

DOING BUSINESS

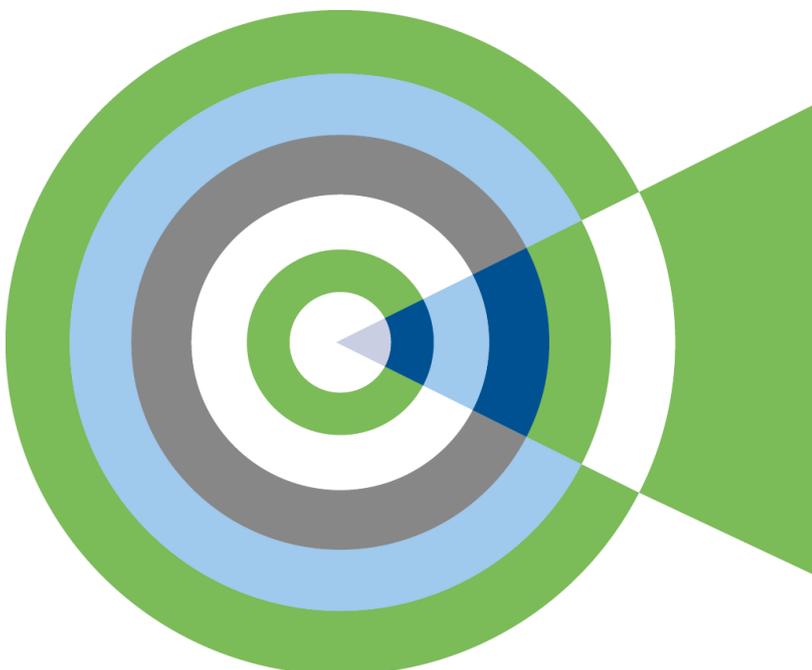
IN GERMANY



The network
for doing
business

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1 – INTRODUCTION

UHY is an international organisation providing accountancy, business management and consultancy services through financial business centres in over 80 countries throughout the world.

Business partners work together through the network to conduct transnational operations for clients as well as offering specialist knowledge and experience within their own national borders. Global specialists in various industry and market sectors are also available for consultation.

This detailed report providing key issues and information for investors considering business operations in Germany has been provided by the office of UHY representatives. A detailed firm profile for UHY's representation in Germany can be found in section 8. You are welcome to contact individual firms for any inquiries you may have.

Information in the following pages has been updated so that they are effective at the date shown, but inevitably they are both general and subject to change and should be used for guidance only. For specific matters, investors are strongly advised to obtain further information and take professional advice before making any decisions. This publication is current at August 2013.

We look forward to helping you do business in Germany.

2 – BUSINESS ENVIRONMENT

GEOGRAPHY AND CLIMATE

Germany is located in the centre of Europe and is one of the largest European countries.

Neighbouring countries are Poland, the Czech Republic, Austria, Switzerland, France, Luxembourg, Belgium, the Netherlands and Denmark.

The capital of Germany is Berlin. However, the main business centres are Hamburg, North-Rhine Westphalia (Cologne, Düsseldorf), Frankfurt, Stuttgart and Munich. International airports are located in all of these cities. Germany also has access to the North Sea and the Baltic Sea. The port of Hamburg is one of the largest container transshipment centres in Europe.

Germany belongs to the temperate climate zone of Central Europe, where the climate is mild. In general, summers are not too hot and in winter, temperatures are around freezing with rare snowfalls. The average annual rainfall is 700mm; the average annual temperature is 10°C.

CONSTITUTION AND GOVERNMENT

Germany is a parliamentary democracy with a pronounced federal structure.

Legislative and executive powers are divided between the federation and the 16 federal states, namely Baden-Württemberg, Bavaria, Saarland, Rhineland-Palatinate, Hessen, Thuringia, Saxony, Saxony-Anhalt, North-Rhine Westphalia, Lower Saxony, Berlin, Brandenburg, Bremen, Hamburg, Schleswig-Holstein and Mecklenburg-Vorpommern. The federal parliament has responsibility for national matters such as international affairs, defence and economic policy and taxation. The legislatures of the 16 federal states are responsible for issues such as education and property.

At the federal level, the most important legislative institutions are the *Bundestag* (federal parliament) and the *Bundesrat* (the upper house representing the federal states). Whilst the power of the German president is limited to representation, the position of the chancellor is fairly pronounced.

The country's constitution is based on the Basic Law passed in 1949. Upon reunification in 1990, its applicability was extended to the states of the ex-German Democratic Republic (GDR).

German legislation is modelled on the old Roman system and has no resemblance to the Anglo-Saxon legal system.

DOMESTIC MARKET

POPULATION, SIZE AND LANGUAGE

Population	81.8 million inhabitants
Land area	357,112 square kilometres, measuring 885 kilometres from north to south and 595 kilometres east to west
Population density	229 inhabitants per square kilometre

Currency	Euro (EUR)
Official language	German

ECONOMY

Germany is a founding member of the European Union.

Germany is also part of the United Nations, the OECD, NATO, the G8 and G20, and the European Monetary Union (EMU).

Based on its nominal gross domestic product (GDP), Germany is the third largest political economy and the second largest export nation. German GDP was EUR 2,570.8 billion in 2011.

In 2011, the service sector accounted for 73.8% of total employment compared with 1.6% in agriculture and 24.6% in industrial production.

Unemployment figures vary year to year. The average rate of unemployment during 2011 was 7.1%. (This compares with rates of 7.7% in 2010, 8.1% 2009, 7.8% 2008, 9.0% 2007, 10.8% 2006 and 11.7% 2005). In August 2012, the rate of unemployment was 6.8%.

The annual average inflation rate was around 2.3% in 2011. In August 2012 this index was 2%. (This compares with rates of 1.14% in 2010, 0.4% 2009, 2.6% 2008, 2.2% 2007, 1.7% 2006 and 2.0% 2005).

The German economic model aspires to be a functioning social market economy, in which free market economics are blended with solidarity and social compromise.

PRICES AND INTEREST RATES

Since Germany is part of the EMU, monetary policy is managed by the European System of Central Banks. The European Central Bank (ECB), based in Frankfurt, is the common monetary authority of all member states of the EMU and is one of the organisations responsible for the supervision of the banking system and the regulation of the money supply. Its two biggest aims are the stability of the price level and to ensure steady economic development. One of the instruments to pursue these aims is the regulation of the price for lent money with prime interest rates.

Prime interest rates influence the business between the ECB and other banks and the exchange rate of the Euro against other currencies. Since 1 January 2012, the basic interest rate has been approximately 0.12%.

FOREIGN TRADE AND BALANCE OF PAYMENTS

Germany is one of the world's most active trading countries with a significant surplus. In 2011, the volume of exports was EUR 1,060.1 billion, while the volume of imports amounted to EUR 902 billion. The foreign trade balance in 2011 reached a surplus of EUR 158.1 billion. In 2010, the surplus amounted to EUR 154.9 billion.

More than 50% of exports of German goods are delivered to European countries. Germany's highest trade surplus resulted in 2011 from its trade with France (total exports EUR 101.51 billion). Other important trade partners are the United States (EUR 73.69 billion in 2011), the Netherlands (EUR 69.32 billion), the United Kingdom (EUR 65.5 billion), China (EUR 64.76 billion) and Italy (EUR 62.0 billion).

