

Germany

Contacts

Dortmund

EY GmbH
Westfalendamm 11
Dortmund
44141
Germany

Carl-Josef Husken
carl-josef.husken@de.ey.com
+49 231 55011 22229

Eschborn/Frankfurt

EY GmbH
Mergenthalerallee 3-5
Eschborn/Frankfurt (Main)
65760
Germany

Martin Riegel
martin.riegel@de.ey.com
+49 6196 996 20238

Stefan Gratzki
stefan.gratzki@de.ey.com
+49 6196 996 27551

Hamburg

EY GmbH
Rothenbaumchaussee 78
Hamburg
20148
Germany

Helmut Rundshagen
helmut.rundshagen@de.ey.com
+49 40 36132 12565

München

EY GmbH
Arnulfstraße 59
München
80636
Germany

Susanne von Petrikowsky
susanne.von.petrikowsky@de.ey.com
+49 89 14331 17323

Christian Reiter
christian.reiter@de.ey.com
+49 89 14331 16539

Stuttgart

EY GmbH
Mittlerer Pfad 15
Stuttgart
70499
Germany

Christian Ph. Steger
christian.steger@de.ey.com
+49 711 9881 11988



1. Types of tax

1.1 Inheritance and gift tax

Germany has a unified inheritance and gift tax called “Erbschaft und Schenkungsteuer” (*ErbSt*), which was reformed effective 1 January 2009 (amended 1 January 2010 and 1 January 2011). *ErbSt* is imposed on any transfer of property at death or by gift (or by deemed gift). The basis of assessment is the benefit accruing to the transferee (beneficiary or donee). The *ErbSt* is regulated on a federal level, although the tax revenue is assigned to the various federal states of Germany.

At present, a court decision by the Federal Constitutional Court (*Bundesverfassungsgericht*) is pending regarding the question whether the German Inheritance and Donation Tax Act in its current form violates German Constitutional Law or not. The hearing (*mündliche Verhandlung*) took place on 8 July 2014; as a rule, a decision of the Federal Constitutional Court will be pronounced within three months after the hearing of the case has been closed.

Note that in the case of German family foundations, there is a deemed gift of property every 30 years, which is subject to unlimited German *ErbSt* (recurrent charge). The 30-year period starts on the date of the first transfer of property to the German family foundation.

1.2 Real estate transfer tax

The transfer of German real estate is basically subject to real estate transfer tax of between 4.5% and 5.0% (depending on where the real estate is located). But a transfer by inheritance or gift and is usually exempt from real estate transfer tax.

2. Who is liable?

2.1 Unlimited liability

Any transfer of worldwide net property either at death or by gift (or by deemed gift) is generally subject to unlimited taxation if either the decedent (donor) or the beneficiary (donee) is considered to be domiciled in Germany for tax purposes. German tax domicile exists if any of the following conditions apply:

- ▶ An individual has his or her residence or habitual place of abode in Germany.
- ▶ A nonresident German citizen has been resident for tax purposes in Germany at any time within the last five years prior to a transfer at death or by gift.
- ▶ A nonresident German citizen is employed by a legal entity organized under German public law. In this case the dependents who live in the household of such German citizen have a German tax domicile as well.
- ▶ A corporation or any other legal entities having their place of management or legal seat in Germany.

2.2 Limited liability

Any individual or legal entity who is not resident as aforementioned will be subject to *ErbSt* only upon the transfer of net property, which is regarded as German-situated according to German national tax law. German-situated property means:

- ▶ Real estate, agricultural and forestry property situated in Germany
- ▶ Assets pertaining to a permanent establishment of a commercial business located in Germany



Germany

- ▶ Shareholdings in German resident corporations if the shareholder owns (individually or jointly with other persons closely related to the shareholder) directly or indirectly at least 10% of the registered share capital
- ▶ Inventions, designs and topographies recorded in a German register as far as assets of a German permanent establishment
- ▶ Assets that have been leased to a commercial business operated in Germany
- ▶ Mortgages or any other receivables secured by German-situated real estate or by German-registered ships, except for such receivables for which negotiable bonds have been issued
- ▶ Any beneficial interests (e.g., right of usufruct) in the aforementioned assets
- ▶ Claims arising from silent partnerships and profit participating loans if the debtor is situated in Germany

A nonresident individual as decedent (donor) is subject to an extended limited tax liability (e.g., with regard to capital claims vis-à-vis domestic debtors or with regard to moveable property abroad), provided:

1. Such individual was subject to unlimited income tax liability in Germany within the last 10 years prior to a transfer at death or by gift and
2. Such individual was cumulatively a German national and subject to unlimited German income tax liability for a combined period of five years within a time period of 10 years prior to the end of the unlimited income tax liability.

