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Amount of tax-free allowance on transfer of assets to family foundation

In a most recent decision, the Supreme Tax Court held that great-grandchildren could also be potential beneficiaries of assets transferred to a family foundation for inheritance and gift tax purposes. They would be the „most distant beneficiary“ according to Section 15 para. 2 of the Inheritance and Gift Tax Act even if they have not yet been born at the time the foundation is established.

Background

Inheritance and gift tax is a tax levied on lifetime gifts and on transfers of value passing on death. This tax is imposed on transfers if testator/donor and/or heir/donee is a German tax resident. Progressive tax rates of 7% up to 50% and tax-free amounts between EUR 20,000 and EUR 500,000 apply, depending on the value and the tax bracket (tax class) which is applied based on the degree of the relationship between testator/donor and beneficiary. According to Section 7 (1) no. 8 sentence 1 Inheritance Tax and Gift Tax Act (IGTA), the transfer of assets to a foundation is deemed to be a taxable gift inter vivos.

Case of dispute

Together with her husband, the plaintiff set up a family foundation. The purpose of the foundation was to ensure adequate provision for the plaintiff and her husband, adequate financial support for the daughter born to the founders and adequate financial support for other descendants of the founders.

With respect to the transfer of assets to the family foundation, the tax office considered the “most remote beneficiaries” within the meaning of Section 15 (2) sentence 1 IGTA to be the “further descendants” listed in the foundation's articles of association. Therefore, the provision on the tax class pursuant toSection 15 (2) IGTA should be applied in the case of dispute, with the effect that the tax rate shall be based on the relationship of the most distant beneficiary to the testator or donor in accordance with the foundation deed. As a result, the tax office considered a tax free allowance of EUR 100,000 based on tax class I („for descendants of the children and stepchildren“) as opposed to the amount claimed by the plaintiff of EUR 400,000.

The tax court of first instance has dismissed the appeal brought by the plaintiff.

Decision

The Supreme Tax Court confirmed the view of the Tax Court of Lower Saxony and rejected the appeal of the plaintiff altogether.

The term "most distant beneficiary" is meant to identify a person who - in accordance with the foundation statutes - is potentially (!) entitled to benefits from the foundation and thus also includes a possible grand-children generation. It is of no relevance if the current beneficiary is related to the donor. The wording of the foundation's purpose in the respective foundation statutes alone is decisive.

The plaintiff felt that the most distant beneficiary was first her daughter, as she was still alive, and grandchildren had not yet been born. Therefore, a tax-free allowance of €400,000 should be considered when assessing the tax. The Supreme Tax Court disagreed by noting that the most remote beneficiary does not necessarily have to be born at the time of the transfer of assets to a family foundation. Nor does it matter whether possible great-grandchildren will ever actually receive financial support from the foundation.

The definition of the “most remote beneficiary” is to be interpreted as the person who is potentially to receive financial benefits from the foundation in accordance with the foundation statutes.

Reference:

Supreme Tax Court, judgment of 28 February 2024 (II R 25/21), published on 30 May 2024.

Schlagwörter

beneficiary, family foundation, inheritance and gift tax