825 After tax profit € 70.175	Business profit € 100 German tax I € - 29.825 After tax profit company level € 70.175 German tax II € 0 *Withheld € - 18.509* *Refunded € 18.509* After tax profit shareholder level € 70.175
Current taxation in Norway	According to DTA no taxation right for Norway	According to DTA no taxation right for Norway	After tax profit company level € 70.175 Norwegian tax I € - 0.589 After tax profit shareholder level € 69.586
Dividends from a Norwegian corporation to an individual person	After tax profit company level € 70.175 Norwegian tax € - 14.049 After tax profit shareholder level € 56.126	After tax profit company level € 70.175 Norwegian tax € - 14.049 After tax profit shareholder level € 56.126	After tax profit company level € 69.586 Norwegian tax II € - 13.884 After tax profit shareholder level II € 55.702
Use of losses in Germany	Corporate tax Unlimited within a period Carry backwards up to € 511,500 Carry forward up to € 1 million without restrictions, exceeding amount to 60 % Municipal trade tax Only carry forward, without restrictions € 1 million, exceeding amount to 60 %	Corporate tax Loss directly allocated to the partners Use of losses ← See left column Municipal trade tax ← See left column	**Company level** Corporate tax Use of losses ← See left column Municipal trade tax ← See left column **Shareholder level** Only a capital loss after disposal/liquidation can be deducted, but no taxation right for Germany according to DTA → No loss deduction (symmetry thesis)

Use of losses in Norway	Norwegian legislation Loss deduction generally not possible (symmetry thesis) European community law Loss deduction must be possible if no possibility exist to offset losses in Germany (freedom of establishment)	Norwegian legislation Loss deduction generally not possible (symmetry thesis) European community law Loss deduction must be possible if no possibility exist to offset losses in Germany (freedom of establishment)	Norwegian legislation Loss deduction generally not possible (symmetry thesis) European community law Loss deduction must be possible if no possibility exist to offset losses in Germany (freedom of establishment) Capital loss Not deductible with profits in Norway, even though DTA allocates taxation right to Norway
Termination of engagement - German tax consequences	Business disposal Capital gain liable to corporate & municipal trade tax Germany Liquidation & asset transfer to Norway Disclosed hidden reserves taxed as capital gains in Germany	Business disposal Capital gain liable to corporate & municipal trade tax Germany Liquidation & asset transfer to Norway Disclosed hidden reserves taxed as capital gains in Germany	**Company level** Disposal of shares No tax effect, besides regulations to expiration of loss deduction Liquidation Capital gain (after disclosure of hidden reserves) is subject to corporate & municipal trade tax **Shareholder level** Business disposal/Liquidation Capital gain liable to corporate & municipal trade tax, but no taxation right for Germany according to DTA
Termination of engagement - Norwegian tax consequences	Capital gain According to DTA, taxation right is allocated to Germany → no taxation in Norway	Capital gain Business partnership is according to DTA considered as permanent establishment → no taxation in Norway	Capital gain DTA allocates taxation right to Norway, but no national taxation of capital gain → no taxation in Norway

Source: Own tables and calculations.

6.2.1. Current taxation

In case a Norwegian corporation expects positive returns from its operations in Germany, the choice of the investment alternative has no significant effect on current taxation. This applies regardless whether the profit is reinvested in Germany or repatriated to Norway.

The German tax burden of the different investment alternatives is generally identical and results in an after tax profit of € 70.175. Thus, if the profit shall be reinvested in Germany, current taxation constitutes not the crucial factor in choosing the most beneficial investment alternative. In case of a distribution to the Norwegian corporation, profit that has been generated by a permanent establishment or a business partnership is not subject to further taxation. In contrast to this, an income distribution by a German corporation leads to 25 % withholding tax on capital investment. Yet, according to the DTA GerNo, the full amount is refunded and the only additional burden is the cost of interest and liquidity as explained in paragraph 5.1.1. Once the profit of the German corporation is distributed to the Norwegian company, the dividends are subject to Norwegian taxation. However, the taxation of dividends, that are distributed to another corporation, are only marginal and lead to an after tax profit of € 69.586. The reason for the very low taxation is the application of the intercorporate privilege. Thus, the differences in the results of a German investment in form of a corporation and a permanent establishment or business partnership are insignificant. As a consequence, also in the case of a reinvestment in Norway, current taxation constitutes not the crucial factor of decision.