2.3 Domicile

Residence

Under German tax law, an individual's residence is the place that he or she occupies under circumstances that indicate that he or she will retain and use it on more than a temporary basis. Residence requires an intent to stay, which must be evidenced by objective criteria. The German tax authorities' interpretation of intent to stay is quite broad: such intent will be presumed if an owned or rented dwelling is used regularly for a certain period of time and not merely from time to time. Therefore, it is possible for an individual to be a resident in different countries at the same time.

Habitual place of abode

The term habitual place of abode implies the location where a person is physically present under circumstances that indicate that his or her presence in that particular place is not merely temporary. As a general rule, a habitual place of abode, and thus tax residence, is deemed to exist if the individual's stay in Germany exceeds six months. In this case, he or she will be deemed resident for the entire period of his or her stay in Germany.

Residence and double tax treaties

Special rules apply with regard to certain double-tax treaties (DTTs). For example, according to the German/US DTT, an individual who is considered a resident in both contracting states pursuant to national tax law but who is a citizen of only one of the contracting states will be deemed domiciled in that state for a period of 10 years after becoming a resident for inheritance- and gift-tax purposes in the other state.



3. Rates

The applicable tax rate depends on the tax class of the acquirer (see below) and the value of the taxable acquisition. The tax assessment basis is the taxable value of the assets transferred after exemptions and reliefs.

Taxable value of the acquisition exceeds	Acquirer in		
	Tax class I	Tax class II	Tax class III
€0	7%	15%	30%
€75,000	11%	20%	30%
€300,000	15%	25%	30%
€600,000	19%	30%	30%
€6 million	23%	35%	50%
€13 million	27%	40%	50%
€26 million	30%	43%	50%

Note that the taxable value of assets, which is excluded from tax under German ErbSt pursuant to a DTT, must be added to the taxable value of the transfer in order to determine the applicable tax rate (progression reserve). Thus, it is not taxable but affects the overall rate.

Donees or heirs not in tax class I who acquire agricultural or forestry or other business assets, interests in a partnership and substantial shareholdings (direct participation of more than 25% of the registered share capital) in a corporation resident in Germany, in the European Union (EU) or in the European Economic Area (EEA) could, under certain conditions, benefit from a reduction. This reduction is the difference between the amounts of inheritance tax calculated on the basis of the tax class to be applied pursuant to the actual relationship to the deceased/donor and on the basis of tax class I. Note that, with regard to this benefit, the anti-abuse rules mentioned below also apply (see Section 4 below).

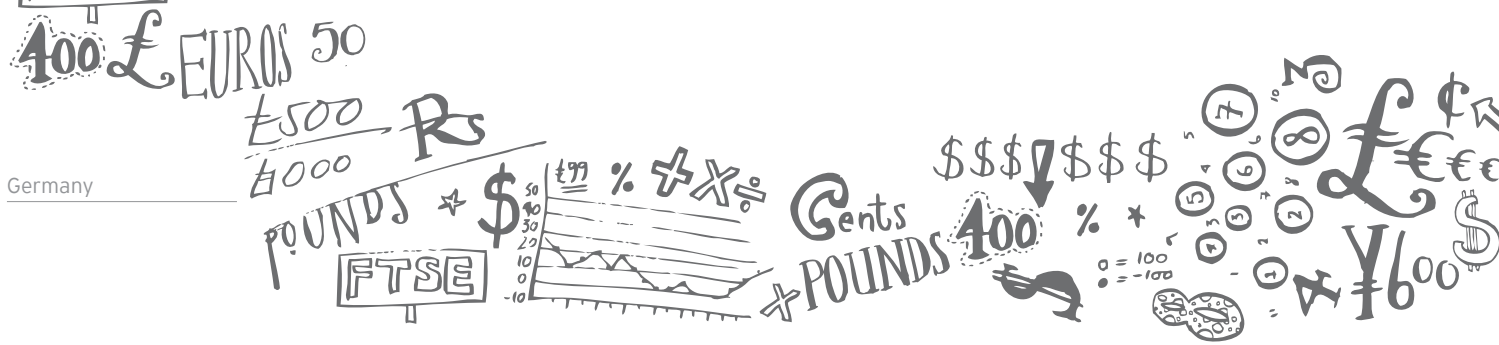
The applicable tax class depends on both the relationship of the donee to the donor (decedent) and the value of the taxable acquisition. Donees are divided into three tax classes:

