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Germany

PRIVATE CLIENT

Contributing firm

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This country-specific Q&A provides an overview of private client laws and regulations applicable in Germany.

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GERMANY PRIVATE CLIENT



1. Which factors bring an individual within the scope of tax on income and capital gains?

Tax liability in Germany is determined by the concept of residence. An individual is a German resident for tax purposes if he or she has either a permanent home or a habitual abode in Germany. An individual has his or her permanent home in Germany, if he or she maintains a dwelling in Germany under circumstances indicating that he or she will maintain and use such dwelling. An individual's habitual abode is at the place where he or she stays under circumstances which allow the assumption that the stay is not only temporary. Generally, a person is deemed to have a habitual abode in Germany if he or she spends more than six months in Germany without any significant interruptions. The worldwide income and assets of individuals whose tax residence is located in Germany are subject to income tax. German tax law considers capital gain to be a source of income. Thus, the same applies to capital gains.

2. What are the taxes and rates of tax to which an individual is subject in respect of income and capital gains and, in relation to those taxes, when does the tax year start and end, and when must tax returns be submitted and tax paid?

Income tax covers income from seven sources:

- income from agriculture and forestry;
- income from trade or business;
- income from self-employment;
- income from employment (salaries and wages);
- income from capital and capital gains;
- income from letting property, especially real property and groups of assets; and
- other income (e.g., income from a pension or leases of movable assets).

The tax rate ranges from 14 to 45 percent progressively with the exception of income from capital and capital gains (see question 3). A solidarity surcharge of 5.5 percent of the tax due was also levied until January 2021. This surcharge was intended to finance the German reunification of 1990. Effective January 1st 2021, the exemption limits were raised to such an extent that only high income earners now pay the solidarity surcharge as well as investors who have exhausted their savings allowance. Corporate tax subjects will not benefit from this tax relief and it will also still apply to capital gains tax.

Unless in case of a withholding tax (see question 3), taxpayers must make advance payments on the 10th of March, June, September and December.

The tax year is the calendar year. Tax returns must be submitted by 31st of July of the following year. However, if the taxpayer is represented by a tax advisor, the deadline is generally prolonged until February 28th of the year after that. For tax returns for 2020, a deadline extension of 3 months applies in principle, meaning the general filing deadline ends on 31st October 2021, whereas for advised taxpayers it ends on 31st May 2022. The interest run will be adjusted accordingly.

3. Are withholding taxes relevant to individuals and, if so, how, in what circumstances and at what rates do they apply?

Income from employment and capital is subject to a withholding tax. Whereas income from employment is taxed at the regular progressive rate (see question 2), income from capital is taxed at a flat rate of 25 percent plus solidarity surcharge. Typically, salaries and wages as well as the distribution of corporate gains (dividends) trigger withholding tax.

4. How does the jurisdiction approach the

elimination of double taxation for individuals who would otherwise be taxed in the jurisdiction and in another jurisdiction?

Germany has signed so-called double taxation agreements with 96 countries as bilateral measures to avoid double taxation for income tax purposes. In addition, double taxation agreements exist with Switzerland, Greece, Sweden, the USA, Denmark and France concerning inheritance and/or gift taxes. Subordinately Germany has taken unilateral measures to credit foreign taxes (§ 34c EStG).

5. Is there a wealth tax and, if so, which factors bring an individual within the scope of that tax, at what rate or rates is it charged, and when must tax returns be submitted and tax paid?

In 1995, the Federal Constitutional Court declared the wealth tax unconstitutional and repealed it at the beginning of 1997. However, proposals to reintroduce the wealth tax have been discussed repeatedly since then.

6. Is tax charged on death or on gifts by individuals and, if so, which factors cause the tax to apply, when must a tax return be submitted, and at what rate, by whom and when must the tax be paid?

