

INHERITANCE AND GIFT TAX: HARMFUL ADMINISTRATIVE ASSETS AND CONSEQUENCES OF CORPORATE TRANSFORMATIONS



BACKGROUND

In the case of transfers of company shares to subsequent generations, extensive considerations must regularly be made in advance in order to make the succession as tax-neutral as possible and to take individual considerations into account. A wide variety of restructuring measures may be necessary to optimize the succession in order to fully reflect economic and tax considerations, in particular those relating to the exemption of business assets in accordance with §§ 13a, 13b of the German Inheritance Tax Act (ErbStG).

However, such restructurings may give rise to young administrative assets and young financial assets which are not subject to any preferential treatment and should therefore be avoided. While young administrative assets refer to the non-operating assets contributed within two years prior to the transfer, young financial assets refer to the positive balance of the contributions less withdrawals.

The BFH had already made statements on administrative assets pursuant to the prior legislation in a total of five rulings dated January 22, 2020. In the meantime, the supreme tax authorities of the federal states have issued a statement on the consequences of various transformation processes in a letter dated October 13, 2022 (BStBl. 2022 I p. 1517).

EFFECT ON YOUNG ADMINISTRATIVE ASSETS AND YOUNG FINANCIAL RESOURCES

The tax authorities have now adopted the BFH's legal opinion for current law. Accordingly, the qualification as young administrative assets depends on whether the assets continue to be allocated to the same business or whether a change of legal form has taken place. The change of business allocation is also relevant for the assessment of young financial assets.

In practice, therefore, the contribution of a sole proprietorship to a partnership or corporation generally results in young administrative assets.

CONSEQUENCES OF THE TRANSFORMATION FOR THE SIMPLIFIED CAPITALIZED EARNINGS VALUE METHOD

In Germany, transformation processes also have an impact on the simplified capitalized earnings value method. Under this method, the company is valued on the basis of the operating results of the last three financial years. By way of clarification, the tax authorities now state that the operating results of the merged company must also be taken into account when determining the capitalized earnings value in the simplified procedure.

In practice, this means that for a valuation as of 1 January 2022, the operating results for 2019 to 2021 must be applied. If a merger has taken place in 2021, the results of the merged company in 2019 and 2020 must also be included for the simplified capitalized earnings value method.

In addition, it must be examined as to which motives led to the restructuring and whether the simplified capitalized earnings value determined can still be regarded as the average annual earnings of the company. This is because, in the opinion of the tax authorities, restructuring measures which (also) aim to maximize profits may justify a mark-up on the average earnings. This may be the case, for example, in the event of a future change in operating results due to the purchase of know-how.

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CONCLUSION

With the identical decrees of the supreme tax authorities, for the statements were made for first time concerning the new law on various restructurings, with which the legal opinion of the tax authorities has now been clarified. This may result in far-reaching consequences for corporate succession optimized for tax purposes in pursuance of §§ 13a, 13b of the German Inheritance Tax Act (ErbStG).

In order to master the complexity and variety of the conceivable issues, BDO's specialist department for business and wealth succession will be happy to provide you with tax law advice and show you the tax options and risks involved in company succession. Please do not hesitate to contact us.

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