Tax class I:

- ▶ Spouse and partners of a registered same-sex partnership under German law
- ▶ Children and stepchildren
- ▶ Descendants of children and stepchildren
- ▶ Parents and ancestors (acquisition by death)

Tax class II:

- ▶ Parents and ancestors (acquisition by gift)
- ▶ Siblings
- ▶ Nephews and nieces
- ▶ Stepparents
- ▶ Sons and daughters-in-law
- ▶ Parents-in-law
- ▶ Divorced spouse and partners of a dissolved registered same-sex partnership



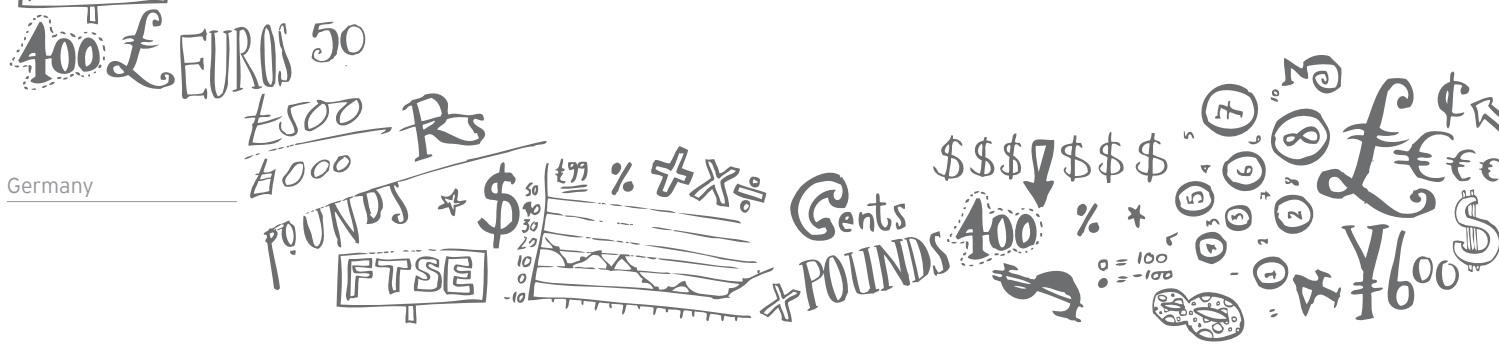
Tax class III:

4. Exemptions and reliefs

- ▶ Household and personal effects up to a value of €41,000 if acquired by a person in tax class I (see Section 3); otherwise up to a value of €12,000.
- ▶ Real estate (including parts of real estate), art items, collections of art and scientific items, archives or libraries, if there is a public interest in preserving such items because of their importance to art, history or science. This is provided because the annual costs associated with those items normally exceed the income generated from such items. It also helps to make assets accessible to the public. The tax exemption for collections of art and scientific items is 60%, and includes parts of real estate. It amounts to 85% of the market value or total exemption if further conditions are met.
- ▶ Donations for a commonly acknowledged purpose (such as birthday presents, wedding, Christmas), but only if at an appropriate value with respect to the occasion.
- ▶ Donations to bona fide churches accepted as such in Germany and to Jewish cultural communities in Germany.
- ▶ Charitable donations.
- ▶ Donations to political parties.
- ▶ Donations to the Federal Republic of Germany, the German states or municipalities and certain charitable foundations.
- ▶ The acquisition of the family home for the owner's use is tax free if it is gifted to the spouse or to the partner of a registered same-sex partnership *inter vivos*. The tax exemption also applies if the family home is passed to the aforementioned acquirers upon death, provided that the acquirer uses the family home for his or her own purposes for a period of 10 years after the acquisition. If there are pressing reasons why the acquirer cannot use the real estate for his or her own purposes (e.g., in the event that the acquirer requires health care), this tax-free status remains unaffected.
- ▶ Children and stepchildren, as well as children of deceased children or stepchildren, can acquire the testator's family home by reason of death without paying tax if the acquirer uses the family home for his or her own use immediately and as far as the living space does not exceed 200 square meters. The portion exceeding 200 square meters is liable to tax. The exemption is lost if the acquirer does not use the family home for his or her own purposes for a period of 10 years after the acquisition.