42.4% of Germany's main exported goods are manufactured products – machinery, automobiles and car parts, and chemical products. One in four jobs in German industry depends on exports.

German industry has increased its competitiveness considerably in recent years and has maintained and expanded its leading market position in the domestic, European and international markets.

THE FINANCIAL AND BANKING SYSTEM

The German banking system and the German financial services industry are stable and well-developed. Frankfurt is the financial centre of Germany. It is the seat of the ECB and the most important stock exchange of the country and the Eurex (the German futures and options exchange).

The German financial system consists of the following:

- Banks
- Insurance companies
- Investment companies
- Operators of stock exchanges and equity markets
- Operators of payment systems
- Central banks
- Trade markets.

The aim of a financial system is to allocate deposits and transform money into loans, making it available for investments. This ensures a significant input to German economic growth.

All available banking transactions and financing options are carried out in Germany. Many forms of debt financing are possible. Short-term arrangements include bank loans, trade credit from suppliers, commercial and financial contracts, factoring of receivables, etc.

Forms of long-term financing include open-market borrowings (bonds, notes, etc) and direct borrowings (mortgages and term loans) from financial institutions. Leasing arrangements represent a further option for long-term financing.

The capital market in Germany has grown in importance over recent years. As a consequence, all major new capital instruments of financing or risk hedging, such as derivatives and swaps, are available to investors.

In addition, the following banking transactions can be carried out:

- Deposits
- Discount business
- Portfolio & investment management

- Guarantee business
- Giro business (cashless payments and clearings)
- Electronic banking.

Banking transactions in Germany are facilitated by an extensive branch network of German banks and credit institutions, as well as extensive international linkages and a sophisticated technical infrastructure.

The German banking industry is national, and is dominated by several large banks. All German banks are federally chartered. The German banking system is characterised by 'universal' banks on one hand and 'niche' players on the other.

Universal banks offer a full range of banking and financial services. These are dominated by internationally known names. The advantage of the universal bank system is that companies can establish long-term relationships with their respective bank, thereby avoiding the short-term view present in the Anglo-Saxon financial markets system. 'Niche' players are smaller financial institutions that have succeeded in offering specialised services.

The German financial institutions system comprises all major forms of enterprise such as private credit institutions, savings banks, co-operative credit institutions, security houses, mortgage houses, trust companies and credit unions. Their responsibilities range from capital and credit for private persons and commercial enterprises, provision of payment solutions to wide-ranging possibilities for the investment of assets.

Foreign banks are permitted to establish German subsidiary operations. They tend to have only a few branches and focus on the business market, rather than providing full-service banking. EU legislation on bank licences has been fully implemented in Germany.

WORKING AND LIVING CONDITIONS

VISA/RESIDENCE TITLE/WORK PERMIT

Generally speaking, all foreigners who are non-EU and non-European Economic Area (EEA) nationals require a visa/a residence title for stays in Germany. Nationals from EU and EEA member states and citizens of Switzerland do not need a visa/a residence title to enter or to reside in Germany. After arrival, they only need to register with the appropriate authority of their residence in Germany.

A short-term visa (the so-called 'Schengen' visa) is sufficient for a stay up to 90 days. For several types of foreigner, a visa is not required for a stay up to three months within a six months period, provided they do not take up gainful employment requiring a work permit in Germany (for example, this applies to nationals of Australia, Canada, Israel, Japan, New Zealand, South Korea and the United States etc). However, such foreigners can only enter Germany if they have valid identity papers. On the planned date of departure from Germany, these papers should have at least three months validity.

For stays of more than three months or if a foreigner intends to take up employment, a national visa and/or a work permit is required. In principle, nationals from the EU and EEA member states and citizens of Switzerland do not require a work permit. However, for some new member states of the EU (countries which acceded to the EU on 1 May 2004 and 1 January 2007) other regulations are applicable during a transitional period. All foreigners from outside the EU and outside the EEA require a work permit in addition to a residence permit if they want to take up gainful employment. This work permit is required before entering Germany. Nationals of Australia, Canada, Israel, Japan, New Zealand, South Korea and the United States may apply for the permit after arrival in Germany.

Under German law, consulates and embassies issue visas of the Federal Republic of Germany. Visas are issued by the mission responsible for the country/area in which the applicant has his/her ordinary residence or domicile. For work permits, the authority in the place where the activity in Germany is to be commenced, has to grant its approval. The Federal Employment Office must also approve the issuance of the visa if the foreigner intends to take up gainful employment.

COST OF LIVING AND HOUSING

The standard of living is high in Germany but costs of living vary broadly and depend mainly on the general cost of living and the place of residence. Munich, for example, is one of the most expensive cities in Germany.

The average costs for housing vary between EUR 7.50–12.50/m² (a base rent per month). The average cost for office space in big cities varies between EUR 15–30/m² for downtown locations and EUR 10–20/m² for suburban areas.

3 – FOREIGN INVESTMENT

There are no substantial restrictions on foreign investment in Germany. Foreign investors are generally subject to the same conditions as German investors.

There are no permanent currency or administrative controls. However, certain investments may involve official registration and permit regulations, which may entail considerable bureaucracy. For example, special licences are required for risky business practices like insurance, commercial banking, brokers and agents, and there are special business permits with regards to environmental regulation pursuant to the Federal Pollution Control Act (*Bundesimmissionsschutzgesetz*). Furthermore, detailed registration regulations at the local administration and tax authorities have to be followed.

Germany is seen by foreign investors as a good location for manufacturing, research and development and establishing a company headquarters. Even during the crisis year of 2009, Germany maintained its international reputation as an investment destination. Germany ranks in sixth place as one of the world's most attractive investment locations (behind China, India, the United States, Russia and Brazil).

The services sector in particular recorded strong interest among investors. The sectors of renewable energies, mechanics and electronics, chemicals and health were particularly seen as attractive. Germany is seen by international investors as reliable and competitive; this applies to its full range of high technologies and services.

Investing companies are mainly from Europe, Asia and North America, but there has been a notable shift of interest towards investors from Asia, especially Indian and Chinese companies. Also noticeable is the interest of Israeli and Turkish companies in Germany, especially the high technology sector, such as medical technology, the health care industry and nanotechnology. In the consumer goods sector, mainly in the textiles and home ware products area, Turkish companies have intensified their commitments.

TEN REASONS FOR INVESTING IN GERMANY

LARGE MARKET

With 82 million inhabitants, Germany is the EU's most populous country and therefore also its largest market. With a GDP of more than EUR 2.5 trillion, Germany is the largest economy in Europe and the third strongest economy in the world.

CENTRAL LOCATION

Germany's central location in Europe makes it a hub for goods and services. Germany has especially benefited from EU enlargement. As a result, it is the only country among the seven most important industrialised nations to increase its share of world trade since 1995.

OPEN MARKET

Germany is an open market and warmly welcomes foreign investors. This is demonstrated by the 22,000 foreign enterprises that have established businesses in Germany and now employ more than 2.7 million people. The German market is open to entrepreneurial investment in practically all areas. There are no longer any state-controlled industries. Germany is receiving increasing attention from private equity firms and hedge funds due to its attractive companies and favourable investment conditions.

