

# Information Paper

for

## Americans with a German Residence Permit

### 1. General.

a. I prepared and have updated this information paper based on my personal experience filing a German income tax return each year for the past 33 years, nearly 20 of those years as fully retired person.

b. Any American citizen who seeks permanent residence in Germany must apply for a residence permit (Aufenthaltstitel). Holders of the Aufenthaltstitel enjoy all of the benefits and rights enjoyed by the German citizens with the exception of the right to vote in elections at various levels of government.

With the benefits, privileges and rights come requirements. One such requirement is to file a German income tax return (Steuererklärung) if the person's income is above the filing threshold (Grundfreibetrag) – for tax year 2025, the thresholds are 12,096.00 € and 24,192.00 € for an individual or joint filers, respectively. The submission deadline varies from year to year. For tax year 2025, the income tax return is due by 31 July 2026. If you use a Steuerberater (tax accountant), the submission deadline is 01 March 2027.

Of note here, if you have directly taxable income that falls under the filing threshold, but also have any other income, such as foreign earned and unearned income, disability compensation from the Department of Veterans Affairs, military retirement, civil service retirement, income from rental property in the United States, etc. - that raises your overall income above the filing threshold, then you must file a German income tax return as well. This is based on Bundesfinanzhof Urteil (decision) III R 50/00.

Actually, any amount of foreign income usually triggers a filing requirement. This is because the tax office would in most cases not know about it and hence would need to be informed. It is very risky in Germany to understate your world-wide income on your income tax return or decide against filing an income tax return at all. Additionally, the tax bracket effect applies even if the directly taxable amount is below the Grundfreibetrag.

To file a German income tax return, the American citizen with the residence permit must have an income tax number (Steuernummer) and a tax identification number (Steueridentifikationsnummer).

The Bundeszentralamt für Steuern (Federal Central Office for Taxes) issues the tax identification number to all persons who are registered in Germany. The German income tax number is issued by the local Finanzamt (German Tax Office) to which the German income tax form is to be submitted.

It is possible to apply for both numbers online.

**2. Income Tax Return.** What must be reported? With few exceptions, all of your income. The list below is not all inclusive, yet covers what most military, civil service and non-appropriated fund retirees receive as income.

**a. Retired Pay or Survivor Benefits from any US Government source.** This is not directly taxable, but is used to determine the tax rate on income that is directly taxable. The procedure to determine the tax rate is the Progressionsvorbehalt.

**b. Social Security Benefit.** If the Social Security benefit was started in 2005 or earlier, 50% percent is directly taxable. The other 50% is tax free. This percentage is grandfathered and will not change. A German law affecting the taxable amount of the German Rente went into effect starting in 2006. This law also applies equally to the Social Security benefit as it concerns the tax free amount. See the comment about Rente under the heading German Income.

**c. Capital Gains – Foreign and Domestic.**

**American and German Bank Interest.** The American bank interest is reported using Form 1099. The German bank interest is reported as a listing of accounts and the amount of interest paid in each account.

**Dividends from Stock Investments.** German stocks are generally accounted for under a depot account. Each year, the manager of the depot, e.g., a bank, will provide a document detailing the dividends paid.

**Profit from Sale of Investments.** When an investment is sold, the depot manager will provide a document showing the value of the sale. Obviously, the profit is the difference between the total purchase price and the amount of the proceeds from the sale. It's very important to keep accurate records reflecting the initial cost of the investment.

**Thrift Saving Plan.** When taking distributions from the Thrift Saving Plan (TSP), the contributions are not taxed by Germany. However, if the distributions include capital gains, then this income is reportable on the German income tax return as a capital gain and the gain that is above the tax free amount is taxed at the 25% rate.

The TSP distributions present some significant problems for the German income tax return. All TSP contributions are pre-tax dollars, similar to the traditional IRA. The developers of the TSP did not take into account that the participating investors are scattered around the world. The TSP distributions do not include a splitting of contributions and earnings, because the entire distribution is taxable in the US. TSP withholds the standard 20% tax unless the participant requests a different withholding. Therefore, to report the distributions in Germany, the TSP participant can only report the total annual distribution as capital gain, the consequence of which is a higher tax bill.

The easiest solution is to roll the entire TSP account into one or more annuities. The annuity management companies can calculate the interest gained over the life of the

annuity and show the splitting of contributions and interest for each year. The mix of contributions and interest is the same year after year.

There is a tax free amount of capital gains in Germany for 2023 thru 2025 – 1,000.00 € and 2,000.00 € for an individual or joint filers, respectively.

*d. Wholly Owned Annuities.* These sources of income are from private savings plans such as individual retirement accounts, 401k plans, Thrift Savings Plan (assumes that the owner uses all or part of the TSP balance to establish an annuity) or private annuities.

If the filer(s) is a retired person, who had started receiving the Social Security benefit at age 65 or 66, then 18% of this annuity income, less own money paid in, is directly taxable, that is, just the interest part of the annuity is taxable by Germany. This annuity income for a retired person, aged 60 or older receiving the Social Security benefit and/or a German Rente, is categorized by the German finance office as Altersvorsorge or private old age income. The percentage directly taxed varies from 22% down to 15% depending on the age at which the governmental retirement annuity benefit was started. The longer a person waits to start their governmental retirement annuity, the lower the percentage of the old age income that is directly taxed.

This annuity income would also be taxable by the US Internal Revenue Service. However, under the joint treaty (Article 18, paragraph 2.) with Germany to avoid double taxation, only Germany has the right to tax this income. Paragraph 2 is quoted: "Subject to the provisions of Article 19 (Government Service; Social Security), annuities derived and beneficially owned by a resident of a Contracting State shall be taxable only in that State. The above reference to Article 19 is meaningless, because the original Article 19 was totally deleted by the protocol signed on 1 June 2006 and the new article, "Government Service," substituted does not cover wholly, beneficially owned annuities.