Transfers by death or gifts are subject to the German inheritance and gift tax (IGT). The tax rates range from 7 to 50 percent, depending on the relationship between the transferor and the transferee, and the value of the share of the estate received. Spouses and descendants pay IGT at a rate of 7 to 30 percent. Transfers between most other relatives are taxed at a rate of 15 to 43 percent. Between unrelated persons, the applicable tax rate is 30 or 50 percent (for more than € 6 million).

The following tax-free allowances apply if either the transferor or the transferee is a resident in Germany:

- spouses receive a personal allowance of € 500,000 and a maintenance allowance of up to a maximum of € 256,000; and
- descendants receive a personal allowance of € 400,000 and an age-dependent maintenance allowance of up to € 52,000.

IGT applies if either the transferor or the transferee is a

resident in Germany. It must be declared and paid upon request by the fiscal authorities. However, the transferee is required to inform the authorities about the transfer within three months. Each transferee is liable for IGT on the value of the assets transferred, regardless of his or her personal wealth. In case of a gift, the transferor must inform the authorities and is liable for IGT as well, even though the transferee is to be charged primarily.

7. Are tax reliefs available on gifts (either during the donor's lifetime or on death) to a spouse, civil partner, or to any other relation, or of particular kinds of assets (eg business or agricultural assets), and how do any such reliefs apply?

There is no IGT on a lifetime transfer of the family home to a spouse and on an equalisation of the gains accrued during the course of a marriage, where the statutory matrimonial property regime of the community of surplus (as provided for by the German matrimonial regime or a similar foreign regime) applies.

Additionally, IGT relief applies when transferring business assets. The transferee can generally choose between the basic relief and the optional relief model. According to the basic relief, up to 85 percent of the business assets do not form part of the tax base. If the taxpayer chooses the optional relief, up to 100 percent of the business assets are not considered part of the tax base. The amount of relief depends on the value of the transferred business assets. The relief is, however, conditional upon the continuing operation of the business for five or seven years (depending on whether basic or optional relief apply) and the preservation of jobs. Regarding the preservation of jobs, depending on the relief model chosen and the number of employees, after the retention period, the total payroll has to amount to at least 250 to 700 percent of the payroll before the transfer. Passive non-operating assets are exempt from the IGT relief. This includes for instance leased real estate, minority shareholdings of 25 percent or less, securities, certain movables like artworks, antique cars and yachts, and liquid funds if they exceed, after deduction of debt, 15 percent of the total value of the business assets. These passive non-operating assets are fully taxable at the regular rate, so far as their value exceeds 10 percent of the total business assets.

8. Do the tax laws encourage gifts (either during the donor's lifetime or on death) to a charity, public foundation or similar

entity, and how do the relevant tax rules apply?

Donations to charitable foundations or other charitable organisations can be deducted from income resp. corporate and trade tax if certain requirements are met.

Deductibility for donations is limited to 20 per cent of the total annual income or 4 per thousand of the total turnovers and for wages and salaries spent in the business year.

Donations to political parties are subject to special maximum amounts.

9. How is real property situated in the jurisdiction taxed, in particular where it is owned by an individual who has no connection with the jurisdiction other than ownership of property there?

A real estate transfer tax with differing regional rates ranging from 3.5 to 6.5 per cent applies to:

- the acquisition of residential real property; and
- the acquisition of a substantial shareholding (at least 90 per cent) in a company holding residential real property.

Since the base for real estate transfer tax is the purchase price, no official valuation is necessary. Subject to the tax claim is, whoever is participating in the transfer.

The real estate transfer tax was reformed with effect from 01.07.2021. Significant changes include the lowering of the tax-relevant participation threshold for the transfer of shares to 90% (previously 95%) and the extension of the minimum holding period from 5 to 10 years, which applies to the transfer of shares as well as property.

An annual property tax may be due on the value of real property at the discretion of the relevant local authority.