INTERNATIONAL LOCATION

Around 7 million foreigners live in Germany. Several metropolitan regions have prominent foreign communities with their own schools, churches, shops and restaurants. For example, a large number of Japanese people live in the Düsseldorf region, many Koreans live in and around Frankfurt and many Chinese live in Hamburg. Approximately 70% of German blue- and white-collar workers speak English.

QUALIFIED PERSONNEL

Germany offers an exceptionally well-qualified, motivated and conscientious workforce. The high standard of knowledge and skills among German employees is internationally recognised.

HIGH LEVEL OF INNOVATION

Germany has 277 international patents per one million inhabitants – more than anywhere else in the world. The close cooperation between industry and world-famous research institutions like the Max Planck and Fraunhofer Institutes swiftly transforms new ideas into products for the world market.

HIGHLY DEVELOPED INFRASTRUCTURE

Germany has a closely knit network of roads, railways and international airports which guarantees swift connections.

LEGAL SECURITY

Germany is a modern constitutional state with transparent and reasonable laws. These advantages are internationally recognised. Among all countries, Germany ranks fourth in terms of legal security.

STRONG 'MITTELSTAND'

The German economy is characterised by privately owned small and medium-sized firms, known as the *Mittelstand*. 85% of all businesses are small or medium-sized. This makes German industry flexible, multi-faceted and competitive. Many of these highly specialised firms are world market leaders in their field.

WORLD-FAMOUS TRADEMARK

Products with the 'Made in Germany' seal stand for the highest quality worldwide. This has played a significant role in maintaining Germany's position as a world export champion for many years. The automobile, mechanical engineering, electrical engineering and chemical sectors are particularly strong. Industries of the future such as environmentally friendly energy production and nanotechnology, in which the number of patent applications is doubling every two years, are steadily gaining in importance.

4 – SETTING UP A BUSINESS

As a foreign investor there are two avenues available to set up a business in Germany, involving the creation of:

- A legally dependent branch of a foreign company, or
- A legally distinct subsidiary.

For natural persons, a sole proprietorship may be the easiest way to establish a business in Germany.

There are also the following methods for doing business in Germany, by establishing:

- An independent sales agent
- An independent distributor
- A representative office.

BRANCH

All foreign investors are able to open a branch of their existing business abroad (individual entrepreneurs, corporations or partnerships). Part of the process does however require the foreign investor to register the branch of their existing business at the local court and municipality. While such a branch is an unincorporated body, it is entitled to act as a legally binding entity in its own name.

SUBSIDIARY

There are various different structures of subsidiaries open to foreign investors when they decide to set up a business in Germany. The German Commercial and Company Law distinguishes between unincorporated companies and corporations.

In deciding what structure is best, thought should be given to what the liability of the subsidiary structure will be. For example, a corporation is a legal entity and is liable itself, limited to the value of its assets, for any debt. In comparison, in an unincorporated company, a partner is personally liable for any debt.

The following section gives a brief overview of the most common ways to open a subsidiary in Germany.

UNINCORPORATED COMPANIES

GENERAL PARTNERSHIP (*OFFENE HANDELSGESELLSCHAFT – OHG*)

A general partnership may be formed by two or more persons or entities (German or foreign corporations, or partnerships of natural persons).

A general partnership may be created by agreement and must be registered. In a partnership, the partners are personally liable, jointly or severally, for all obligations of the partnership. A general partnership is a legal entity and can acquire rights, create obligations, acquire ownership and have other legal rights (eg the partnership can sue). Fiscally, a partnership is seen as a transparent vehicle. The partners contribute capital and efforts and reap the fruit of their labour as agreed upon in the partnership's agreement. Without a statement to the contrary in the partnership's agreement, all partners are entitled to manage and represent the general partnership.

LIMITED PARTNERSHIP (*KOMMANDITGESELLSCHAFT– KG*)

As with a general partnership, a limited partnership may be formed by two or more persons or entities (German or foreign corporations, or partnerships of natural persons). A limited partnership may be created by agreement and must be registered. In comparison with a general partnership, in a limited partnership there are ‘general’ partners with unlimited liability and also limited partners. A limited partner’s liability is restricted to their contributions to the partnership. This restriction only becomes effective after registration at the local court. Unless otherwise agreed upon, limited partners do not participate in the management and cannot represent the limited partnership.

A GmbH & Co. KG is an example of a limited partnership with a sole general partner being a private limited liability company (*Gesellschaft mit beschränkter Haftung, GmbH*). The main characteristics of a GmbH & Co. KG are:

- Limited liability of the general partner
- The partnership owns the company’s assets
- The partnership runs the actual business under an administration
- There is management and representation of the general partner.

DORMANT PARTNERSHIP (*STILLE GESELLSCHAFT*)

A dormant partnership may be created by a contribution to an already existing enterprise (partnership, company, etc). A dormant partnership is not a legal entity but a financial participation on a contractual basis. Dormant partners do not participate in the management of the enterprise, cannot represent the dormant partnership and the contribution of the dormant partner can simply be seen as an investment. The dormant partner shares in the enterprise’s profits and losses. As a special feature of the dormant partnership, the dormant partner is not discernible externally.

CIVIL LAW ASSOCIATION (*GESELLSCHAFT BÜRGERLICHEN RECHTS – GBR*)

A civil law association may be formed by two or more persons and it is created in agreement by the founders in order to achieve a common purpose. Although a civil law association is not a legal entity, a civil law association itself is legally responsible. Property can be acquired by the association and can be owned by the partners in joint tenancy. Each partner is liable without restriction for the association’s obligations. They also manage and represent the association as a joint venture and all decisions require the consent of every partner.

This form of incorporated company is commonly used by small entrepreneurs, self-employed persons and other short-term projects of larger enterprises or joint ventures (eg large construction projects). A civil law association is not registered.

PROFESSIONAL PARTNERSHIP (*PARTNERSCHAFTGESELLSCHAFT*)

A professional partnership is a company of freelance professionals, for example architects, engineers, consultants, lawyers and auditors. A professional partnership may be established by written agreement of the partners and must be registered. A professional partnership may create rights and obligations, acquire and own property and sue or be sued. However, it is not a legal entity. The partners are jointly and severally liable. In a situation where only a number of partners cause a liability to the partnership due to their misconduct, then only these partners are liable. Partners are entitled to manage and represent the partnership as desired, unless otherwise stated in the partnership agreement.

CORPORATIONS

There are a number of different forms of corporation.

In Germany, unlike unincorporated bodies, a corporation is regarded as a separate legal entity. The shareholder's liability is restricted to the value of their assets. Corporations do not depend on a certain number of shareholders and may be formed by one or more persons including corporations, partnerships or individuals, regardless of their nationality or place of residence.

Establishing a corporation and maintaining it is more expensive than partnerships or proprietorships. Corporations are more heavily regulated by German business and company law and require more review and information.

In Germany, corporations can be traded privately or publicly. In the case of a private corporation, shares may not be sold to the general public. Public corporations are subject to various disclosure and reporting requirements and have to file prospectuses with the relevant securities commission before offering shares to the general public.

STOCK CORPORATION (*AKTIENGESELLSCHAFT*)

In Germany, a stock corporation is one of the two most frequent forms of a corporation. Stock corporations are a popular structure for commercial enterprises with large capital needs. Generally speaking, the major difference between a limited liability company and a stock corporation is that a stock corporation can trade its shares on the stock exchange. A stock corporation may be both quoted on one of the German stock exchanges (eg on the largest one in Frankfurt) or be held as long-term participations without being quoted. A stock corporation may deal out its shares by contracts of sale, whereas for a limited liability company contracts of sale must be notarised.

