



GERMAN TAX OVERVIEW

The German tax law is very complex and numerous exemptions (and deductions) apply, therefore it is necessary to consult a German tax advisor/accountant in all individual cases. The following information is merely a brief introduction for individual non-resident investors holding property in Germany (as private asset) and must not be viewed as an exhaustive tax guide or tax advice.

Business income and other types of income (German tax law distinguishes seven different forms of income for tax purposes) are out of scope of this brief guide. The following information applies to property held as a private asset only; property held as a business asset is taxed differently.

INCOME TAX (INDIVIDUAL)

Income tax is levied on all German income. As a general guide, the tax is progressive and levied at rates of 15-42%. In addition, a solidarity surcharge (to pay for the former East Germany integration) of 5.5% of the total tax due is payable. (The top rate of 42% is only levied on profits exceeding 52,152 euro.)

There are two types of income tax – tax on wages (*Lohnsteuer*) and tax on income (*Einkommensteuer*). The difference is the method of collection; tax on wages is withdrawn at source and paid to the tax office by the employer, while income tax (on income from self-employment, rental income, investments, etc) is paid directly by the individual taxpayer.

Based on the previous year's tax assessment tax payers have to make tax pre-payments in quarterly installments (March, June, September, December). The tax return for the year needs to be filed by 31st May of the year to follow. Adjustments are made for eventual under- or overpayment.

Germany has been undergoing positive changes in its tax law in the last few years. The individual income tax rates have been decreased, from 53% (1998) to 42% (2005) in case of highest rate, and down to 15% from 25.9% as far as lowest rate. (The Merkel government has now agreed on a corporate tax reform to lower the total tax liability of corporations to 29.83% from current 38.65%, possibly effective 1 January 2008. To compensate, some of the many tax avoidance loopholes are to be closed.)

The non-taxable minimum is currently 7,664 euro for single persons (or 15,328 euro for married couples), however, there are some exceptions where this may not apply.

OTHER TAXES

There is a number of other taxes, including VAT (*Umsatzsteuer* or *Mehrwertsteuer*), additional sales taxes on certain goods such as alcohol, tobacco, gasoline, etc, other business taxes, church tax, etc. (Church tax of 8% of the income tax is only payable by those officially affiliated with one of the main churches.

VAT is being increased from 16% to 19% (effective 1 January 2007), although a lower rate of VAT applies to certain products, while others (such as medical goods) are exempt.

HOLDING REAL ESTATE

Real estate tax

German property is subject to a real estate tax (*Grundsteuer*), levied annually. The tax base is the 'assessed value' (*Einheitswert*). The tax depends on several factors including location, size, use, local municipal coefficient, etc. Typically, for a 1 bedroom apartment in Berlin the tax will be in the region of 200-500 euro p.a. (Real estate tax is generally paid by the tenant.)

Rental income

Rental income is taxed as income (see section on Income Tax) and is subject to the progressive tax rate. Interest on loans provided to finance real estate, expenses and property related cost (eg. management fees, insurance, etc) can be deducted from the taxable rental income.

Depreciation

Real estate is subject to tax depreciation on an annual basis. (Land cannot be depreciated.) Buildings are depreciated over 40-50 years, depending on the year of construction. (2% annual depreciation applies to buildings constructed in/after 1925, 2.5% for buildings constructed prior to 1925.) This effectively lowers the annual tax payable in Germany.

Special rates apply to modernisation of listed (*Denkmalschutz*) buildings – modernisation costs can be depreciated over 12 years (9% p.a. for the first eight years and 7% p.a. in the next four years). Modernisation of not listed properties follows the standard depreciation rates.

See following page for BUYING AND SELLING REAL ESTATE

BUYING AND SELLING REAL ESTATE

Transfer tax

Transfer of German property is subject to a transfer tax (*Grunderwerbsteuer*) – equivalent of stamp duty – levied at a rate of 3.5% (of the purchase price). It is generally paid by the buyer.

Capital gains

Currently profits made on sales of properties held as a private asset are not taxed if the property has been held for over 10 years. However, there are plans to introduce a (20%) capital gains tax in the coming years.

MOST COMMON LEGAL FORMS

Property investors typically choose one of the following legal forms in which to own German real estate: individual ownership, partnership under civil code, limited company. A partnership is not taxed as a separate legal entity, each partner is liable to pay tax on his share of income from the property according to his individual tax status. While a partnership is easy to establish and handle, a limited company will, due to the formal procedures, incur higher costs (of notaries, accounting) and commercial tax obligations.

NOTES

Germany has concluded double tax treaties with all of world's developed economies.

Sources: PriceWaterhouseCoopers; Stb D. Rot; Bundesfinanzministerium