Until now, this has been calculated by means of a fixed standard value. Recently, the Federal Constitutional Court ruled that the property values last determined in 1964 or 1935 are incompatible with the constitutional principle of tax equality. In order to maintain the property tax as an essential source of revenue for the municipalities, a reform was necessary. As a result, a new assessment basis for calculating the property tax was adopted. In the future, the assessment will be based

on the plot area, the standard land value, the type of property, the age of the building and the rent level, and is thus not intended to reduce the tax amount but merely to redistribute it. In particular, the reform also reintroduced the so-called 'Grundsteuer C', which is intended to apply to undeveloped but ready-to-build land and to counteract housing speculation.

In principle, the new regulations are nationwide, unless a federal state makes use of its right to independent regulation. These can still be introduced until the end of 2024; in 2025, the property tax will be measured according to the new law.

Ownership of the residential property establishes tax liability, regardless of the owner's residence.

10. Are taxes other than those described above imposed on individuals and, if so, how do they apply?

VAT applies to the net turnover of the entrepreneur at a tax rate of 19 per cent or 7 per cent (for certain tax-privileged turnover, e.g. food).

Any business operating through a permanent establishment in Germany, with the exception of independent personal services, is liable to trade tax. The tax rate is determined by the local authorities of the relevant municipality. However, trade tax may generally be credited against the individual's personal income tax.

Church tax is also levied on church members as a supplement to income tax. The tax rate varies between 8 and 9% depending on the federal state.

11. Is there an advantageous tax regime for individuals who have recently arrived in or are only partially connected with the jurisdiction?

Upon establishing residency in Germany, the taxpayer is generally considered fully tax liable. Therefore, the length of his stay is irrelevant for tax purposes. However under some circumstances, taxpayers fall under the regime of limited tax liability. This may occur, when the individual has neither a permanent home, nor a habitual abode in Germany, but gains income from a source (see question 2) from within Germany.

12. What steps might an individual be advised to consider before establishing

residence in (or becoming otherwise connected for tax purposes with) the jurisdiction?

In order to avoid IGT, any gifts should be made before any of the individuals involved establish residency in Germany. Due to the fact that an individual becomes subject to German income tax with his or her worldwide income, any income (in particular capital gains) should be realised before entering Germany in cases where the individual finds himself or herself in a more advantageous tax situation before his relocation. However, with regard to business assets or real estate, gains from the sale of these assets will, in many cases, not become taxable in Germany where a tax treaty with the state in which such property is situated is applicable.

13. What are the main rules of succession, and what are the scope and effect of any rules of forced heirship?

German law grants testamentary freedom. The testator is therefore free to choose his heirs and how his estate shall be distributed. He is, however, not obliged to make a Will. In that case, the legal rule of succession is as follows:

(each of the following categories precludes the subsequent heirs from receiving a share of the deceased's estate):

- children of the deceased and, subordinated, their descendants;
- parents of the deceased and, subordinated, their descendants;
- grandparents of the deceased and, subordinated, their descendants; and
- great-grandparents of the deceased and, subordinated, their descendants.

Relatives within a particular category inherit in equal shares (succession per stirpes).

There is a forced heirship regime. Descendants, spouses, civil partners and parents are entitled to make a monetary claim for a compulsory share of the deceased's estate if they are excluded from the testator's will or if the share granted to them is less than their compulsory share. A relative's compulsory share generally amounts to 50 per cent of the value of that relative's share on intestacy.

14. Is there a special regime for

matrimonial property or the property of a civil partnership, and how does that regime affect succession?

Three matrimonial regimes are possible:

- Under the community of accrued gains, the spouses' property does not become common property. However, accrued gains, that spouses acquire during the marriage are equalised if the marriage ends. The community of accrued gains regime applies, when there is no marriage contract in effect. This regime affects succession in that the surviving spouses share is increased by a quarter of the estate.
- The spouses can by contract agree on a separation of assets. The surviving partner's statutory share of the estate depends on the number of children the deceased had. In case of one child, the surviving partner inherits $\frac{1}{2}$, in case of two children, $\frac{1}{3}$, and more than two children he or she always inherits $\frac{1}{4}$. If there are no children, the surviving spouse will receive the legal share,
- In case of a joint property regime, which can also be agreed upon by contract, the deceased's spouses share in the common property remains part of the estate. Thus, general provisions apply.