A stock corporation has a management and supervisory board. A shareholder of a stock corporation may be a member of one of the aforementioned boards but cannot direct the managers on how to conduct the business of the corporation.

As a precondition for its formation, a stock corporation must be registered and present a share capital of EUR 50,000,00.

LIMITED LIABILITY COMPANY (GESELLSCHAFT MIT BESCHRÄNKTER HAFTUNG)

A limited liability company is the other very common type of corporation in Germany. This form of corporation is used by both German medium-sized businesses (these are very often family-owned and owner-managed businesses) and subsidiaries of foreign companies in Germany. The handling of the business and administrative efforts are less formal and complex in comparison with a stock corporation.

Under German law, a limited liability company must register itself with a share capital of at least EUR 25,000. The founding act and the articles of association have to be notarised and the corporation does not exist before completion of registration.

A limited liability company is managed and represented by the managing directors, who are chosen by the shareholders. A shareholder can also be a managing director. A managing director can be directed by a shareholders' resolution.

Under the relevant legislation, a limited liability company's office can be registered in a different locality than the place of its actual business activity. Under German legislation, the limited liability company's existence does not depend on the place of business activity and this may be abroad. However, the limited liability company must have a German postal address.

BUSINESS COMPANY (UNTERNEHMERGESELLSCHAFT, HAFTUNGSBESCHRÄNKT)

A business company is a type of a limited liability company and may be founded under similar conditions. However, in contrast to a limited liability company, the amount of share capital of a business company may be appointed in the articles of association. The minimum amount of share capital is EUR 1.

Due to the limited liability and the small amount of share capital, a business company does not have good credit.

REAL ESTATE INVESTMENT TRUST

Effective from 1 January 2007, Germany introduced the Real Estate Investment Trust (REIT) which is a tax-exempt legal entity. Under German law, a REIT is a listed stock corporation and must meet the following conditions:

- It must have a German-registered office and place of business
- Shares must be registered for trading on a public exchange in a member state of the EU or EEA
- The free float (volume of shares traded on the stock exchange) at the time of listing must be at least 25%
- Its real estate assets account for at least 75% of its gross assets
- Rental income from real estate accounts for at least 75% of its total income
- 90% of its income is distributed to its shareholders.

Although corporations meeting the above requirements are exempted from income tax, trade tax and the solidarity surcharge, the REIT is not a popular company structure in Germany.

LIMITED PARTNERSHIP WITH SHARE CAPITAL (*KOMMANDIT-GESELLSCHAFT AUF AKTIEN*)

A limited partnership with share capital is comparable with a stock corporation. However, at least one general partner is personally liable for the company's debts. This form of corporation is also not popular in Germany.

SOCIETAS EUROPAEA (SE)

A SE is a corporation based on the law of the EU. A SE may be registered in any member state of the EU whereby its company domicile can be easily relocated to another state of the EU. A SE has its own legal entity and must present share capital to the amount of EUR 120,000. It may be founded by a merger of stock corporations from at least two different states of the EU or by conversion.

FOREIGN COMPANIES

As a result of the right of free movement of business within the EU, companies regulated by the jurisdiction of another state of the EU may move their company domicile to Germany. In this case, German courts must observe the legal characteristics of such a company and must not apply German law only.

OTHER TYPES OF COMPANY/BUSINESS ENTERPRISE***SOLE PROPRIETORSHIP (EINZELKAUFMANN)***

A sole proprietorship is the simplest form for running a business under German law. A sole proprietorship is not a legal entity but the business of a natural person with full liability. This structure is especially popular with small businesses. It requires no formal filing or reporting over and above maintaining proper records and obtaining the necessary local permits. The liable proprietor is subject to taxation and must register the business.

INDEPENDENT SALES AGENT/DISTRIBUTOR AND REPRESENTATIVE OFFICE

If a foreign investor does not intend to have any staff based in Germany, then the easiest way to set up a business relationship is through independent sales agents and independent distributors. It is common practice to use sales agents or independent distributors to sell a foreign company's goods in Germany. A representative office in Germany is not subject to all the requirements of opening a branch or subsidiary.

In all cases, deciding on the most sensible form of investment or structure for doing business in Germany, depends on the individual circumstances of a business.

5 – LABOUR

EMPLOYMENT CONTRACTS

The employment contract forms the basis of the relationship between an employee and employer.

The terms of the contract can be freely negotiated by both parties subject to existing legislation, collective agreements where applicable (see below) and bargaining agreements with a potential works council where applicable (see below).

Every employment contract has to comply with the current legislation and the labour law based on the jurisdiction of the Federal Labour Court.

Most of the basic rights and duties of the employer and the employee are settled in labour protection laws such as the following:

- 1) German Civil Code
- 2) Act concerning continued remuneration during sickness
- 3) Act concerning vacation paid
- 4) Working-time act
- 5) Act against unfair dismissal
- 6) Acts concerning maternity protection and parental leave
- 7) Act concerning severely disabled employees
- 8) Act concerning trainees.

This legislation has to be reflected in any contracts, as well as during the on-going employment relationship.

COLLECTIVE AGREEMENTS

According to German law, employer associations and trade unions are able and entitled to negotiate wage settlements and working conditions in collective agreements without interference from government bodies. Wage bargaining represents a collective process during which working conditions and wage settlements are negotiated for entire occupational groups in various industries.

A collective agreement is valid for the employment relationship if the employer is a member of the Employers' Association and the employee is a member of the labour union. Membership is voluntary. Employers who are a member of the Employers' Association frequently declare that collective agreements are applicable in the employment contract in order to treat organised and non-organised employees equally. For smaller companies without membership of the Employer's Association, generally no collective agreement is declared as applicable.

In some industries, collective agreements exist which have been declared as applicable for all employees in that industry by the government, regardless of any memberships.

BARGAINING AGREEMENTS

Working conditions can also be settled by the employer and the works council and are binding for all employees of the company. German companies are not obliged to have a works council. It is up to the employees themselves to establish one. If a works council exists, it has many rights of co-determination and to information based on the Works Council Constitution Act. In addition, the works council must be informed and consulted prior to any termination. If the council is not consulted, a termination is considered invalid.

TERMINATION OF EMPLOYMENT CONTRACTS

Every employer and employee can, at any time and without a notice period, terminate the employment contract extraordinarily based on a severe cause, such as criminal behaviour of the employee, non-payment of salary or discrimination by the employer.

For a normal termination, both parties have to fulfil a relevant notice period stated in the German Civil Code, the labour contract and/or collective agreements.

In small companies, generally with not more than ten employees, the employer normally does not need a special reason for an ordinary dismissal and generally does not have to compensate the employee.

In larger companies, generally with 10 or more employees, the employer needs a reason for a dismissal, to comply with the Act against unfair dismissal. There are detailed requirements for a termination which can be based on the behaviour of the employee, personal or operational reasons. Employees can file for unfair dismissal at the Labour Court with the aim of continuing the employment relationship. These cases are often settled by an agreement which brings termination of the employment and a compensation payment. Works councils have several rights with regards to any dismissal cases by the employer.

SOCIAL INSURANCE

Social insurance coverage in Germany is statutory for all employees.

