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Residential portfolio and German inheritance/gift tax

Transfer of company property portfolios to successors on preferential rates or even tax-free where applicable

Extensive real estate portfolios are a major topic in inheritance and gift tax consulting, as the transfer of real estate assets can trigger large tax amounts and potentially force the acquirer to sell assets to pay the tax. However, under certain conditions, there is the possibility within the framework of a so-called housing company to transfer a business real estate portfolio to the successor with tax benefits or even tax-free. The housing company is subject to strict conditions, which the FG Münster addressed in a recent ruling dated October 10, 2024.

Why it could become increasingly difficult to meet the requirements of a housing company at this time and what implications arise for practice are outlined below.

The Basic Benefit Rules

For real estate rented for residential purposes, inheritance and gift tax law grants a relief of 10 percent in § 13d ErbStG. This means that only 90 percent of the real estate value is considered in the valuation and subject to taxation.

For business assets, on the other hand, reliefs of 85 percent under the regular exemption or even 100 percent under the optional exemption may be possible. Compared to private assets, there is generally a higher tax exemption.

In exceptional cases, companies that own exclusively rented apartments can also claim the high benefits for business assets. However, this requires that the company does not have too much so-called harmful administrative assets. This harmful administrative asset regularly includes properties that are leased to third parties. This can be a problem for real estate companies, as a result of which a benefit and thus a tax relief are excluded.

But: The legislator works here with an exception, which states that properties leased to third parties do not belong to harmful administrative assets if a housing company exists. With this regulation, the legislator wants to spare commercially active companies that also employ workers.



Requirements for a Housing Company

To benefit from this exception, all of the following three requirements must be met:

- The real estate belongs to a business asset,
- the main purpose of the business is the rental of apartments, and
- the activity requires an economic business operation.

The FG Münster had to particularly consider the third requirement and judge whether the operation of a housing company that provides certain additional services alongside rental requires an economic business operation or not.



Opinion of the FG Münster

The FG Münster decided that the requirements of the housing company must be interpreted narrowly and cannot be considered fulfilled simply because the leasing of properties is accompanied by offered, optional commercial services. It is rather important that the main purpose of the business is the rental of apartments, whose fulfillment requires an economic business operation. Accordingly, only services that the tenant must obligatorily use and for which they have no choice should be included.

As a result, it is not sufficient that the apartments are in the business assets of a commercially active company. For a commercial rental activity, the pure asset management – here the rental – must step back behind the commercial activity.

A commercial rental activity can be assumed in individual cases if the landlord provides unusual special services – e.g., cleaning, guarding the building, providing and monthly changing bed linen, or maintaining a sick room – or if a company organization is required due to constant tenant changes.

What follows from the judgment and for whom is it significant?

The judgment of the FG Münster goes beyond the previous case law on housing companies, as the previously required „original business character“ in the sense of a commercial enterprise was present in the case and yet a tax benefit was denied. Furthermore, the judges presented an even more restrictive interpretation, according to which the existence of a housing company „should only rarely be applied.“

The current judgment is of enormous importance for entrepreneurs who are considering (or have to consider) transferring a business that primarily leases residential properties. If the increasingly narrow requirements of the housing company cannot be met and the judgment of the FG Münster should stand before the BFH, only the number of rented apartments can enable a tax benefit.

Because the tax administration has bound itself by the regular presumption in the inheritance tax guidelines, according to which a housing company is assumed if the main purpose is the rental of residential space and more than 300 apartments are rented at the time of taxation. Even the current judgment should not change the binding effect, as in the judgment case, a company was explicitly transferred that comprised less than 300 apartments.

Facts

For possible transfers of potential housing companies, the number of rented apartments – up to and including 300 apartments or more than 300 apartments – remains a decisive factor. To ensure that you still have reaction options in the event of a possible rejection by the tax administration, you should therefore include corresponding reclaim rights in the gift contracts. Here, too, careful and forward-looking tax planning can be more than „half the battle“ to benefit from tax advantages.

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