15. What factors cause the succession law of the jurisdiction to apply on the death of an individual?

As of 17 August 2015, the conflict of laws rules of the EU Succession Regulation apply. They are valid in all EU member states except Denmark, Ireland and the United Kingdom. According to the Regulation, the deceased's habitual residence at the time of his or her death is relevant for the question of which succession law is applicable, instead of his or her nationality.

16. How does the jurisdiction deal with conflict between its succession laws and those of another jurisdiction with which the deceased was connected or in which the deceased owned property?

According to the EU succession regulation, if it is obvious that the deceased had a closer relationship to another state, that state's law will apply under certain circumstances. There is, however, the opportunity to opt for the succession law of an individual's nationality by a

Will, a joint Will or by an agreement as to succession. In addition, provisions on legal jurisdiction, recognition and enforcement of decisions and authentic instruments and on the European certificate of succession are part of the Regulation. As a general rule, the legal jurisdiction shall be determined by the habitual residence at the time the individual dies. The EU Succession Regulation is not applicable to trusts, hence the respective national conflict of law regime applies.

Even if the EU Succession Regulation does not apply directly vis-à-vis third states, from the German point of view its provisions with regard to the determination of the applicable law apply accordingly.

17. In what circumstances should an individual make a Will, what are the consequences of dying without having made a Will, and what are the formal requirements for making a Will?

There are two valid forms of wills: the holographic and the public will. The holographic will has to be handwritten, dated and signed by the testator. The public will has to be signed before and certified by a notary public. Neither form of will requires a witness. Should there be no Will or should a Will not meet the formal requirements, the statutory rule of inheritance applies (see question 13). An individual should make a Will, if he or she in any way does not wish to have the statutory rules of inheritance to be applied to his or her estate.

If an individual has no residency in Germany but owns residential property, he or she generally does not fall under German inheritance law (see question 15 and 16), so the formal requirements for making a Will can differ.

18. How is the estate of a deceased individual administered and who is responsible for collecting in assets, paying debts, and distributing to beneficiaries?

The deceased's estate is generally administered by the heirs. A testator can appoint an executor, who shall be responsible for executing the testator's testamentary dispositions. In case of such appointment, the executor has the power of disposal and the duty to effect a partitioning of the estate among the heirs.

19. Do the laws of your jurisdiction allow individuals to create trusts, private

foundations, family companies, family partnerships or similar structures to hold, administer and regulate succession to private family wealth and, if so, which structures are most commonly or advantageously used?

Trusts are generally not recognised in Germany as Germany did not ratify the HCCH Convention on the Law Applicable to Trusts and on their Recognition 1985. Structures commonly used in Germany to hold assets are corporations, partnerships and foundations.

20. How is any such structure constituted, what are the main rules that govern it, and what requirements are there for registration with or disclosure to any authority or regulator?

Corporations provide limited liability, as shareholders are not liable for the corporation's debts. A corporation must be registered in the German trade register, which generally provides a list of the shareholders. The register also contains information about the share capital and the directors.

There are various ways in which a partnership can be set up. Most kinds of partnerships need to be registered in the trade register as well. Further, in certain constellations partners must also be listed as ultimate beneficial owners in the transparency register.

Private foundations have no shareholders but endowment property. They are represented by a board. A private foundation can be voluntarily listed in the index of German Foundations and is listed in the register of the associated federal state (so-called 'Stiftungsverzeichnis'). According to the reform of the German law of foundations, a national register of foundations visible to the public will be installed as of 2026 (so-called 'Stiftungsregister'). Registration in the transparency register along with their beneficial owners is compulsory, as long as the foundation's registered office is within Germany. The reporting obligation does not apply to foundations under public law. Since the implementation of the 5th EU Money Laundering Directive there is an extended public access to the Transparency Register without the need for a legitimate interest. However, inspection is limited to certain data while public authorities and, in some cases, credit institutions and others have a full right of inspection.

