



Investing in German Real Estate from abroad – is your company liable to corporate or personal income tax?

Assessment of company's legal type for tax purposes
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Foreign investors earning income from German real estate are generally liable to German income tax on this income. The German tax system differentiates between natural persons, which are taxed with personal income tax and corporations, which are taxed with corporate income tax. Foreign companies could be categorized either as corporation or as private company, which would be taxed with income tax as applicable for its members. In the following article we will provide an overview how companies are assessed and categorized for German tax purposes.

Differences in tax treatment between foreign private and corporate investors

Tax treatment of real estate investment in Germany differentiates between private and corporate income tax not only for the applicable tax rate but also for the extent of taxable income. The applicable tax rate on such income is a flat rate for corporate investors of 15% (plus solidarity surcharge), while personal income from German real estate investment is taxed at a progressive rate of up to 45% (again plus solidarity surcharge). The tax base is wider for corporate investors though; while e.g. profit from sale of real estate property by a corporate investor will be taxed, it will be tax free for private investors after a certain holding period. Our [article "Investing in German Real Estate from abroad – Taxation of corporate and private investors"](#) broadly outlines, how income for foreign natural persons and corporations investing in German real estate is taxed.

The German tax system thus differentiates between natural persons, which are taxed with personal income tax, and corporations, which are taxed with corporate income tax. Private companies are generally disregarded for these tax purposes. Their incomes are allocated to the members of the company, which will be liable for the income tax.



Assessment of company type

German Fiscal Authorities reserve the right to assess whether a foreign company investing in Germany qualifies as a private company or as a corporation for German tax. The foreign tax treatment or foreign election options such as “check the box” do not impact the German assessment. **The assessment for German tax purposes is also independent from the civil status of a company.** This might be unexpected for investors established in the legal company form from another EU-country, as their civil status in Germany would follow the assessment in the country of foundation.

The assessment for tax purposes is made in two steps:

1. Comparison of the general foreign legal type to German legal company types laid down in civil law (Pre-set classification list)
2. Individual assessment of the foreign company on certain comparative criteria

Step 1: Preset classification

Most foreign legal company types, are directly comparable to German legal company types, e.g. the Dutch “CVoA” relates to German “KGaA”, the Swedish “AB” and the Turkish “A. S.” to a German “AG”, or the South African (Pty) Ltd and the Polish “Sp.z.o.o.” to a German “ GmbH”. Their tax treatment follows the treatment of the equivalent German company. Investors should thusly refer first to general classification lists laid down by the Federal Ministry of Finance (e.g. BMF circular dated from 24.12.1999), which contain the equivalent German legal company type for a lot of foreign legal company forms.

Step 2: Individual assessment

In other cases, foreign law leaves more degrees of freedom when establishing a company organized as certain legal type, e.g. LLCs formed in the USA. Also certain foreign company types are not directly comparable to any existing German legal company type (e.g. Liechtensteins “Treuunternehmen”). For investors, which are organized as such companies no pre-set assessment exists. In this case the classification for German tax purposes needs to be determined on an individual level, based on the companies statues of organization or articles of association and applicable civil law. German fiscal courts have set forward categories which need to be analyzed for classification, e. g. whether or not individual members forming the company bear liability, to which degree management decisions are centralized or if the company needs minimum capital to be raised by members.



Summary

Due to the independent assessment by German fiscal authorities, companies which qualify in their country of residence as separate taxable entity could be transparent for German tax purposes and their members taxed with individual income tax and vice versa. As a change in classification fundamentally impacts German taxation, such assessment can pose an unforeseen pitfall for investors. This risk can be hedged proactively, though, e. g. by developing an assessment together with a German tax advisor and proactive clarification.