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By PwC Deutschland | 08. März 2023

No limited inheritance tax liability in the event of acquisition by bequest

According to a decision of the Supreme Tax Court real estate located in Germany can be passed on tax-free if the testator grants the beneficiary the real estate by means of a foreign bequest (legacy). Provided, however, neither the testator nor the beneficiary is German citizen, and both live abroad.

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Background

The decedent, who died in 2013, had lived in Switzerland until her death. In her will she bequeathed a piece of real estate in Munich to her niece, the plaintiff, who lived in the USA. In 2014, the bequest was fulfilled, and the plaintiff was entered in the land register as the owner of the property. The tax office assessed inheritance tax as a result of the transfer of the property by way of a gift. The plaintiff, on the other hand, believed she did not owe any tax because of her foreign domicile and therefore contested the limited German tax liability asserted by the tax office. The appeal was rejected by the Munich Tax Court as court of first instance.

Decision

The Supreme Tax Court confirmed the arguments of the plaintiff. If a testator living abroad bequeaths domestic real estate to a person also living abroad, the foreign beneficiary does not have to pay German inheritance tax. (Note: here one must distinguish between a legatee and an heir; a legacy does not make the recipient an heir.) Unlike German citizens and persons with residence or permanent abode in Germany, foreign heirs or legatees are liable to pay tax only to a limited extent. They pay inheritance tax only on the acquisition of ownership of certain legally defined assets, including, in principle, domestic real estate. However, exemption from inheritance tax applies if they are bequeathed such real estate through a legacy in the testator's will.

In this respect, there is sort of a legal loophole because in the case of a legacy/bequest, the beneficiary does not acquire the property itself, but only a claim to the transfer of ownership of this property. The transfer of ownership must then take place separately afterwards and requires notarization. The situation is different if foreign heirs receive domestic real estate as part of the statutory succession. In this case, ownership of the domestic real estate passes directly to the foreign heir upon the death of the foreign testator. German inheritance tax is then due.

As pointed out in the press release published by the Supreme Tax Court the tax-free acquisition of domestic real estate by means of foreign bequests might prove to be a legally valid arrangement. However, it should be observed that, since 2015 and the entry into force of the EU Regulation (EU) No 650/2012 on matters of succession and on the creation of a European Certificate of Succession, caution is required in cases of inheritance in other EU countries: In certain EU countries, e.g. Poland, a bequest has a direct effect. Hence, the person benefiting from the bequest/legacy would also directly inherit the ownership of the domestic real estate. Tax-free acquisition of domestic real estate would then not be possible.

Source

Supreme Tax Court, decision of 23 November 2022 (II R 37/19) published on 28 February 2023.

Schlagwörter

limited inheritance tax liability