21. What information is required to be made available to the public regarding such structures and the ultimate beneficial ownership or control of such structures or of private assets generally?

Besides type and scope of the relevant economic interest the transparency register must show the name, date of birth, nationality and place of residence of the ultimate beneficial owner. Previously, the transparency register only contained entries if there were no entries available in other registers, such as the trade register. In the future all companies must positively report their beneficial owners to the transparency register regardless of whether the company is already subject to reporting obligations under other public registers.

22. What is the jurisdiction's approach to information sharing with other jurisdictions?

The background to the expansion of the transparency register was the interconnection of all European transparency registers via a central European platform – the so-called Business Registers Interconnection System (BRIS). The BRIS system improves collaboration between the business registers of Member States and enables cross-border information sharing on corporate data. Germany transposed the European legal requirements into national law on 10.06.2021.

23. How are such structures and their settlors, founders, trustees, directors and beneficiaries treated for tax purposes?

A corporation is subject to German corporate tax, which amounts to 15 per cent plus solidarity surcharge. In addition, a trade tax is levied. A foreign corporation with income from German sources might be subject to German corporate tax. If a foreign corporation has a branch in Germany that constitutes a permanent establishment, the corporation will be subject to German corporate tax and trade tax on all income effectively connected to this permanent establishment. Distributions to shareholders are subject to income tax.

Partnerships are fiscally transparent in Germany for income tax purposes. The partners are subject to income tax at their individual tax rates plus the solidarity surcharge, whereby the new regulation of the solidarity surcharge with an increase in the exemption limits also leads to partial or even complete relief here (see question 2). If the partnership is engaged in trade or

business, the partnership itself is subject to trade tax. Trade tax levied from the partnership is (to a large extent) credited against the income tax of the partners if they are individuals.

Charitable foundations are tax privileged. The formation of a charitable foundation neither triggers any inheritance or gift tax, nor real estate transfer tax if real property is transferred gratuitously to the foundation. A charitable foundation is released from almost every current form of taxation, especially corporate tax and trade tax. In contrast, a family foundation is not tax-privileged. Taxation of a family foundation generally complies with the taxation of corporations, however, a family foundation can receive income not only from trade or business but any type of income. Distributions to beneficiaries are subject to income tax.

24. Are foreign trusts, private foundations, etc recognised?

Trusts are generally not recognised in Germany (see question 19). Income received by a foreign trust may be attributed to the settlor or the beneficiaries if they are German residents.

25. How are such foreign structures and their settlors, founders, trustees, directors and beneficiaries treated for tax purposes?

Even though trusts are not recognized, they can, however, trigger inheritance and gift tax in several ways. The establishment of a trust by residents or of a trust comprising assets located in Germany is considered to be a transfer of assets that is taxable in accordance with the Inheritance and Gift Tax Act. Distributions to beneficiaries during the trust period or on the trust's dissolution may trigger income tax, if the beneficiary is a German resident or if German situs assets are distributed. According to a recent ruling of the German Federal Fiscal Court distributions from a foreign family foundation to a German resident are only subject to German gift tax, if they are not in accordance with the purpose of the foundation as laid down in its statutes. Corporate tax can be triggered if income is received by a foreign trust from German sources. The worldwide income of a foreign trust may be subject to corporate tax if the trust's management is in Germany and if certain other conditions are met; for example, if the effective management of a trust is vested with a trustee resident in Germany. Undistributed income received by a foreign trust can be attributed to the settlor or the beneficiaries if they are German residents. In this case, it can be subject to the settlor's or the beneficiary's personal

income tax.

26. To what extent can trusts, private foundations, etc be used to shelter assets from the creditors of a settlor or beneficiary of the structure?