The compulsory insurance plan serves to protect people from hardship due to sickness, nursing, work-related accidents and unemployment. Moreover, statutory pension insurance is compulsory for all employees.

Social insurance contributions are paid nearly half by the employer and half by the employee. They are paid to the authorities directly by the employer. Any gross payment agreed upon by parties does not include the social insurance contributions to be paid by the employer (nearly half of the rates mentioned below).

TABLE 1

Social security contribution rates for 2012

CONTRIBUTION TYPE	RATE
Health insurance	15.5 % of the gross monthly salary
Nursing insurance	1.95 % of the gross monthly salary
Pension insurance	19.6 % of the gross monthly salary
Unemployment insurance	3 % of the gross monthly salary

Salaries higher than the following gross monthly salaries do not cause a further increase of contributions.

TABLE 2

2012 income thresholds (monthly, upper limit)

	OLD FEDERAL STATES	NEW FEDERAL STATES
Health & nursing insurance	EUR 3,825	EUR 3,825
Pension and unemployment insurance	EUR 5,600	EUR 4,800

Employees earning above certain limits (in most cases higher than mentioned above for health and nursing insurance) are free to join the compulsory health insurance system and can choose a private health insurance provider. An employer has to participate in these contributions too.

6 – TAXATION

The taxation of commercial activities in Germany depends on the particular form of business organisation.

The main aspect to be considered in this context is that unincorporated companies are not taxable entities for the purposes of income or corporate income tax. They are only subject to trade tax and any income of unincorporated companies is taxed at the level of the shareholders. In contrast, a corporation represents an independently taxable entity for all kind of taxes (transparent taxation).

For general information on taxation in Germany, please see:

<http://www.bundesfinanzministerium.de>

UNINCORPORATED COMPANIES AND INDIVIDUALS – INCOME TAX

TAXABLE PERSONS

German residents are liable to income tax on their worldwide income, while non-residents are generally liable to tax on certain German-sourced income. An individual is a German resident if his/her domicile or habitual place of abode is in Germany. A domicile is a home at the disposal of the taxpayer which he/she maintains for a long term. A habitual place of abode is a location where an individual is physically present for a continuous period of more than six months.

Partnerships, such as an OHG, KG, GBR, professional partnership and sole proprietorship, are not generally considered as separate legal entities. Therefore, the partners themselves are usually subject to all rights and obligations. Accordingly, partnerships are not subject to income or corporate income tax, but only to trade tax. Income from a partnership is allocated to the partners. Where partners are individuals, it is subject to income tax at the level of the partners, where an individual tax rate is applicable to each partner. Where partners are corporations, it is subject to corporate income tax.

In order to achieve tax burden neutrality between partnerships and corporations, individuals have the possibility to choose a reduced income tax rate applicable to the retained earnings (*saurierte Gewinne*) of a partnership, which amounts to 28.25% plus a solidarity surcharge, bringing the total rate to 29.8%. After offsetting personal income tax against trade tax payments, retained earnings of a partnership will therefore be subject to an average tax burden similar to that of a corporation under corporate income taxation.

In cases where earnings are distributed to the partners, the distributed earnings are subject to a subsequent taxation of 25% plus a solidarity surcharge, resulting in a total rate of 26.35%, provided and insofar as the annual balance between a partner's capital contribution and withdrawals exceeds the annual profits of the company or the partner's share in the company ('excess withdrawals'). Germany has entered into a large number of agreements for the avoidance of double taxation with other countries. Most treaties make provisions for a situation where an individual is resident in two different countries.

Terms of agreements for the avoidance of double taxation override German tax law and, if an individual is deemed to be a resident of a foreign country under such an agreement, his/her German tax liability will then be computed in accordance with provisions of the treaty agreement for the avoidance of double taxation.

TAXABLE INCOME

Taxable income comprises the entire annual income from the following sources:

- Agriculture & forestry
- Business establishments (trade)
- Independent professional services
- Employment
- Capital investment
- Rental income from immovable property and certain tangible movable property
- Income from royalties
- Other income (gains from private transactions, alimony, annuities, etc.)

Income tax is computed on a progressive scale. German legislation allows for the deduction of certain expenses economically linked with the various sources of income. Relief can be granted for itemised expenses. In some cases, relief can be granted on the basis of standard allowances.

There are two different methods to compute taxable income – the net worth comparison method and the net income method. The income from agriculture and forestry and from business establishments or trade is calculated on the basis of the net worth comparison method. For employment, capital investment, rental income and other income, the net income method applies. Income generated from independent professional services uses the net worth comparison method if it is chosen by the tax payer. Income from capital investment, which includes dividends, interest, royalties, income from typical silent partnerships, capital gains from the sale of shares (provided a participation in the corporation of which the shares are sold of less than 1%) and financial instruments, is generally subject to a flat withholding tax of 25%, plus a solidarity surcharge which brings the total rate to 26.35%. For this income, an allowance of up to EUR 801 per year is granted. Expenses economically connected to investment income are not deductible. However, in cases where the tax burden by the flat withholding tax exceeds the marginal income tax rate of the taxpayer, the taxpayer can opt for an assessment. Furthermore, some other exemptions of the flat withholding tax exist.

LOSSES

In principle, losses can be fully offset against income of the same year. However, some restrictions apply with regard to capital losses from capital investments or from the sale of shares or from private transactions.

In general, losses up to EUR 511,500 can be used to minimise the profit of the preceding year. Further, losses can be carried forward for use in the following years under the so-called 'minimum taxation rules' (up to EUR 1,000,000 of net income can be offset without restrictions; any exceeding losses may be offset against up to 60% of the net income exceeding EUR 1,000,000).

TAX RATES

In 2012, individuals were subject to federal rates of taxation as shown in the table below.

TABLE 3

Overview of income tax rates and allowances for individuals

	SINGLE	MARRIED	TAX RATE
Basic personal allowance	EUR 8,004	EUR 16,008	0%
Progressive rates of:	EUR 8,005 – 52,881	EUR 16,009 – 105,763	14 – 42%
Tax rate as of:	EUR 52,882 – 250,730	EUR 105,764 – 501,461	42%
Highest tax rate as of:	EUR 250,731	EUR 501,462	45%

A 5.5% solidarity surcharge is levied on the amount of tax computed according to the allowances and rates shown in the table above.

Taxes on income from employment are based on the employee's monthly salary (PAYE). It is the employer's duty to deduct tax and to forward it to the fiscal authorities. At the end of the year, the tax amount withheld throughout the year will be certified on the employee's wage tax card in order to be taken into account in the final income tax assessment.

UNINCORPORATED COMPANIES AND INDIVIDUALS – TRADE TAXATION

TAXABLE PERSONS

Individuals and unincorporated companies carrying on a trade or business in Germany are subject to trade tax. Trade tax is collected by the municipalities.

TAX CALCULATION AND TAX RATE

The basis for the trade tax computation is the income for income tax purposes, subject to certain adjustments. Some expenses that can be deducted for income tax purposes are non-deductible for trade tax purposes and vice versa. In 2012, major adjustments include:

- A 25% non-deductibility of the sum consisting of interest payments for debts, annuities and permanent charges
- Profits of a silent partner
- 20% of lease payments for movable assets and 50% of lease payments for immovable assets
- 25% of licence payments if a threshold of EUR 100,000 is exceeded.