In case the Norwegian corporation intends to distribute dividends to its shareholders in form of an individual person, the profit is subject to further taxation in Norway. Since the taxable base is basically the same (€ 70.175 and € 69.586), the after tax result of € 56.126 for a permanent establishment and a business partnership are nearly identical to the after tax profit of € 55.702 for a corporation. Thus, a distribution to an individual person does not influence the outcome.

6.2.2. Use of losses

As with an individual person, the choice of the investment alternative in Germany is not of significant importance for a Norwegian corporation in regard to the use of losses. The losses of a permanent establishment, a business partnership and a corporation on company level can be deducted according to the German regulations of the corporate and municipal trade tax (see 5.1.2.1). Based on the symmetry thesis, the Norwegian tax authorities do not allow a tax deduction of losses that are generated in Germany. However, as mentioned before, European Community law requires the possibility to offset losses in certain situations.

On the shareholder level of a corporation, a capital loss can, neither in Germany nor in Norway, be deducted from other profits. Since the deduction of capital losses is in principal dependent on the taxation of capital gains, the next paragraph about the termination of engagement will present the issue in greater detail.

6.2.3. Termination of engagement

In case a Norwegian corporation intends to establish a business in Germany in order to generate a capital gain through the sequential disposal of its operations, the investment alternative of a corporation leads to zero taxation on the level of the Norwegian company and is thus superior to other forms of investment. As previously, the following paragraph explains which circumstances lead to this statement:

A possible capital gain from the disposal or liquidation of a permanent establishment or business partnership leads to a corporation and municipal trade tax liability in Germany. Also the DTA GerNo is allocating the taxation right to Germany. If the German business operates in form of a corporation, we have to distinguish between company and shareholder level as well as between disposal and liquidation. On a company level, Germany is only taxing the hidden reserves in case of liquidation while a disposal of shares does not lead to any taxation at all. On a shareholder level, German national legislation establishes a tax liability for capital gains from disposal as well as liquidation. However, the DTA GerNo is allocating the taxation right to Norway and Germany exempts capital gains from taxation. Even though Norway has a taxation right according to the DTA GerNo, its national legislation does not include the taxation of capital gains if the Norwegian shareholder is a corporation itself. As a consequence, a capital gain from the disposals of shares in a German corporation is not subject to any taxation as long as the profit is not distributed by the Norwegian corporation.

Following table is illustrating the taxation of capital gains under the same general assumptions as stated in paragraph 6.1.3:

Table 8: Taxation of capital gains of a corporation

	Permanent establishment / Business partnership		Corporation	
Disposal	Capital gain (1) German taxation After tax capital gain	€ 100 € - 29.825 € 70.175	Capital gain German taxation After tax capital gain company level Norwegian taxation After tax capital gain shareholder level	€ 100 - € 100 - € 100
Liquidation	Capital gain (1) German taxation After tax capital gain	€ 100 € - 29.825 € 70.175	Capital gain (1) German taxation After tax capital gain company level Norwegian taxation After tax capital gain shareholder level	€ 100 € - 29.825 € 70.175 - € 70.175

Calculation:

(1) € - 15 (Corporate tax) + € - 0,825 (Solidarity surcharge) + € - 14 (Municipal trade tax)

Source: Own table and calculations.

When comparing the after tax capital gain of the different investment alternatives, we can see that the disposal and the liquidation of a permanent establishment as well as a business partnership results in the same amount of € 70.175. This is also the case for the liquidation of a corporation, leading to the same after tax value. In contrast to this, the disposal of shares of a corporation causes, at these levels, no taxation at all and results thus in the highest 'after tax' capital gain of € 100. As a consequence, the investment alternative of a corporation is the best possible choice for a Norwegian corporation that intents to establish a business in Germany in order to generate a capital gain through a sequential disposal.

6.2.4. Excursus: Aspects other than taxation

Even though aspects other than taxation are not the focus of this thesis, it is closely related to the topic and should be taken into account when choosing an appropriate investment alternative for a German business operation. Thus, following excursus is providing a short overview about some factors that could influence the decision between the different types of investment.

The founding and operating of a corporation is, in comparison to a permanent establishment, considerably more complex. A corporation is subject to certain disclosure requirements and the establishment requires a considerable amount of seed capital.[144] Especially if the timeframe of the investment is limited, these points have to be carefully evaluated in regard to the benefits of an investment alternative in form of a corporation. One aspect that can constitute a significant advantage is the limited liability of a corporation's shareholders. In case the German business venture contains a fair chance of failure and if this unsuccessful attempt is likely to imply large liabilities, a separate legal entity with a strict separation between personal and business assets provides an important security for the Norwegian investor. In other words, a personal liability as implied by a permanent establishment might be very much undesirable if the Norwegian company is involved in 'risky businesses'. In addition, a market presence with a German legal form might be beneficial in order to acquire customers or recruit business partners in Germany. The reason for that is that people tend to be more confident to do business with national and thus familiar business entities. The other way around, an unknown legal form of a foreign country might have a deterrent effect on a German customer or business.