Agricultural, forestry or business assets





An additional allowance of up to €256,000 is granted to the surviving spouse and the surviving partner of a registered same-sex partnership, provided that the surviving spouse or the surviving partner of a same-sex partnership is not entitled to pension payments upon the death of the spouse or the partner of a registered same-sex partnership. If so, the allowance is reduced by the net present value of such pension claims. An additional allowance of up to €52,000 is granted to surviving children (up to age 27) depending on their age. Any entitlement to pension and similar payments reduce the allowance in the same way as described for the spouse or the partner of a registered same-sex partnership.

Generally, on any transfer of property subject to ErbSt, the German financial authorities must be notified within three months of the transfer by the recipient. In the case of *inter vivos* transfers, the transferor also has a reporting obligation. There are, however, certain exceptions to this notification obligation if i.a. the acquisition is evidenced by a deed certified by a German court or by a German notary public. In the case of a donation certified by a German notary, a notification is not required.

- Since the inheritance tax reform has come into effect on 1 January 2009, the tax assessment basis for the German ErbSt is the FMV of the transferred asset. The key principles are set out below.



- 127



7. Trusts, foundations and private purpose funds

7.1 Trusts

German civil law does not contain specific provisions for trusts, and Germany has not ratified the Hague Convention on the Recognition of Trusts dated 20 October 1984.

For example, a foreign trust with German-situated property set up by a will is invalid from a German civil law perspective. Any trust that is created will be assimilated to the legal entity under German civil law, which most closely resembles the provisions of the trust (e.g., foundation, aggregation of property, nominee agreement, execution of a last will).

Taxation of the trust

The tax authorities classify a trust on the basis of the following criteria:

- ▶ *Revocable trust*: The ownership of the assets cannot be transferred to the trust. Income and assets of the trust remain taxable in the hands of the settlor.
- ▶ *Irrevocable trust*: The ownership of the assets can be transferred to the trust. The trust itself with its income and assets is subject to tax.

Taxation of the endowment with capital – inheritance and gift tax

The German tax treatment of a trust created under a foreign jurisdiction depends mainly on the economic substance of the foreign settlement. The basic criterion for determining whether the formation of a trust does constitute a taxable event under German tax law depends on whether the settlement involves a final and irrevocable disposal of economic ownership of the transferred assets. The transfer of assets to a trust is only subject to gift tax if the trust is then factually and legally able to freely dispose of the assets. According to the German Supreme Tax Court, the review of this criterion should be limited to the civil law position. The ruling stated that the party to whom the assets are attributable from an economic perspective is irrelevant. Consequently, the structure must be deemed a revocable trust and not constitute a transaction subject to gift tax if the settlor has reserved the following rights under the trust's constitution:

- ▶ To amend the constitution at any time
- ▶ To revoke the trust at any time
- ▶ To issue instructions to the trustee

Accordingly, the creation of a grantor's trust is, as a rule, not subject to gift tax if the settlor of a grantor's trust reserves the right to issue wide-ranging instructions to the trustee that extend to revoking the trust. In contrast, gift tax is regularly incurred in the transfer of assets to a revocable trust, as the trustor merely reserves the right to revoke the trust but not the right to issue any other instructions to the trustee. In that case, as a rule, the transfer of assets to a revocable trust should trigger gift tax. The later revocation of the trust donation also causes the tax relating to the past to be extinguished.

Tax class III is applied to foreign trust transfers and subjected to gift tax.

Taxation of the beneficiaries

Establishing a foreign trust leads to income tax consequences. There are certain risks with regard to pre-immigration trusts, as follows:

- ▶ If it is possible for the settlor to revoke the trust and unconditionally reclaim the assets (a revocable trust), and if the settlor has substantial influence on the investment decisions of the trustee, then the items of income (*Einkünfte*) and assets of the trust will most likely be taxed as items of income and assets of the settlor (viewed as a nominee arrangement).
- ▶ Irrevocable trusts of which more than 50% of the beneficiaries or remaindermen are relatives of the settlor are treated as foreign "family foundations," and, are subject to the German controlled foreign companies (CFC) legislation (i.e., if the settlor is a resident in Germany, the items of income of the trust will be directly attributed to him or her and be subject to German income tax irrespective of whether there is a distribution to the beneficiaries).



