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By PwC Deutschland | 31 January 2018

RETT-Blocker: Indirect unification of shares through an intermediary partnership

The Supreme Tax Court has decided that where an intermediary partnership holds direct or indirect interests in a real-estate-owning company, the relevant holding for establishing its interest in the related real-estate holding company, is its interest in the capital of the partnership and not the interest in the jointly owned property according to the law of property.

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Thus a share acquisition through an intermediary partnership can lead to a unification of shares within the meaning of the Real Estate Transfer Tax Act (“RETT Act”), if at least 95% of the share in the capital of the partnership is subsequently to be allocated to the purchaser.

Background

The question before the Court was whether the share acquisition of the appellant, a British limited company, had led to a unification of shares for Real Estate Transfer Tax (“RETT”) purposes. The appellant acquired all the shares in A AG in March 2005. The A AG held 100% in another British limited company which in turn held 100% of the shares in B Holding.

In December 2004, prior to the acquisition of the group by the appellant, B Holding had transferred, as a capital contribution, a 5.09 % share in D GmbH to a newly established limited partnership C KG. B Holding held a 100% interest in C KG as the limited partner, whilst the general partner C GmbH held 0%. B Holding held 94.04% in the general partner C GmbH with the remaining 5.96% being held by a bank.

After the December 2004 transfer B Holding held 94.04 % in D GmbH and C KG held 5.06%. D GmbH held real estate in Germany and also a 99.99958% interest in E AG. The remaining interest in E AG was held by A AG. E AG itself held real estate and also had shareholdings of at least 95% in a large number of companies and partnerships, which likewise owned real estate in Germany.

Tax authorities assumed an abuse of law

Based upon the shareholder structure the tax authorities took the view that the acquisition of shares in A AG by the appellant had led to a unification of shares within the meaning of the RETT Act (i.e. leading to a charge to RETT). According to the tax authorities, no commercial reason or any other important reason was evident for the establishment and interpolation of the C KG, so that an abuse of law had to be assumed.

The appellant’s appeals against this decision were unsuccessful at all instances. The Supreme Tax Court found that where domestic real estate belonged to the assets of an entity, a legal transaction, which established the right to the transfer of one or more shares in the entity, is subject to RETT where at least 95% of the interests in that entity are unified either directly or indirectly in the hands of the purchaser. The direct or indirect unification of at least 95% of shares in the entity will also give rise to RETT where no transaction giving rise to a legal obligation has preceded the unification.

The charge to tax only arises through the acquisition of the last share. The transaction, which leads to the acquisition of this share, is indeed the moment which triggers the tax. However, the subject of taxation is not the share acquisition per se, but rather the attribution of at least 95% of the shares into one hand which is its consequence. Thus the person in whose hands the shares are united as a result of the share acquisition will

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be treated for RETT purposes as if he had purchased the real estate from the entity whose shares are united in his hands.

Change in judicial precedent

This judgement represents a tightening of the rules and a change in the Court's precedent set in its decision of 8 August 2001 (II R 66/98), in which it held that in the case of a partnership, in which another entity has a share, the jointly owned interest in the partnership assets should be the basis for the allocation of the shares in the other entity. This meant that, as in the case of a company, the level of the interest held was relevant.

The introduction of "beneficial interest" as basis for RETT in the amended RETT Act was intended in particular to bring acquisition processes using the so-called RETT Blocker into the RETT net. The new rule therefore applies to direct and/or indirect interests in the capital or in the assets of an entity. This does not mean that interests according to the law of property apply, rather all interests in the capital or in the assets of an entity are to be considered proportionately regardless of legal form. The introduction of the new rules does not mean that for earlier periods share acquisitions through an intermediary partnership should not be considered as part of the interest in the entity's capital, as they are for an intermediary company. To this extent indirect interests in real-estate-owning entities are to be treated the same regardless of the legal form.

Source:

Supreme Tax Court decision of 27 September 2017 (II R 41/15) published on 24 January 2018.

Keywords

RETT, Taxation of real estate, unification of shares