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Inheritance Tax for legacy given on condition precedent

If spouses set up a bequest in the form of a so-called Berlin will (Berliner Testament) for children who do not claim their compulsory portion upon the death of the first deceased, the surviving spouse as the heir of the first deceased cannot deduct the bequest as a liability, as the bequest is not yet due. In a recent ruling, the Supreme Tax Court also held, that the child as successive heir must pay inheritance tax on the final legacy as it originates upon the death of the surviving spouse.

Background

Under the so-called “Berlin will” - Section 2269 of the German Civil Code (BGB) - spouses mutually appoint each other as sole heirs and specify that the children only inherit after the death of the second spouse, the children are thus designated as final heirs. The assets of the first deceased are initially transferred completely to the surviving spouse. Hence, in the second case of inheritance the children only become heirs of the last deceased and not also heirs of the first deceased. A special contractual provision (clause) known as “*Jastrowsche Klausel*” (Jastrow clause) offers a way of structuring joint wills or inheritance contracts to prevent the assertion of compulsory portion claims as far as possible. Children who demand their compulsory share after the first person dies will also be given the compulsory share for the second inheritance (so-called compulsory share penalty clause).

This might have negative tax implications, depending, i. a., on the degree of the relationship between testator/donor and beneficiary, on the amount of the personal tax-free allowance and the amount of connected liabilities deductible from the bequest received.Such adverse effects were claimed by the plaintiff in a case on which the Supreme Tax Court now rendered its final judgment.

In the **case of dispute**, the plaintiff's parents initially drew up a so-called Berlin will. The couple named the plaintiff and three of her sisters as heirs of the surviving spouse. A brother and another sister were disinherited. In addition, the will contained the above mentioned *Jastrowsche Klausel*. The disinherited siblings of the plaintiff claimed their compulsory share after the death of the first deceased father. The plaintiff accordingly received claim for the legacy upon the death of her father, which became only due upon the death the mother. After the mother had died, the tax office assessed inheritance tax against the plaintiff for the bequest after the mother. The prior bequest (upon the death of the father) was neither added to the acquisition nor deducted as a liability of the estate. The plaintiff, on the other hand, was of the opinion that the bequest had been added to her acquired assets twice and was therefore deductible as a liability from the assessment basis. The Tax Court of Hamburg had rejected the appeal.

Supreme Tax Court decision

The Supreme Tax Court confirmed the decision of the Hamburg tax court and rejected the plaintiff’s appeal. **In detail:** The value of the legacy was initially taxed after the death of the father with the mother as his sole heir. As the heir of the first deceased, the mother could not deduct the bequest as a liability of the estate when received as the bequest was not yet due (because the legacy was given on a condition precedent – so called “*betagtes Vermächtnis*”). The child as subsequent heir must pay tax upon the death of the longer-living spouse. In the case of dispute, the plaintiff as the final heir was subject to inheritance tax on the legacy due after her mother. Only at this point in time was she able to deduct the earlier bequest as a liability.

Since the bequest in the case of dispute had already arisen at the time, but only became due upon the mother's death, the father's estate was transferred to the mother in its entirety, i.e. including the assets from which the bequest was to be fulfilled. The bequest was therefore only subject to taxation once for the

plaintiff.

As to **the amount of liabilities** linked to the inheritance the Supreme Tax Court noted the following: The legacy given on a condition precedent corresponded to the statutory inheritance share after the death of the father, the liability from the bequest being equal to the amount which the deceased mother had incurred. The latter amount was higher - also per individual heir, because four heirs were still alive at the time - than the contingent legacy given to the three living heirs. Therefore, both amounts (the attributed legacy and the liability to be deducted) were not identical.

In its **press release** the Supreme Tax Court **summarized the tax effects** of the case in brief: The fact that inheritance tax arises twice with regard to the legacygiven on a condition precedent – i. e. once (without the possibility of deduction as an estate liability) for the mother after the death of the father and second for the plaintiff after the death of the mother - is admittedly unfavorable for the taxpayers, but from a legal point of view not to be questioned. It comes as a result of the use of the *Jastrowsche Klausel*, which - in order to provide the surviving spouse with sufficient liquidity - allows the bequest to accrue on the death of the first deceased spouse, but only become due on the death of the longer-living spouse.

Despite everything, the value of the legacy is in fact subject to tax twice, first for the surviving spouse, where the legacy is included in the taxable acquisition without the possibility of a deduction of liabilities, and secondly for the plaintiff as legatee at the time the legacy falls due.

Reference:

Supreme Tax Court, judgment of 11 October 2023 (II R 34/20), published on 27 February 2024.

Keywords

double charge, inheritance tax