For trade tax purposes, the income of individuals and unincorporated companies is minimised by an allowance of EUR 24,500.

Trade tax rates vary from one municipality to another, because municipalities have a degree of discretion when fixing the multiplier on this tax, which is one part of the effective trade tax rate. The other part of the effective trade tax rate is a federal base rate of 3.5%. The system of computation is fairly complicated, but the average trade tax rate is approximately 14% on the basis of a multiplier of 400%. If there is a higher multiplier, trade tax rates increase. For example, Berlin has a multiplier of 410%, Cologne 450%, Dusseldorf 440%, Frankfurt aM 460%, Hamburg 470%, Stuttgart 420% and Munich 490%.

A firm with permanent establishments spread over several municipalities will have the tax distributed amongst the municipalities according to a key based on the size of the payroll.

Due to the 2008 Business Tax Reform, trade tax has to be considered as a non-deductible tax expense for income and trade tax purposes from 2008 onwards. However, a part of the trade tax (the weighting factor of 3.8 on income for trade tax purposes multiplied with the federal base rate) can be deducted from the personal income tax burden of individuals/partners of a partnership.

LOSSES

Trade losses cannot be carried back; however, they can be carried forward without any limit in time under the 'minimum taxation rules' (as already mentioned).

TABLE 4

Example calculation of income tax and trade tax for unincorporated companies

	EXAMPLE (EUR)	
Trade tax		
Taxable income for trade tax purposes	1,000,000	1,000,000
Amount of deduction	<u>24,500</u>	
	975,500	
<hr/>		
Assessment base (Base rate 3.5%)	34,143	
Trade tax (multiplier 400%)	136,570	136,570
<hr/>		
Income tax		
Taxable income before taxes	1,000,000	
<hr/>		
Tax rate pursuant to §32a Abs. 1 S. 2 Nr. 5 German Income Tax Act		
Income tax	434,306	
<hr/>		
Deduction of trade tax pursuant to §35 German Income Tax Act (Trade tax assessment base x 3.8)	<u>129,742</u>	
Final income tax	304,565	304,565
Solidarity Surcharge 5.5%	16,751	16,751
Net income		542,114

CORPORATIONS – CORPORATE INCOME TAX

TAXABLE ENTITIES

Corporations, such as stock corporations, limited liability companies etc., are subject to corporate income tax and a solidarity surcharge.

Corporations which have their legal seat or place of management in Germany have unlimited tax liability in Germany with regards to their worldwide income; all income of resident corporations constitutes business income, irrespective of its source.

In cases where a corporation does not have its legal seat or place of management in Germany, it is liable for tax only on its income derived from German sources, which includes:

- Income derived from a permanent establishment or a permanent representative in Germany
- Gains from the sale of shares in a German corporation
- Rental income
- Investment income.

The tax treatment depends on whether the tax is levied via a filing and assessment procedure (eg business income derived from a permanent establishment) or via a withholding tax procedure (eg dividends, interest, rental income from movable assets and royalties).

TAX BASES AND RATES

Since 2008, corporate income tax is payable for income and capital gains of resident corporations at a rate of 15% of taxable income, regardless of whether the income is distributed or not.

A 5.5% solidarity surcharge is imposed on the corporate income tax, resulting in an effective tax rate of 15.825%.

Corporate income tax is levied on the total amount of income of a corporation after the deduction of business expenses, though some restrictions exist with regards to the deductibility of business expenses, personal expenses, taxes, interest and dividends. Furthermore, depreciation and amortisation rules have to be considered.

Withholding taxes have to be paid on dividends and interest payments to resident corporations at a rate of 25% plus a solidarity surcharge of 5.5%, resulting in an effective tax rate of 26.375%. These withholding taxes are creditable against the tax liability of the recipient.

The same rates apply for non-resident corporations. However, the withholding tax rate for dividends and interest payments to these non-resident corporations may be minimised by regulations of double tax treaties or EU Directives. Furthermore, there is additional withholding tax regulation for income subject to the tax withholding procedure.

TAX SYSTEM

As corporations are taxed as separate legal entities and independently from their shareholders, the risk of double taxation exists in cases where profit distributions are made to shareholders, since taxes are levied at the level of the corporation and at the level of shareholders. The basic aim of the corporate income tax system is to avoid or reduce such double taxation.

Today, in Germany, a double taxation system is in place which considers the risk of double taxation insofar as corporate profits are taxed at the level of the corporation (at the corporate income tax rate) and dividends are taxed at the level of the shareholders. This is done by not taking total dividend payments.

Under the former so-called 'imputation' or 'split-rate system', a full imputation credit was granted to resident shareholders. This ended in 2001, when transitional regulations were arranged. From 2002 to 2008, a 'half-income-system' was applied at the level of shareholders. From 2009 onwards, the 'half-income-system' was replaced by the 'partial-income-system'. Furthermore, a distinction is now made between private shareholders and shares which are held as business assets.

In the case of private shareholders, a flat withholding tax on dividends is applied at a rate of 25% plus a solidarity surcharge of 5.5%, resulting in a total rate of 26.375%. However, there are some further restrictions. For the business income of shareholders, 60% of the dividends are taxable (ie included in a shareholder's personal income tax base) and 40% are tax-exempt. However, shareholder expenses related to distributed profits are deductible by 60%.

If the shareholder is a corporation, distributed profits are exempt from taxation. However, an amount equivalent to 5% of a corporation's dividend is treated as a non-deductible business expense. Hence, 95% of the dividend income is tax-exempt at the level of the shareholder. Expenses incurred which relate to such income are fully deductible for corporate tax purposes.

In every case, the corporation paying the dividend has to deduct withholding taxes at a rate of 25%. These withholding taxes are creditable against the tax liability of the recipient.

Payments of certain amounts to non-residents are subject to withholding taxes. These include payments such as royalties and licence fees, and interest and management fees.

CAPITAL GAINS

Capital gains resulting from the sale of shares held by a corporation are fully exempt from corporate income tax. However, an amount equivalent to 5% of the capital gain is treated as a non-deductible business expense. Hence, 95% of the capital gain is tax-exempt. There is no minimum participation requirement, nor any minimum holding period, except in cases where there are restructuring situations when a seven-year holding period is required. In cases where the value of the shares has been written down tax-efficiently and has not been re-valued before the sale of the shares, the capital gain is not tax-exempt to the extent of the write-down.

At the present time, write-downs due to impaired value are not tax deductible.

All other capital gains are subject to corporate income tax and withholding taxes. However, up to 100% of capital gains resulting from the sale of real estate and buildings may be offset against the costs of similar assets acquired in the same year, the preceding year or in the following four years.

LOSSES

Losses are deductible. Losses up to EUR 511,500 may be carried back to the preceding year. Losses exceeding this amount may be carried forward for use in following years under minimum taxation rules.

However, any loss carry-forward will be erased during reorganisations and when change-of-control-rules apply. The transfer of more than 25% and less than 50% of a corporation's shares within a five-year period to one person or parties related thereto, results in pro rata forfeiture of losses. If more than 50% of the shares are transferred, losses will be erased in total. Losses resulting from the sale of shares are not tax deductible.

Restrictions apply to the offset of losses derived from foreign operations.

