

## "Making things easy for repentant tax evaders" What is it all about??

Sebastian Korts, MBA, attorney at law, certified attorney at tax law

Petra Korts, MBA, attorney at law, certified attorney at tax law

([www.korts.de](http://www.korts.de))

In all probability, for the first time in the history of the Federal Republic of Germany there will be an amnesty for tax offenders regarding all types of income. The ministerial draft bill which is meanwhile available is at present being completed with some more items by the federal ministry of finance; however, a change to the core provisions is unlikely so that these can be presented here even now.

### A. Previous law

Up to now repentant tax evaders had only the possibility of reporting themselves to the tax office, thus going unpunished. This self-accusation, however, eliminates only the possible criminal consequences in relation to tax offences. With regard to the fiscal consequences there are no special arrangements. This means that all existing fiscal provisions are applicable without exception.

Here is a (simplifying) example as an illustration:

A building contractor has made EUR 2.3 m a year between 1992 and 2002 by employing illicit workers. In order to achieve this result he has had expenses of EUR 1.3 m. These expenses include EUR 300,000 in (below-standard) wages and EUR 1 m in material costs. However, the material costs have come under operating expenditure of his existing business. The profit of EUR 1 m has been transferred to Switzerland and administered there, whereas the building contractor has spent all the revenue from the administration privately.

In case of a self-accusation exempting him from punishment he has to pay tax on the total profit (EUR 10 m) with his personal tax rate (current maximum tax rate: 48.5%). In addition, he has to pay 6% interest on tax evasion a year. Furthermore, the tax office will expect him to pay 16% value-added tax. In conclusion he has to pay the entire ancillary wage costs and social security contributions of the employees extra, that means both the employer's and employee's contribution along with the income tax (an estimated 70% of the total wages) for as an employer he is liable for the payment of the ancillary wage costs and social security contributions. It has to be taken into account that in cases like these the authorities can take the standard minimum wage as a basis for assessment and not the wage actually paid to the employees.

Referring to this case this yields the following (very simplified) calculation:

EUR 600,000 as the (standard) basis for assessment results in the following annual tax:

EUR 485,000 income tax

EUR 368,000 turnover tax

EUR 51,180 interest on tax evasion

(on income tax and turnover tax)

EUR 420,000 ancillary wage costs and

social security contributions

EUR 1,324,180

To put it simply, the entrepreneur thus pays 133% taxes on his profit. Seen over period of ten years, he would pay an estimated 150%, i.e. EUR 15 m, due to the current interest. Those reporting themselves to the tax office will go unpunished.

### B. New amnesty arrangement

In order to benefit from the new amnesty arrangement tax evaders must completely report their income withheld in the years 1992 to 2002 to the tax office and pay extra tax within five days.

The tax evaders must work out the tax themselves. In the case of this subsequent declaration and payment the applicable tax rate is only 25% for a short time. With the payment of this lump sum

all tax claims of the state are met. Inheritance, property or turnover tax are just as settled as possibly existing obligations to pay extra social security contributions.

Thus the law is (almost) perfect with regard to fiscal matters but from a criminal point of view it still has some loopholes. In the above-mentioned example the entrepreneur has not only committed tax evasion but has also violated various other (penal) laws. One just has to think of the act on illegal employment, the regulation on working hours or the section on money laundering - and the failure to pay social security contributions is of course also a criminal offence. According to the current bill the entrepreneur would only go unpunished regarding the tax evasion, whereas the other criminal offences would not be covered by the amnesty.

Meanwhile even the federal ministry of finance has realized that the amnesty regulation would be to no avail if a tax dodger had to expect prosecution because of these "collateral offences" due to his statements in the amnesty declaration. Therefore bans on utilization will be incorporated in the law. This means that the fiscal facts disclosed by the tax evader must not be used for the criminal prosecution of non-fiscal offences. The concrete wording of these provisions is currently still kept secret so that a more detailed explanation is not possible.

In terms of figures the amnesty arrangement, referring to the example above, results in the fact that altogether the entrepreneur has to pay only 25% of his total income of EUR 23 m. Compared to the total loss and an extra payment of property shares which have not been earned at all in the case of a self-accusation, the entrepreneur pays EUR 5.75 m and thus keeps EUR 17.25 m. This amount of money can remain abroad. All tax claims and claims to social security contributions are met once and for all.

### C. Special provisions

The bill for the amnesty still does not lay down how to deal with income which a partner of a corporation has obtained from the latter without good reason. If the partner now declares this income, this could have negative effects on the corporation's corporate tax. However, as it could be heard from the federal ministry of finance an amendment to the bill is being prepared which is to avoid this consequence.

With foreign circumstances certain peculiarities have also to be taken into account. For instance, it was very popular with German taxpayers to transfer their withheld property to Liechtenstein institutions held in trust - often through the agency of Swiss banks. In our experience such transfers are as a rule considered taxable donations by the tax offices. Therefore the taxpayer must not forget to state also these facts in their declaration. This transaction would then be settled with the payment of the 25% or 35% tax. However, it must be taken into account that the transfer back of the property from the institution to the taxpayer may also be a donation. If this transfer back takes place after the declaration has been made, this would not be covered by the settlement effect of the amnesty. The transaction would have to be reported separately to the tax office and tax would have to be paid on it separately.

The tax evaders don't have to add any proof to the declaration and the tax office does not check their statements either. However, if the tax office discovers an unclear income at a later time, the taxpayer must prove that this income has been taken into account in the amnesty declaration; that means that the settlement effect of the 25% lump-sum taxation also covers this income.

This is the obligation of the person making the subsequent declaration. If the citizen cannot prove it, the tax office will assume undeclared income and thus a tax evasion - and then it is even too late for a self-accusation!

Specialized lawyers give advice both on the self-accusation and on the way "things are made easy for repentant tax evaders".