- ▶ If the settlor is a nonresident, but one beneficiary or remainderman is resident in Germany, the items of income and assets of such an irrevocable trust will be attributed proportionally to such beneficiary or remainderman and will be subject to German income tax irrespective of whether there is a distribution to the beneficiaries.
- ▶ If the income from the trust fund is kept in a lower-tier company in which the trust (if applicable with a related party) holds more than 50% (1% in the case of certain investment income), the items of income of such company will be attributed to the settlors or beneficiaries proportionally as well.
- ▶ Following the proceedings initiated against Germany for breach of contract in connection with the considerable doubt as to the compliance with European law, the German CFC legislation was modified in 2009. Consequently, items of income should not be attributed if the trust or its management is domiciled in an EU/EEA Member State. Nevertheless, the beneficiaries of the income of the trust must additionally provide evidence that they have legally and factually been deprived of the power of disposal over the trust assets.
- ▶ If the income from an irrevocable trust is distributed to beneficiaries residing in Germany, it is taxable in Germany provided that there has been no taxation according to German CFC legislation. Thus, the German CFC law takes priority over the German income tax law.

That tax impact can be avoided by the use of structures familiar to German civil law, which may achieve the intended economic result. For example:

- ▶ *Provisional and reversionary heirs (Vor- und Nacherbschaft)*: appointment of a spouse as the provisional heir (broadly speaking, giving full ownership for their remaining lifetime, but subject to certain safeguards that can partially be released by the testator) and children as reversionary heirs (full ownership at the death of the provisional heir).
- ▶ *Usufruct (Nießbrauch)*: the donor can either be retained or transferred. In a usufruct, only the value of the property reduced by the value of the usufruct is subject to tax, not the total value of the donee-acquired property.

7.2 Foundations

According to German civil law, a foundation is an organization that, by using its capital, promotes a special purpose set by the founder. Usually, the capital of the foundation needs to be preserved and only the income is spent for the defined purpose. A foundation has its own constitution regulating its organizational structure and codifying the purposes set by the founder. A foundation has no members or shareholders and can be formed as a legal entity.

The foundation is formed as a legal entity by way of a unilateral declaration of intent (*Stiftungsgeschäft*) of the founder and the approval of the supervising local authority (*Stiftungsaufsichtsbehörde*). The founder declares to establish the foundation, gives the constitution and endows the original capitalization. The constitution sets out the purpose and regulations for the organization of the foundation.

Taxation of the foundation

The foundation itself is subject to tax. Charitable foundations exclusively pursue special charitable purposes according to the German General Fiscal Code and enjoy tax shelter. If the only purpose of the foundation is the provision of benefits to the founder's family members (*Familienstiftung*), the foundation is not tax privileged.

Taxation of the endowment with capital – inheritance and gift tax

The endowment with capital of a foundation – either by the first endowment or by an external donation – is a gift because the founder or donator does not receive anything in return (like a share or membership right). If a foundation inherits capital, the inheritance is regarded as an acquirement by reason of death according to the Inheritance and Gift Tax Act. Such endowments are generally subject to inheritance and gift tax provided that the foundation is factually and legally able to freely dispose of the assets endowed to it by the founder.





8.2 Forced heirship

The German Civil Code provides strict forced heirship rules enabling certain persons to claim a share of an estate if they are excluded from succession by the decedent's last will.

The descendants, the spouse, the partner of a registered same-sex partnership and the parents of the decedent may claim an amount of up to one-half of their intestacy share (see Section 8.5). Please note that the claim is for cash only and will not entitle the (partially) excluded claimant to any property in specie that forms part of the estate.

The forced heirship claim amounts to a cash value equivalent to the share of the FMV of the estate on intestacy:

- ▶ Less the FMV of any *inter vivos* gifts from the decedent to the claimant, if at the time of donation the donor stipulated that the gift should be credited against the mandatory share.
- ▶ Plus the FMV of any *inter vivos* gift from the decedent to a third person within the 10-year period prior to the death of the decedent. The addition is reduced by one-tenth for each year following the earlier bequest provided the succession takes place on or after 1 January 2010.

According to a ruling of the German Supreme Court with regard to a previous version of the respective provision, the 10-year period will not begin unless the donor gives up any economic use with respect to the gift (e.g., the 10-year period will not begin if a right of usufruct is retained by the donor).