In the end it should, however, be noticed that the valuation of the aspects other than taxation has to be conducted in consideration of the individual characteristics of the business venture and a general recommendation cannot be provided.

[144] Höhn/ Höring, 2010, p. 94.

7. Summary and Conclusion

In the initial part of this master thesis, the personal income, corporate and municipal trade tax are identified as the most relevant types of taxation in order to address the topic. With focus on the bilateral agreement between Germany and Norway, special attention is given to the relevant DTA income categories of business profits, dividends and capital gains. After equipping the reader with this fundamental knowledge, the thesis defines significant tax aspects of investment decisions. In this respect, current taxation, use of losses and termination of engagement are considered as the most important factors. The investigation of the various legal forms arrives at the conclusion that a Norwegian company can operate in Germany through a permanent establishment, a business partnership or a corporation.

The main part of the thesis is conducting a detailed analysis by examining the different investment alternatives according to the previously determined frame of references. The results display significant differences as well as extensive overlaps in the taxation of these alternatives. Especially the investment alternatives of a permanent establishment and a business partnership deliver more or less the same results. In contrast to this, a corporation shows major differences in regard to taxation. Furthermore, it can be observed that also the legal form of the Norwegian parent company can influence the tax outcomes in a considerable way.

A tabulated summary of the main points constitutes the base for the evaluation which points out the main differences in taxation and gives recommendations for certain situations. In this regard, the author distinguishes between the parent company in form of an individual person and a corporation and reaches following conclusions:

In case a Norwegian individual person is planning a long-term investment in Germany and expects positive returns which shall be reinvested in Germany, a subsidiary in form of a corporation has advantages in regard to current taxation. However, if the main objective is to repatriate the profit instead of reinvesting it, an alternative without the foundation of a corporation might be the better choice for some companies. In regard to the use of losses, the choice of the investment alternative has neither in Germany nor in Norway a significant effect. Yet, in the special case that the individual person is expecting the liquidation of its operations in Germany after a certain period of time, the legal form of a corporation provides the possibility to offset capital losses in Norway. It can also be recognized that a

Norwegian company with the main intention to generate a capital gain through later disposal of the German business can achieve a tax benefit by choosing the legal form of a corporation.

In case a Norwegian company is a corporation and expects positive returns from its operations in Germany, the choice of the investment alternative has neither a significant effect on current taxation nor on the use of losses. This applies regardless whether the profit is reinvested in Germany or repatriated to Norway. In regard to the termination of engagement, if a Norwegian corporation intends to establish a business in Germany in order to generate a capital gain through the sequential disposal of its operations, the investment alternative of a corporation leads to zero taxation on the level of the Norwegian company and is thus superior to other forms of investment.

Even though the choice of the investment alternative can have a major effect on the tax burden of a business, the decision should also include aspects other than taxation. In many cases, the differences in the tax burden and thus the differences in the after tax profits might be marginal or even zero between the investment alternatives. In such a case, characteristics as liability, seed capital, organisational structure as well as disclosure requirements and auditing duties should be taken into account. All these aspects, as well as tax considerations should be included in the analysis and appropriate to the intended business operation.

A basic understanding of the German tax system is essential when planning to enter the German market. Such knowledge can be gathered by reading relevant literature or information provided by the authorities. However, due to the great complexity of the topic, the author advises firms to seek professional counselling in order to make optimal decisions regarding the most appropriate investment alternative.

At the end of this thesis, the author would like to finish with a recommendation for the Norwegian tax authorities. Even though the symmetry thesis is commonly applied and generally approved by the ECJ, there are certain situations when a denial of a loss deduction in Norway is contradictory to EEA law. Thus, the Norwegian tax legislation should include the possibility to offset these kinds of losses as an ultimo ratio. In this way, multinational active Norwegian companies would enjoy an increased level of legal certainty.

