


Current issues surrounding German inheritance tax



The decision of the
German Federal
Constitutional Court
(„BVerfG“) of 17
December 2014 and
its consequences

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■ Agenda

1. Legal background
2. The content of the decision of the BVerfG of 17 December 2014
3. First reactions
4. Possible new regulations
5. Need for action

■ Legal background

The previous exemptions under sections 13a, 13b Inheritance and Gift Tax Act („ErbStG“)

	Regular exemption	Optional exemption
Amount of assets exempt from taxation	85%	100%
Retention period	5 years	7 years
Permissible portion of administrative assets	≤ 50%	≤ 10%
Total wages and salaries (with >20 employees)	400% of the initial wages and salaries, aggregated within the 5-year period	700% of the initial wages and salaries, aggregated within the 7-year period
Partial reduction of the exemption	400%, less the actual aggregated wages and salaries in per cent	700%, less the actual aggregated wages and salaries in per cent
Check	At the end of the 5-year period	At the end of the 7-year period

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The content of the decision of the German Federal Constitutional Court



Key considerations:

The privileges for business assets are **disproportionate**, in so far as they go beyond small and medium-sized enterprises without an **economic needs test**.

The **aggregate wages and salaries regulation** disproportionately privileges enterprises with up to 20 employees

The preferential treatment of up to 50 % **administrative assets** applies without any viable justification

The law allows for **tax planning**, which the Act does not aim to achieve and which cannot be justified under the principle of equality.

- Declaration of incompatibility of the current ErbStG with the Basic Law
- **Continued application of the ErbStG** and order for the legislator to legislate until **30.6.2016**

The content of the decision of the German Federal Constitutional Court

Details:

Economic needs test

- Large enterprises are not covered by the purpose of the Act
- Refraining from individual checks of SMEs by way of assessment by the legislator is justified
- The more extensive the exemption, the higher the justification requirements
- Therefore: no justification for large enterprises without an individual economic needs test

Aggregate wages and salaries

- The minimum of >20 employees results in 90 % of all enterprises to be exempt from the aggregate wages and salaries regulation.
- Central justifying element of safeguarding jobs ceases to apply.

Administrative assets

- „All-or-nothing principle” results in unequal treatment of enterprises with administrative assets of (just about) >50%.
- No justification for unequal treatment of other assets which cannot be treated preferentially.
- Wrong incentive to restructure business assets in order to exhaust the permissible portion of 50 %

Tax planning

- This includes in particular, the split of enterprises in order to avoid the obligation on total wages and salaries and the restructuring of administrative assets into corporate structures (as well as the “cash-GmbH”)
- The continued application of the rules does not result in a protection of legitimate expectations in case of a retroactive abolition of this

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First reactions

Urteil zur Erbschaftssteuer: Schäuble sendet Beruhigungsadresse an Firmenerben

Die Reaktionen auf das Urteil gegen Privilegien für Firmenerben reichen von Empörung bis Gelassenheit. Finanzminister Schäuble deutet es als Sieg um. Aus seiner Sicht geht es nur um ein paar Detailfragen.

Spiegel online on 17.12.2014

Erbschaftsteuer-Urteil
„Eine sozialpolitische
Kampfansage“
Stuttgarter Nachrichten on 18.12.2014

STANDPUNKT
Erbschaftsteuer hat Luft nach oben
Von Cansel Kiziltepe und Ralf Stegner
FAZ on 15.12.2014

Nur wenig Änderungen an Erbschaftssteuer

Minimalinvasiv und schnell soll die gerichtlich bestellte Reform der Erbschaftssteuer vonstatten gehen. So kündigt es zumindest Finanzminister Schäubles Abteilungsleiter Sell an. Einige Streitpunkte bleiben.

Handelsblatt on 8.1.2014

Schäuble schockt die Unternehmen Harte Bedürfnisprüfung in der Erbschaftsteuer geplant

FAZ on 24.2.2015

Assessment

- Intention of the Federal Ministry of Finance can be discerned, to swiftly undertake the reform and as compliant as possible with the decisions from Karlsruhe.
- In such a case, in particular the need for an **economic needs test** as postulated by the BVerfG opens the door to tightened rules.
- The possibility that further tax planning arrangements could be affected by retroactive legislation cannot be ruled out, but seems unlikely.
- At the moment, there seem to be some disagreements between the Federal Ministry of Finance on the one hand, and a few Ministries of Finance of the Laender on the other.