German citizens can avoid these rules only by a pre-death waiver by the potential claimant. Such waiver may in some events require separate counsel for the claimant and will be valid only if performed by notarial deed.

8.3 Matrimonial regimes and civil partnerships

German family law distinguishes between three marital property regimes:

- ▶ Statutory marital property regime (*Zugewinnngemeinschaft*): community of accrued gain): according to this regime, spouses and partners of a registered same-sex partnership hold their assets as separate property during their marriage or partnership, although there are partial restraints on management and disposal. Upon divorce or death, the gain accrued on the property of the spouses or the partners of a registered same-sex partnership during the marriage or the partnership is to be shared. Note that the determination of the claim for such division is subject to a rather complex procedure, which is beyond the scope of this publication. The statutory regime may be modified (within certain limits) by a marriage contract or by a contract between the partners of a registered same-sex partnership (see Section 8.4).
- ▶ Upon formal agreement (by marriage contract or by a contract between the partners of a registered same-sex partnership), which has to be implemented by notarial deed, the spouses and the partners of a registered same-sex partnership may elect one of two contractual matrimonial property regimes, which may be further modified (within certain limits) by the contract as well.
- ▶ Separation of property (*Gütertrennung*): under this regime, each spouse or partner of a registered same-sex partnership holds his or her property independently in separate ownership. Management and disposal are not subject to any limitations deriving from the marital status.
- ▶ Community of property (*Gütergemeinschaft*): under this regime, all assets become the joint property of the spouses or the partners of a registered same-sex partnership (common property). Immediate joint ownership is also presumed for any assets acquired by each spouse or partner of a registered same-sex partnership during the marriage or the partnership while this property regime is in force. Assets that cannot be transferred by legal transaction do not become common property (*Sondergut*). Within the marriage contract or the contract between partners of a registered same-sex partnership, the spouses or the partners can agree to exclude certain assets from common property (*Vorbehaltsgut*). Assets acquired on inheritance at death or by gift are also excluded if so stipulated by the decedent or the donor.



Germany

8.4 Intestacy

A will is a legal document that regulates an individual's estate after his or her death. Germany will normally accept the formal validity of a will drawn up under the laws of the deceased's domicile, nationality and place of residence at the time the will is made or at the time of death. Whether an individual has the personal legal capacity to make the dispositions in a will is generally governed by the law of the deceased's citizenship.

If there is no valid will at his or her death, the deceased's estate passes under predetermined rules known as intestate succession. Where there are cross-border issues, the Conflicts of Law provisions will be relevant.

A system of succession per stirpes governs intestate succession that divides the possible intestate heirs into different orders depending on the relation to the decedent, while the closest applicable order excludes the more distant orders.

1st order	Spouse, or partner of a registered same-sex partnership and children
2nd order	Parents and their descendants
3rd order	Grandparents and their descendants
4th order	Great-grandparents and their descendants
Further heirs	More distant relatives and descendants
No heirs	State

Within the first three orders, a system of per-stirpes distribution and lineal heirs applies. Note that the intestacy rules are partially influenced by the matrimonial property regime. To simplify the depiction, "spouse" refers to "spouse or partner of a registered same-sex partnership" in the following table.

Statutory regime	Spouse and 1 child* survives	Spouse and 2 children* survive	Spouse and 3 children* survive
Community of accrued gain	Spouse: one-quarter + one-quarter	Spouse: one-quarter + one-quarter	Spouse: one-quarter + one-quarter
	Child: one-half	Children: one-quarter each	Children: one-sixth each
Separate property	Spouse: one-half	Spouse: one-third	Spouse: one-quarter
	Child: one-half	Children: one-third each	Children: one-quarter each
Community of property	Spouse: one-quarter	Spouse: one-quarter	Spouse: one-quarter
		Children: three-eighths each	Children: one-quarter each

*Children of a predeceased child of the intestate parent take their parent's share.

In the event that only the spouse or the partner of a registered same-sex partnership survives (no children), the surviving spouse or the partner of a registered same-sex partnership is entitled to one-half of the estate if relatives of the second order or grandparents of the decedent are still alive at that time, and is entitled to the whole estate if only more distant relatives of the decedent are alive.



Germany has concluded estate tax treaties with the following countries:

- ### Additional reading materials

EY GmbH/BDI, *Die Erbschaftsteuerreform* Berlin: STOTAX Stollfuß Medien, 2009.