Appendix

Appendix A: Term definition

English	German
Sources of income	
Income from agriculture and forestry	Einkünfte aus Land- und Forstwirtschaft
Income from capital investment	Einkünfte aus Kapitalvermögen
Income from employment	Einkünfte aus nichtselbständiger Arbeit
Income from independent personal services	Einkünfte aus selbständiger Arbeit
Income from rentals and leases	Einkünfte aus Vermietung und Verpachtung
Income from trade and business	Einkünfte aus Gewerbebetrieb
Other income from incidental activities	Sonstige Einkünfte
Types of taxes	
Corporate tax	Körperschaftsteuer
Income tax	Ertragsteuer
Municipal trade tax	Gewerbesteuer
Personal income tax	Einkommensteuer
Solidarity surcharge	Solidaritätszuschlag
Value added tax	Umsatzsteuer
Withholding tax on capital investment	Kapitalertragsteuer
Legislation	
Code of commercial law	Handelsgesetzbuch
Corporate tax act	Körperschaftsteuergesetz
Fiscal code	Abgabenordnung
Foreign transaction tax act	Außensteuergesetz
Income tax act	Einkommensteuergesetz
Municipal trade tax act	Gewerbesteuergesetz
Municipal trade tax directives	Gewerbesteuer-Richtlinien
Reorganisation tax act	Umwandlungssteuergesetz
Solidarity surcharge act	Solidaritätszuschlaggesetz
Types of entities	
Branch	Zweigniederlassung
Business partnership	Personengesellschaft
Corporation	Kapitalgesellschaft
General partnership	Offene Handelsgesellschaft
Limited company	Aktiengesellschaft/Gesellschaft mit beschränkter Haftung
Limited partnership	Kommanditgesellschaft
Permanent establishment	Betriebstätte
Private limited company	Gesellschaft mit beschränkter Haftung
Public limited company	Aktiengesellschaft
Subsidiary	Tochtergesellschaft

General terms

Alienation	Veräußerung
Articles of association	Satzung
Balancing of losses	Verlustausgleich (in einer Periode)
Basic federal rate	Steuermesszahl
Business assets	Betriebsvermögen
Co-entrepreneur	Mitunternehmer
Dealing-at-arm’s-length	Fremdvergleich
Domicile	Wohnsitz
Fictive independence	Wirtschaftliche Selbständigkeitsfiktion
Flat rate withholding tax	Abgeltungssteuer
General partner	Gesellschafter
Habitual abode	Gewöhnlicher Aufenthalt
Individual person	Natürliche Person
Initial tax rate	Eingangssteuersatz
Intercorporate privilege	Schachtelprivileg
Interest advantage	Zinsvorteil
Interest disadvantage	Zinsnachteil
Legal entity / person	Juristische Person
Limited partner	Kommanditist
Limited tax liability	Beschränkte Steuerpflicht
Liquidation	Aufhebung
Liquidity advantage	Liquiditätsvorteil
Liquidity disadvantage	Liquiditätsnachteil
Loss carry back	Verlustrücktrag
Loss carry forward	Verlustvortrag
Loss deduction	Verlustabzug (zwischen Perioden)
Management board	Vorstand
Marginal tax burden	Grenzbelastung
Minimum taxation	Mindestbesteuerung
Net principle	Nettoprinzip
Non-business expenses	Sonderausgaben
Parent company	Stammhaus / Muttergesellschaft
Partial income method	Teileinkünfteverfahren
Partnership agreement	Gesellschaftsvertrag
Permanent representative	Ständiger Vertreter
Personal assets	Privatvermögen
Place of management	Geschäftsleitung
Preferential tax treatment for retained profits	Thesaurierungsbegünstigung
Progression clause	Progressionsvorbehalt
Proportional zone	Proportionalzone
Registered office	Unternehmenssitz (Handelsregistereintrag)
Separation principle	Trennungsprinzip
Shareholders’ meeting	Hauptversammlung
Sole proprietor	Einzelkaufmann
Supervisory board	Aufsichtsrat
Symmetry thesis	Symmetriethese

Tax allowance	Steuerfreibetrag
Tax amendment act	Jahressteuergesetz
Taxable base	Bemessungsgrundlage
Taxable income	Zu versteuerndes Einkommen
Termination	Auflösung
Territorial principle	Territorialprinzip
Total income	Summe der Einkünfte
Trading profits	Gewerbeertrag
Transfer of functions	Funktionsverlagerung
Transparency principle	Transparenzprinzip
Unlimited tax liability	Unbegrenzte Steuerpflicht
World income principle	Welteinkommensprinzip

Appendix B: Calculation of the reinvested profit after German taxation

X = Reinvested profit after German taxation

$X = € 100 - (X \cdot 0.2825 \cdot 1.055) - (€ 100 - X) \cdot 0.45 \cdot 1.055 - € 14 + € 13.3$

$X = € 62.94884837 \approx 62.949$

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