EARNINGS STRIPPING RULES

Earnings stripping rules replaced the former thin-capitalisation rules following the 2008 Business Tax Reform. Now, a general limit on the deduction of interest payments is given, which applies to all kinds of debt financing. According to the earnings stripping rules, interest expenses are fully deductible if they do not exceed interest income. Any exceeding net interest expense is also deductible in cases where it does not exceed EUR 3 million. If the net interest expense is more than EUR 3 million, such interest expense is only deductible up to 30% of EBITDA (earnings before interest, taxes, depreciation and amortisation).

However, the limit rule does not apply if any of the following conditions are satisfied:

- The company is not a member of a consolidated group (a group of companies that can be consolidated under International Financial Reporting Standards – IFRS), or
- The equity ratio of the German subgroup is equal to or higher than the equity ratio for the group as a whole, as shown on the balance sheet of the preceding fiscal year (the so-called 'escape clause'). A deviation up to 1% downwards is not harmful. A 'group' is defined as a group of entities that could be considered under IFRS, regardless of whether a consolidation has actually been carried out. The escape clause does not apply if any entity in the worldwide group has received loans from a substantial shareholder (more than 25%) or related party not included in the group and if the interest paid on such a debt exceeds 10% of the net interest expense.

CORPORATIONS –TRADE TAX

TAXABLE ENTITIES

All corporations carrying on a business in Germany are subject to trade tax.

TAX CALCULATION AND RATES

In principle, the rules and regulations applicable to the computation of trade tax for corporations correspond to those applicable for unincorporated businesses. However, the allowance of EUR 24,500 does not apply for corporations.

Furthermore, dividends received from shareholdings in resident or non-resident companies are subject to trade tax if the participation is less than 15% at the beginning of the fiscal year, although these dividends are tax-exempt with regards to corporate income tax (see previous section).

TABLE 5

Example calculation of income tax and trade tax for corporations

EXAMPLE (EUR)		
Trade tax		
Taxable income for trade tax purposes	1,000,000	1,000,000
Amount of deduction	<u>0</u>	
	1,000,000	
<hr/>		
Assessment base (Base rate 3.5%)	35,000	
Trade tax (multiplier 400%)	140,000	140,000
<hr/>		
Corporate income tax		
Taxable income before taxes	1,000,000	
<hr/>		
Tax rate pursuant to §23 sec. 1 German Corporate Income Tax Act (15%)		
Corporate income tax	150,000	150,000
Solidarity Surcharge 5.5%	8,250	8,250
Net income		701,750

TABLE 6

Example calculation of income and other taxes for a shareholder

	PRIVATE (FLAT WITHHOLDING TAX) – EUR	BUSINESS (PARTIAL INCOME SYSTEM) – EUR
Dividend from corporation	701,750	701,750
Withholding tax (25%)		175,438
Flat withholding tax (25%)	175,438	
Solidarity Surcharge (5.5%)	<u>9,649</u>	<u>9,649</u>
Cash dividend	516,663	516,663
<hr/>		
Taxable income of shareholder (60% of 701,750)		421,050
<hr/>		
Income tax (on 421,050)		
Tax rate pursuant to §32a Abs. 1 S. 2 Nr. 5 German Income Tax Act		
Income tax		173,779
Solidarity Surcharge 5.5%		9,558
Net income	516,663	518,414
(Creditable withholding tax and solidarity surcharge have been considered; church tax has not been considered)		

TABLE 7

Comparison for incorporated and unincorporated companies

	CORPORATION	UNINCORPORATED COMPANY
Profit before tax	1,000,000	1,000,000
Trade tax (multiplier 400%)	140,000	136,570
Corporation tax + solidarity surcharge	158,250	-
Income tax + solidarity surcharge in case of full distribution		<u>321,316</u>
Net income	701,750	542,114

TAXATION OF PERMANENT ESTABLISHMENTS IN GERMANY

According to German tax law, a permanent establishment is defined as an operational facility (representation office, plant, sales office, etc.) that serves to carry out business activities in Germany.

Commercial activities include all sorts of business transactions that exceed the mere preparation of business contacts or other auxiliary services. The permanent establishment has its own internal organisation and bookkeeping and could, therefore, exist as an independent commercial entity without major restructuring efforts.

Because there are different national definitions of the term 'permanent establishment', the tax committee of the Organisation for Economic Co-operation and Development (OECD) has come up with a uniform definition (cf. article 5, OECD sample convention).

The right of taxation is usually regulated by means of Treaties for the Avoidance of Double Taxation between Germany and another country. In most cases, taxation takes place in Germany in line with the international principle of the place of operations. The other country, therefore, does not levy taxes on the profits of permanent establishments located in Germany.

If the foreign parent company is an unincorporated partnership, then the profits of the permanent establishment located in Germany are usually subject to German income tax.

Profits are, as a consequence, exempt from further taxation in the parent company's country of domicile. Losses of a permanent establishment can only be offset against positive income within the scope of the limited liability for taxes in Germany. Both a loss carry-back and a loss carry-forward are possible for the income of a permanent establishment.

If the 'parent company' is a corporation, the profits of the permanent establishment will be subject to corporation tax and trade tax.

SOLIDARITY SURCHARGE

The solidarity surcharge on income and corporation tax has been introduced to raise additional funds for German reunification.

The solidarity surcharge amounts to 5.5% of the respective income or corporation tax burden assessed for the fiscal year.

The surcharge applies to individuals as well as corporations, associations and conglomerations of property with limited or unlimited tax liability located in any part of Germany.

The solidarity surcharge has been introduced only as a temporary tax burden. It will be phased out eventually, although no definite time has been set by legislation.

OTHER TAXES

VALUE ADDED TAX (VAT)

German VAT is a general tax on the consumption of goods and services in Germany. In principle, all entrepreneurs, corporations or individuals are subject to VAT. This applies also to non-resident entrepreneurs who offer supplies or perform services in Germany.

Several regulations exist that set out whether goods or services are subject to German VAT. The German VAT Act complies predominantly with the Council Directive 2006/112/EC (VAT Directive).

The VAT liability for goods or services can fall under one of three main categories:

- Taxable at the standard rate (currently 19%) or at the reduced rate (7%)
- Exempt
- Outside the scope of Germany.

In Germany, for some kinds of services and supplies, a reverse-charge-system is applicable.

CHURCH TAX

Residents in Germany who have chosen to officially register themselves as members of the Roman Catholic or Protestant-Lutheran churches are liable to church tax. Church tax is not a sub-category of personal income tax. However, the amount of church tax depends on the personal income tax liability.

Depending on the federal state, church tax is between 8–9% of an individual's personal income tax burden. Church tax is collected by the tax authorities and distributed among the churches.

Secular persons or members of other religious affiliations are not liable for church tax.

7 – ACCOUNTING & REPORTING

ACCOUNTING AND CORPORATE RECORDKEEPING

Adequate financial records must be kept by all businesses operating in Germany.

Books must clearly show all commercial transactions and the financial position pursuant to generally accepted accounting principles. Bookkeeping must be maintained in such a way that an outside expert can derive, within a reasonable timeframe, an overview of the business operations and the position of the firm. Business operations need to be comprehensible from their origins through to completion.

At the end of each financial year, both unincorporated and incorporated firms must prepare their annual financial statements, including a balance sheet as well as an income statement.

