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Changes of shareholders in a property-owning partnership

When determining whether a corporation with a direct interest in the partnership owning real estate is considered a new shareholder within the meaning of Section 1 (2a) sentence 4 of the Real Estate Transfer Tax Act because at least 90% of the shares are transferred to new shareholders, only the shareholding in the corporation must be taken into account. In a most current judgment, the Supreme Tax Court held that a previous participation of the new shareholder of the corporation in the partnership owning the real estate is irrelevant in this respect.

Background

Section 1 (2a) sentence 1 and 4 RETT Act: 1 Where a partnership owns a domestic site (property) and where partnership changes over a ten-year period (formerly, as in the case of dispute: five-year period) lead to at least 90 per cent (formerly, as in the case of dispute: 95 per cent) of the capital falling directly or indirectly to new partners, the ownership of the site shall be deemed to have been transferred to a new partnership.**4** A corporation with a direct shareholding is deemed to be a new shareholder in its entirety if at least 90 percent (95 per cent) of its shares are transferred to new shareholders.

The case of dispute: The ownership of the plaintiff (a limited partnership) until 31 Dec 2016 was as follows: T, among others, was a general partner without a capital interest. As limited partners, R held 10 % and R-GmbH 90 % of the shares in the plaintiff. The sole shareholder of R-GmbH was R. He held the shares in R-GmbH in trust for L-AG based in Switzerland.

With effect of 31 December 2016, R transferred his 100% shareholding in R-GmbH to T. T undertook to assume R's position as trustee with the result that T subsequently held the shares in R-GmbH in trust for L-AG. At the same time, R transferred his 10% shareholding as a limited partner in the plaintiff to M-Verwaltungs-GmbH as of 31 December 2016.

As trustee, A-AG held a 100% interest in B-GmbH on behalf of the plaintiff as trustor. On a lower-tier level, i. e. via C-GmbH, there were 100% shareholdings in E-GmbH and F-GmbH, each of which held real estate.

The tax office assumed that the change in the plaintiff's shareholder structure due to the transfer of the 100% shareholding in R-GmbH from R to T along with the replacement of the trustees was subject to real estate transfer tax with regard to the shareholding in the property-owning plaintiff. The appeal before the Tax Court of Lower Saxony was successful. In the opinion of this court, the acquisition by T of all shares in R-GmbH, which held a limited partnership interest in the plaintiff, did not trigger real estate transfer tax. T was „not a new shareholder“ within the meaning of Section 1 (2a) sentence 1 RETT Act as he had been a general partner in the plaintiff for more than five years.

Decision

The Supreme Tax Court granted the appeal, overturned the decision of the lower tax court, and referred the case back for a different hearing and final decision.

Contrary to the opinion of the tax court, the transfer from R to T of all shares in R-GmbH which held a 90% direct interest in the plaintiff as a limited partner, results in R-GmbH to be regarded in full as a new shareholder of the plaintiff within the meaning of Section 1 (2a) sentences 1 and 4 RETT Act. This, and in conjunction with the simultaneous transfer of the 10% shares in the plaintiff from R to M-Verwaltungs-GmbH, directly and completely changed the plaintiff's shareholder structure as foreseen in Section 1 para. 2a sentence 1 RETT Act.

When determining whether a corporation with a direct interest in the property-owning partnership is to be considered as a new shareholder only the interest in the corporation is to be taken into account. A transparency or “look-through approach”, which was equally possible for partnerships and corporations in indirect structures from an economic point of view prior to the 2015 Tax Amendment Act, was no longer possible according to the version of Section 1 para. 2a RETT Act as applicable in the year of dispute.

Accordingly, “new shareholders” are persons who did not previously hold an interest in the corporation. A previously existing shareholding of a new shareholder of the corporation in the property-owning partnership is not decisive. Even if the new shareholder in the corporation was already a shareholder of the property-owning partnership before acquiring his share he does not qualify as an existing shareholder of the corporation for the application of Section 1 (2a) sentence 4 RETT Act.

Finally, the Supreme Tax Court was not able to determine, based on the findings of the lower tax court, whether all the properties named in the disputed assessment notification belonged to the plaintiff: Not only properties included in the assets of the plaintiff were listed in the notice but also properties that were part of the assets of the plaintiff's subsidiaries.

Note: New rules were brought about in the course of the Tax Amendment Act 2015 regarding the taxation of indirect ownership changes in partnerships for real estate transfer tax (“RETT”) purposes (Sec. 1 (2a) RETT-Act) Real Estate Transfer Tax Act.

In an earlier (pre-2015) decision, the Supreme Tax Court has held that hat an indirect change in the shareholdings in the members of a real estate partnership was less than a complete change of interest in the partnership. With its decision the court has confirmed its case law regarding share transactions made prior to the enactment of the Tax Amendment Act 2015 (see our [blog post of 6 December 2020](#)). For transactions prior to the entry into force of the changes in Section 1 (2a) RETT Act under the 2015 Tax Amendment Act, indirect structures at all levels of participation by corporations and partnerships could be taken into account equally (by taking a „look-through approach“ from an economic point of view). This is no longer possible for transactions after 5 November 2015.

Takeaway: Although this judgment was based on Section 1 (2a)RETT Act as revised by the 2015 Tax Amendment Act (95% threshold and five-year monitoring period), it should also be relevant for the currently applicable version of Section 1 (2a) RETT Act (90% threshold and ten-year monitoring period) and for the similar provision of Section 1 (2b) RETT Act that applies to corporations.

Source:

Supreme Tax Court, judgment of 31 July 2024 (II R 28/21) published on 12 December 2024.

Keywords

limited partnership, real property