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Possible new regulations

Economic needs test for large enterprises: Who must be in need?

Enterprise	Acquirer
BVerfG: Object of protection is the enterprise (link to the SME-limits – arbitrariness?)	BVerfG: Possibility of linking it to the acquirer (contradiction in the ruling of the BVerfG)
Factual exemption of enterprises encompassed in the tax system	But: Preferential tax treatment of the acquirer
Economically: Inheritance tax is paid out of the business assets	Legally: Acquirer is the debtor of the tax
Immense difficulties in determining criteria for the economic needs test (investment rate, cash flow, rating, liquidity)	Possibility of including previous acquisitions, joint acquisitions, as well as other assets

Possible new regulations

Economic needs test:

Suggestion of the Federal Ministry of Finance:

- Focusing on the acquirer
- Fixed limit for the economic needs test (acquisitions of >20 Mio. EUR)
- 20 Mio. EUR represents a limit (and not a tax-free amount)
- If the limit is exceeded and there is no reason for exemption, in general, full tax liability arises (even if the business is continued and the jobs are safeguarded)
- In this case, the acquirer must use up to half of his disposable private assets for payment of the inheritance tax

■ Possible new regulations

No change of the valuation law

- Due to the regular award of (full) exemption, partial valuation has been of secondary importance in the past.
- The valuation rules (in force since 2009) regarding business assets have not been objected to by the BVerfG; accordingly, changes in the valuation law are not to be expected.
- The value impairing consideration of restrictions according to the company or partnership agreement continues to be missing.
- In case the exemption rules should be tightened, the valuation will in future become the central issue.
- Problems:
 - Multiplier in the simplified income capitalization approach to valuation (currently > 18)
 - Consideration of the deferred income tax

Possible new regulations – time frame

Transposition period

30 June 2016

(should not be exhausted; no retroactivity)

What happens, if, on 1 July 2016, no new Act has come into force?

- The decision makes clear, that a discontinuation of the exemption rules in accordance with sections 13a, 13b ErbStG in isolation, with the consequence, that all acquisitions would be taxed uniformly or, that business assets would be fully exempt, is unimaginable, since both outcomes would be incompatible with the will of the legislator.
- This implies, that, in this case, inheritance tax would be rendered inoperative altogether.
- In such a case, the BVerfG would have the option, to issue an injunction. Regarding the specific features of such an injunction, however, there is no clarity.

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■ Need for action

- Entrepreneurs, whose enterprises
 - have a **strong equity position** or **extensive administrative assets**,
 - employ **between 5 and 20 employees** and/or
 - **exceed the scope of small and medium-sized enterprises**,should complete the business succession before the new regulations come into force.
- Enterprises with a small number of partners or shareholders should take action.
- Proprietors of housing companies should take action.

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Practice Areas:

- Domestic and International Tax Law
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Personal data

- Bank apprenticeship
- Studied law in Konstanz, Cambridge (M.A., 1998), Hamburg, Yale (LL.M.; 1996), Regensburg (Ph.D.; 2000)
- Practice at a major international law firm in New York (1996-1997)
- Admitted to the bar in 2000, joined P+P Pöllath + Partners in 2001

Additional facts

- Managing director of the Berliner Steuergespräche e.V. (Berlin Tax Forum)
- Member of the advisory board of the Institute for Foundation Law at the Bucerius Law School
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- Mergers & acquisitions
- Business succession and wealth planning
- Expatriation taxation
- Advice for foundations
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Personal data

- Born in 1962
- Tax consultant since 1992
- Study of economics in Bamberg and Munich (1988 Diplom-Kaufmann, 1992 Dr. rer. pol.)
- Partner since 2013

Additional facts

- Since 2008 Honorary Professor at the Martin-Luther University of Halle-Wittenberg
- Chairman of the advisory board of the Institut der Steuerberater in Hessen e.V. (Institute of Tax Consultants)
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