Where assets governed by foreign property law have been transferred to an irrevocable trust effectively formed under foreign trust law, the trust can shelter these assets from the settlor's or beneficiary's creditors.

Since private foundations are recognised, they generally are an appropriate means to shelter assets from creditors.

27. What provision can be made to hold and manage assets for minor children and grandchildren?

Minors can hold assets directly. In order to legally obtain an asset by contract from a parent or grandparent, a family court must typically appoint a legal guardian. Thereafter, it is generally the parents' duty to administer the asset.

Testators typically provide for executorship (see question 17) with regard to assets that are inherited by minors. For lifetime gifts, family companies can be used to control the minors' rights with regard to the assets, e.g. through golden shares for the donor.

28. Are individuals advised to create documents or take other steps in view of their possible mental incapacity and, if so, what are the main features of the advisable arrangements?

When a person loses mental capacity, generally a guardian has to be appointed to represent that person in all legal matters, under supervision by a court. This can usually be avoided by providing a valid power of attorney which empowers a person to full legal representation.

29. What forms of charitable trust, charitable company, or philanthropic foundation are commonly established by individuals, and how is this done?

There are three main forms of charitable organisations:

- Registered associations;
- Charitable foundations; and
- Charitable limited liability companies ("gGmbH").

Charitable organisations in Germany are fully tax privileged. Their recognition requires that the organisation's activities are dedicated to the altruistic advancement of the general public in material, spiritual or moral aspects. These purposes must be pursued altruistically, exclusively and directly

30. Have any specific tax policies or approaches been implemented, on a temporary or permanent basis, to take account of the Covid 19 pandemic?

As a result of the Corona pandemic, numerous tax law adjustments were made to relieve affected taxpayers. For example, tax payments could be deferred without interest until the end of September 2021. The enforcement of tax debts will be suspended and advance payments of income, corporate and trade tax can still be reduced. There have been no special regulations regarding tax remission due to the Corona pandemic. Tax balance sheets are sufficiently flexible, e.g. with the possibility of partial write-offs, and are therefore also precise in pandemic times. In many cases, the change in work processes has led to increased short-time work, which is also tax-exempt as a wage replacement benefit in the event of a top-up. In addition, there is the possibility of paying tax-free allowances to employees. As a result of the pandemic, VAT was also temporarily reduced (July 1st 2020 to December 31st 2020) from 19 to 16% and from 7 to 5% to strengthen the economy.

31. What important legislative changes do you anticipate so far as they affect your advice to private clients?

The most relevant legislative change in 2020 has been the implementation of Council Directive (EU) 2018/822 – commonly referred to as "DAC 6". The German legislator introduced obligations to report cross-border tax arrangements, if at least one EU member state is affected and the arrangement falls within one of the categories called "hallmarks".

The Act has retrospective effect. Any cross-border tax arrangement taking place after June 24th 2018 has to be reported. Arrangements that were implemented between June 24th 2018 and June 30th 2020 must be reported by August 31st 2021. All other cross-border arrangements are due to be reported within 30 days.

The duty of reporting arrangements primarily falls upon “intermediaries”. An intermediary is any person that promotes, designs for a third party, organizes, makes available for implementation or manages the implementation of a reportable cross-border arrangement. In case of such intermediary being bound by confidentiality (e.g. lawyers), he or she must inform other intermediaries or even the taxpayer himself about his duty to report the tax arrangement.

In addition, the modernisation of corporate income tax law will come into force on January 1st 2022 (so called ‘Gesetz zur Modernisierung des

Körperschaftssteuerrechts’ (KöMoG)). The main aim is to make it possible to tax commercial partnerships and partnership companies in the same way as a capital companies. This is intended to strengthen the competitiveness of family businesses. Amendments to the Reorganisation Tax Act are also intended to enable tax-neutral extended restructuring.

Besides that, the foundation reform and the reform of the law on guardianship and custodianship were decided this year but will not come into force until 2023. The corresponding changes are expected to have an impact on the advice given to private clients.

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