The term "annuities" as used in this paragraph means a stated sum paid periodically at stated times during a specified number of years, under an obligation to make the payment in return for adequate and full consideration (other than services rendered).

US Tax relief is sought using the Form 8833. The same form, with a different treaty article and paragraph, is used to seek tax relief for the US taxation of Social Security benefits, which can include the normal old age pension and possibly a Social Security disability payment that is also taxed by Germany. If you are a retired veteran, not yet eligible for the old age pension from Social Security, but receiving a Social Security disability payment, you must report this income to the German Finanzamt on your annual German income tax return.

### 3. German Income.

*a. Rente.* There is a tax free portion, which is determined based on the year the person retires. The amount of the tax free portion that is calculated at the start of the Rente remains the same even though the total Rente may be increased via cost of living adjustments. Starting in 2006 the tax free portion was 48%. The tax free

portion continued to be reduced by 2% per year through 2020 at which time the tax free portion is 20%. The tax free portion was reduced to 19% and 18% for 2021 and 2022, respectively. Starting in 2023, the tax free portion is reduced by ½ of 1% per year. Ultimately, retirees starting their Rente and Social Security in 2058, will not enjoy a tax free portion.

**b. Income from an employer.** This income is directly taxed.

**c. All Free-Lance Income – Billing for Services Rendered.** Generally, free-lance income is earned working in the home office. As a free-lance person, there are a number of write-offs that can be applied to these earnings. The details about these write-offs are beyond the scope of this paper. A German tax advisor can provide the guidance needed to determine the documentation required to support the write-offs.

#### **4. Some Comparisons of US and German Income Tax Returns.**

If the retired person is a dual filer (US and German tax law), the German Tax Office can demand to review a copy of the US income tax return. If they see income that should have also been included on the German income tax return, they will ask for the tax documents, essentially the Forms 1099. In the case of wholly owned annuities, in addition to reviewing the Forms 1099, they may also ask to see the contracts that were signed with the company(s) paying the annuities. With this degree of review, it is important to be able to show the German finance office the splitting of each periodic payment (interest and own money).

There is a survivor benefit that is not directly taxable by the US or Germany. This benefit is the Dependency and Indemnity Compensation (DIC). It is paid to a survivor whose spouse died on active duty or died as a military retiree when the death was attributable to a service-connected injury or illness. A Form 1099 is not issued to the survivor receiving DIC and it is not reported on the US or German income tax return. The same holds true for Retirees or U.S. Veterans receiving a Veterans Affairs disability payment. The disability payment is not subject to direct taxation by the US or Germany. A Form 1099 is not issued to the Veteran and it is not reported on the US or German income tax return.

This exemption is covered in the original Article 19, Government Service; Social Security, of the Convention between The United States of America and The Federal Republic of Germany for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital and to Certain Other Taxes, signed on 29 August 1989. In a protocol, signed on 1 June 2006, amending the aforementioned convention, the original Article 19 was entirely deleted and replaced with a new Article 19, Government Service. The wording of the exemption in both the original (paragraph 1. c) and revised (paragraph 3.) Article 19 are identical. Therefore, disability payments should never be reported on the German income tax return.

However, there is another consideration on reporting income not directly taxed. Article 23, Relief from Double Taxation, of the tax treaty, includes a statement, the impact of which is often missed when reading the article. It states that Germany retains the right to use any income that is tax free and derived under the other

articles of the treaty towards the determination of the tax rate with the Progressionsvorbehalt calculation. As you already know, non-disability military retirement is used to determine your tax rate. Military disability retirement is also used to determine your tax rate. The basis for this is found in German income tax law. These two pension benefits are termed Versorgungsbezüge, based on time in service, and therefore, are used to determine your tax rate.

There is a current requirement, which recently came to light, to report VA DIC and VA disability benefits income as world-wide income and it is used to determine the tax rate through the Progressionsvorbehalt calculation on income that is directly taxed.

Before the Finanzamt can use this income to determine the tax rate, under German tax law, they must determine the type of income that they are dealing with, because only certain types of income can be used under the Progressionsvorbehalt. Currently, under German law, VA disability and DIC are characterized as income that is not specifically listed as income that can be used with the Progressionsvorbehalt. Therefore, it should not be used to determine the tax rate.

In May 2022, responding to a request for clarification of this issue from an American veteran concerning the use of his disability benefit to calculate the tax rate, the Finanzgericht (Finance Court) Baden-Württemberg issued a decision that US VA disability benefits are not taxable and are not considered to determine the tax rate. Unfortunately, his local Finanzamt challenged this decision and sent a request for review to Bundesfinanzhof (BFH) in Munich.

The grounds for the Finanzgericht Baden-Württemberg decision are solid and the favorable decision should be upheld by the BFH. However, until the BFH renders a decision, disability benefits and DIC must be reported as world-wide income on the Einkommensteuererklärung. Some Retirees and veterans think that because the decision by the Finanzgericht Baden-Württemberg was favorable, they are not required to report this income. The decision will remain favorable, if and when the BFH renders a decision that supports the findings of the Finanzgericht Baden-Württemberg.

**5. Summary.** If an American retired person or American survivor of a retired person is a permanent resident of Germany with an Aufenthaltstitel, they must comply with all legal requirements, especially the filing of a German income tax return if their total income is at or above the filing requirement threshold.

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Date prepared: 20 November 2020, last update: 25 November 2025