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By PwC Deutschland | 19 November 2024

Inheritance tax: Tax-free amount in case of parent deemed deceased under civil law

German Civil Code in Section 2346 provides for a fiction of pre-death inasmuch as the person renouncing is excluded from intestate succession as though he or she had no longer been alive at the time of the devolution of the inheritance. The grandson of the deceased (the plaintiff) who had invoked this provision claimed the higher tax-free amount of €400,000 upon the inheritance. To no avail, as the Supreme Tax Court held in a most recent decision.

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Background

As regards the Inheritance, estate, and gift taxes progressive tax rates of 7% up to 50% and tax-free amounts between €20,000 and €500,000 apply, depending on the value and the degree of the relationship between testator/donor and beneficiary. According to the specific provision in Section 16 (1) No. 2 of the **German Inheritance and Gift Tax Act** (IGTA) the transfer to the children of deceased children (...) remains tax-free in an amount of EUR 400,000. To put it in another way, this is the allowance that would have been granted to the grandson if his father had already been dead.

Section 2346 (1) of the **German Civil Code** specifies that relatives and the spouse of the testator may renounce their right of intestate succession by contract with the testator. The person renouncing is excluded from intestate succession as though they had no longer been alive at the time of the devolution of the inheritance; they do not have a right to a compulsory share.

In**the case of dispute**, the plaintiff's father had waived his statutory inheritance rights towards his own father - the plaintiff's grandfather - by contract. Under civil law the father was therefore deemed to be deceased and was not entitled to a compulsory share pursuant to Section 2346 (1) Civil Code.

When the grandfather died, the plaintiff, i.e. his grandson, became the legal heir. He therefore applied to the tax office for the aforementioned tax-free amount of € 400,000. However, the tax office only granted the plaintiff a tax-allowance of € 200,000, i.e., the allowance to which he was entitled as a grandson after his deceased grandfather as his own father had waived his statutory share of the inheritance but was still alive when his grandfather died (Section 16 (1) No. 3 IGTA).

In contrast, the plaintiff believed he was to be regarded as the „child of a deceased child“ due to the fiction of predeath under civil law as stipulated in Section 2346 (1) sentence 2 Basic Law according to which the renouncing father is treated as if he was no longer alive at the time of the inheritance after the death of the testator.

The action before the tax court of first instance was not successful.

Decision

The Supreme Tax Court agreed with the opinion of the lower tax court and dismissed the plaintiff's claim as unfounded.

The wording of Section 16 (1) No. 2 alt. 2 IGTA, which grants the higher tax-free amount of € 400,000 in the circumstances specified therein, is unambiguous. It entitles “children of deceased children” to claim the higher tax-free amount.

The rules for granting the inheritance tax allowances are intended to favor the descendants of the first generation (children). In the case of grandchildren the legislator has not considered the family ties to be that close and grants a lower tax-free amount (€200,000).

The legislator did not intend to extend the higher tax-free allowance to children who are only deemed

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deceased by law but who are still alive at the time of the grandparent's death. The preferential (higher) allowance is not appropriate if the deceased's descendant is still alive and can continue to provide for the financial needs of his or her child, i.e. the deceased's grandchild. In addition, the child who is excluded from statutory succession can continue to inherit by will upon the death of their parent and then claim his or her own tax-free amount as a child of €400,000. A situation where the grandchild was also entitled to the higher tax-free amount would be a type of legal tax avoidance by obtaining a double benefit which is not intended by law.

Source:

Supreme Tax Court, decision of 31 July 2024 (II R 13/22) – published on 14 November 2024.

Keywords

inheritance tax allowance