

- a* to the extent that different conditions would apply for the deduction of interest paid to residents and non-residents and it will therefore be important to determine, for purposes of that paragraph, whether the application of the rule is compatible with the provisions of paragraph 1 of Article 9 or paragraph 6 of Article 11 (see paragraph 74 above). This would also be important for purposes of paragraph 5 in the case of thin capitalisation rules that would apply only to enterprises of a Contracting State the capital of which is wholly or partly owned or controlled, directly or indirectly, by non-residents. Indeed, since the provisions of paragraph 1 of Article 9 or paragraph 6 of Article 11 form part of the context in which paragraph 5 must be read (as required by Article 31 of the *Vienna Convention on the Law of Treaties*), adjustments which are compatible with these provisions could not be considered to violate the provisions of paragraph 5.'
- d* The last part of this passage would permit the disallowance of interest which exceeded an arm's length amount. However, art 24(4) of the Germany-US treaty (and art 24(5) of the OECD Model) makes no reference to arm's length amounts. The Bundesfinanzhof declined to give effect to this change to the Commentary, on grounds that it reflected only the views of tax authorities and not the subsequent practice of the contracting states to the relevant convention.
- e*

COMMENTARY

- f* The case is closely related to the decision of the German Federal Fiscal Court (Bundesfinanzhof) of 8 September 2010 (case no I R 6/09) which was printed in (2010) 13 ITLR 646.
- Under the German thin capitalisation rules which were in force until 2000 (or 2001 if the taxpayer's financial year deviated from the calendar year), interest payments made by a German corporation were re-qualified into non-deductible constructive dividends for tax purposes if among other conditions the payment was made in respect of a borrowing granted by a shareholder with a minimum interest of at least 25% of the share capital but without entitlement to a tax credit under the so-called 'imputation system'. This system was applicable at the time in order to avoid double taxation when a German corporation distributed profits to its shareholders. It implied that the shareholder would obtain a credit for the corporate income tax paid by the corporation on the distributed profits.
- g*
- h*
- i* The most important category of cases where the credit was not granted to the shareholder were cases in which the shareholder was not subject to a tax assessment in Germany, ie cases with a non-resident shareholder.
- To prevent circumventions of the rule interest would also be re-qualified as a constructive dividend if it was paid on a borrowing from a related

party of the shareholder with no entitlement to a tax credit or from a third party having recourse to the shareholder or the related party. a

In contrast to decision no I R 6/09, the case at hand involves a borrowing not from the shareholder itself but from a related party to the shareholder, precisely from an Irish sister company which was also a 100% subsidiary of the US parent. The German tax authorities argued that in such constellation no violation of the ownership non-discrimination rule (art 24(4) of the US-German treaty which corresponds to art 24(5) of the OECD Model Convention) was present because it was sufficient for the German rule to apply that the lender was not entitled to a corporate income tax credit and the lender was obviously not the shareholder. This view had even been expressed in a circular by the Federal Ministry of Finance dated 15 December 1994. The Federal Fiscal Court does not share it, though, and has now clearly stated that the wording of sec 8a of the Corporate Income Tax Act which was valid until 2000 also required a shareholder that was not entitled to a corporate income tax credit (even if it was not the lender). The court took the opportunity to clarify that the amended version of sec 8a which generally took effect on 1 January 2001 did not require a foreign owner and therefore did not infringe art 24(5) of the OECD Model. The court's decision of 8 September 2010 had left some doubts in this respect (see my note in (2010) 13 ITLR 646 as well as Avery Jones et al., (2011) World Tax Journal 179, at 202). Yet, the amended version was not applicable in the case at hand, although the facts partly related to 2001, because the taxpayer's financial year deviated from the calendar year which made the old rule applicable. b
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The Federal Fiscal Court adhered to its reasoning already formulated in the 2010 decision with regard to the Swiss-German treaty according to which the requirement of sec 8a Corporate Income Tax Act that the shareholder be not entitled to a corporate income tax credit is a direct discrimination which is prohibited by art 24(5) of the OECD Model (see also Rust in *Klaus Vogel on Double Taxation Conventions*, 4th edn, art 24, notes 109 and 110). g

The court rejected the argument of the tax office that art 24(3) of the US-German treaty (art 24(4) OECD Model) prevails over art 24(4) as *lex specialis* in respect of the types of payments which it explicitly mentions, ie interest, royalties and other disbursements paid by an enterprise of a contracting state to a resident of the other contracting state. Two main reasons speak against the priority of art 24(3) in the present case. First, the conditions of art 24(3) are not fulfilled since the interest payments were not made to a US resident, but to an Irish resident (sister company of the payor). Secondly, both rules have a different scope. Article 24(3) prohibits a discriminatory tax treatment of payments made to any resident of the other contracting state, not necessarily the h
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a shareholder. Article 24(4) prohibits discriminatory tax treatment which is linked to the residence of the shareholder in the other contracting state. Therefore, both treaty clauses need to be applied side by side.

b It was unnecessary for the court to investigate whether the requalification of interest into a constructive dividend could be justified by the arm's length principle because the judges held that art 24(4) of the USA DTC 1989 could not be construed as to include a reservation in favour of art 9(1) and art 11(4) such as art 24(3) USA DTC 1989 did. The Federal Fiscal Court moreover refused to give authority to no 79 of the OECD Model Commentary as amended in 2008 because the treaty had already
c been concluded 20 years earlier and the Commentary also did not reflect the practice of the contracting states in the sense of art 31 of the Vienna Convention on the Law of Treaties. It merely revealed the opinion of fiscal authorities represented in the OECD. This so-called 'static interpretation'
d of tax treaties is consistent jurisprudence of the German court.

Juergen Luedicke

16 January 2014. The following judgment was delivered.

e **JUDGMENT**

LEITSÄTZE

f [1] Gewährt eine nicht zur Anrechnung von Körperschaftsteuer berechnete (ausländische) Kapitalgesellschaft ihrer unbeschränkt steuerpflichtigen (inländischen) Schwester-Kapitalgesellschaft ein Darlehen, werden die dafür gezahlten Zinsen nur dann nach § 8a Abs. 1 Satz 1 Nr. 2 i.V.m. Satz 2 KStG 1999 a.F. in verdeckte Gewinnausschüttungen umqualifiziert, wenn auch die (gemeinsame) Muttergesellschaft nicht zur
g Anrechnung von Körperschaftsteuer berechnete ist (Klarstellung des Senatsurteils vom 8. September 2010 I R 6/09, BFHE 231, 75, BStBl II 2013, 186; entgegen BMF-Schreiben vom 15. Dezember 1994, BStBl I 1995, 25 Tz 19).

h [2] § 8a Abs. 1 Satz 1 Nr. 2 i.V.m. Satz 2 KStG 1999 a.F. ist nicht mit dem Diskriminierungsverbot des Art. 24 Abs. 4 DBA- USA 1989 vereinbar (Anschluss an Senatsurteil vom 8. September 2010 I R 6/09, BFHE 231, 75, BStBl II 2013, 186).

TATBESTAND

i I. Die Geschäftsanteile der am 6. April 2000 errichteten Klägerin und Revisionsklägerin (Klägerin), einer GmbH mit abweichendem Wirtschaftsjahr zum 30. September, wurden vom 11. Mai 2000 bis zum 30. September 2001, den beiden Streitjahren, von einer US-amerikanischen Kapitalgesellschaft (A-LLC) gehalten. Die letztere hielt in jenen Jahren