In addition, corporations must prepare notes to the financial statement and a management report. The latter must make reference to the development of the company's main business activities. Furthermore, an assessment of the present situation and future developments must be made. The notes to the financial statement must include details as prescribed by statute and by law. These details need to give further explanation to individual items in the balance sheet and income statement respectively.

German legislation has incorporated the rules and regulations of the European Economic Community (EEC) Fourth Directive on accounting and reporting issues, the EEC Seventh Directive on consolidated accounts and the EEC Eighth Directive on account control and external auditing requirements. The last modification was made with the implementation of the EU-Fair-Value-Directive and the EU-Modernisation-Directive.

The required statutory corporate records generally include:

- The documents of incorporation
- The company articles
- All minutes of shareholders' meetings
- A register of shareholders and directors
- Prescribed accounting documents.

The prescribed accounting documents include the following:

- Commercial business records, inventories, opening balance sheets, annual financial statements, management reports, procedural instructions and other organisational documents necessary for interpreting such documents
- Incoming business correspondence
- Copies of mailed business correspondence.

Records need to be kept regularly for ten years. If the documents are needed for tax purposes, a longer period of keeping may become effective.

The German Commercial Code (HGB) also prescribes the preparation of inventories for the end of every business year. The inventory must be taken within a period consistent with orderly business practice. Certain procedures for simplifying the keeping of an inventory are allowed if they are in accordance with generally accepted accounting principles. The informational value of the inventory prepared by these methods must match the informational value of an inventory prepared on the basis of a physical count.

AUDIT REQUIREMENTS

Unincorporated companies are generally not obliged to appoint an external auditor. The audit and disclosure requirements do, however, take effect when certain size criteria are met. These are currently set at:

- A balance sheet total exceeding EUR 65 million
- An annual turnover exceeding EUR 130 million
- An annual average of more than 5,000 employees.

At least two of the above thresholds must be exceeded on three successive balance sheet dates.

The audit requirements for corporations and for a special limited partnership (GmbH & Co. KG) are contained in the German Commercial Code which groups corporations into class sizes shown in the table below.

TABLE 8

Corporation class sizes, effective from 2012

	SMALL	MEDIUM
Balance sheet total	≤ EUR 4,840,000	≤ EUR 19,250,000
Turnover	≤ EUR 9,680,000	≤ EUR 38,500,000
Employees	≤ 50	≤ 250

Small corporations are those that do not exceed at least two of the aforementioned criteria. Medium-sized corporations are those that exceed at least two of the criteria in column one but, at any given time, do not exceed at least two of the criteria in column two. Corporations that exceed two of the criteria in column two are classified as large. The respective characteristics need to be met on two successive balance sheet dates.

Companies listed on the stock exchange, banks, insurance companies and other companies acting in the financial sector are always classified as large corporations.

The annual financial statement and the management report of companies which are not small, according to the aforementioned definition, must be examined by an external auditor. Only audited annual financial statements can be adopted.

The legally required consolidated financial statement and consolidated management report of companies always need to be examined by an external auditor.

DISCLOSURE REQUIREMENTS

The legal representatives of companies must file the annual financial statement at the electronic commercial register without undue delay after its presentation to the shareholders, and no later than nine months (for small corporations, 12 months) into the following business year after the closing day. The law distinguishes again between different class sizes of company, as shown in the table below:

TABLE 9

Type of disclosure, according to company size

	SMALL	MEDIUM	LARGE
Disclosure of balance sheet	CR	CR	FG
Income statement	-	CR	FG
Notes to the financial statement	CR	CR	FG
Management report	-	CR	FG

CR = Commercial Register

FG = Federal Gazette

Large corporations are also subject to disclosure of their annual financial statements and of the management report in the Electronic Federal Gazette.

8 – UHY REPRESENTATION IN GERMANY

BERLIN

UHY Lauer & Dr. Peters KG
Zimmerstraße 23
D-10969 Berlin
Germany

Phone: +49 30 22 65 93-0
Fax: +49 30 22 67 90 50
Email: berlin@uhy-berlin.de
Website: www.uhy-berlin.de

Contacts: Reinhold Lauer at lauer@uhy-berlin.de
Dr. Ulla Peters at peters@uhy-berlin.de

BREMEN

Clostermann & Jasper Partnerschaft
Kleiner Ort 5
D-28357 Bremen
Germany

Phone: +49 421 16 23 70
Fax: +49 421 16 23 725
Email: info@clostermann-jasper.de
Website: www.clostermann-jasper.de

Contacts: Oliver Gampper at og@clostermann-jasper.de
Torsten Jasper at tj@clostermann-jasper.de

COLOGNE

Dr. Leyh, Dr. Kossow & Dr. Ott KG
Siegburger Str. 215
D-50679 Cologne
Germany

Phone: +49 221 36 00 60
Fax: +49 221 36 00 66 6
Email: koeln@lko.de
Website: www.lko.de

Contacts: Gunter Stoeber at gunter.stoeber@lko.de
Horst Leyh at horst.leyh@lko.de
Birgit Seidel at seidel@lko.de

FRANKFURT

UHY Wahlen & Partner
 Gerbermühlstraße 7
 D-60594 Frankfurt am Main
 Germany

Phone: +49 69 6605 9379 0
 Fax: +49 69 66059379 99
 Email: frankfurth@uhy-wahlen.de
 Website: frankfurt@uhy-wahlen.de

Contact: Thomas Wahlen at thomas.wahlen@uhy-wahlen.de

HAMBURG

Clostermann & Jasper Partnerschaft
 Esplanade 41
 D-20354 Hamburg
 Germany

Phone: +49 40 530 29 65 0
 Fax: +49 40 530 29 65 65
 Email: info@clostermann-jasper.de
 Website: www.clostermann-jasper.de

Contact: Torsten Jasper at tj@clostermann-jasper.de

MUNICH

Dr. Langenmayr GmbH
 Wirtschaftsprüfungsgesellschaft
 Seidlstrasse 30/VII
 D-80335 Munich
 Germany

Phone: +49 89 55 17 07 0
 Fax: +49 89 55 17 07 49
 Email: lp@dr-langenmayr.de
 Website: www.dr.-langenmayr.de

Contacts: Johannes Bitzer at jbitzer@dr-langenmayr.de,
 Edmund Weigert at weigert@uhy-deutschland.de
 Thilo Rath at trath@dr-langenmayr.de

STUTTGART

Kullen Mueller Zinser Treuhand GmbH
 Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft
 Amundsenstraße 6
 D-71063 Sindelfingen/Stuttgart
 Germany

Phone: +49 7031 863 900
 Fax: +49 7031 863 899

Email: stuttgart@uhy-deutschland.de
Website: www.kullen-mueller-zinser.de

Contact: Sebastian Otten at sebastian.otten@k-m-z.de

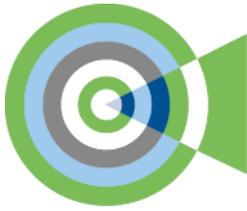
ROSTOCK

UHY Lauer & Dr. Peters KG
Platz der Freundschaft 1
D-18059 Rostock
Germany

Phone: +49 381 4 44 450
Fax: +49 381 4 44 45 29
Email: rostock@uhy-rostock.de
Website: www.uhy-berlin.de

Contact: Ulla Peters at peters@uhy-berlin.de

For current contact details, please visit: www.uhy-deutschland.de



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