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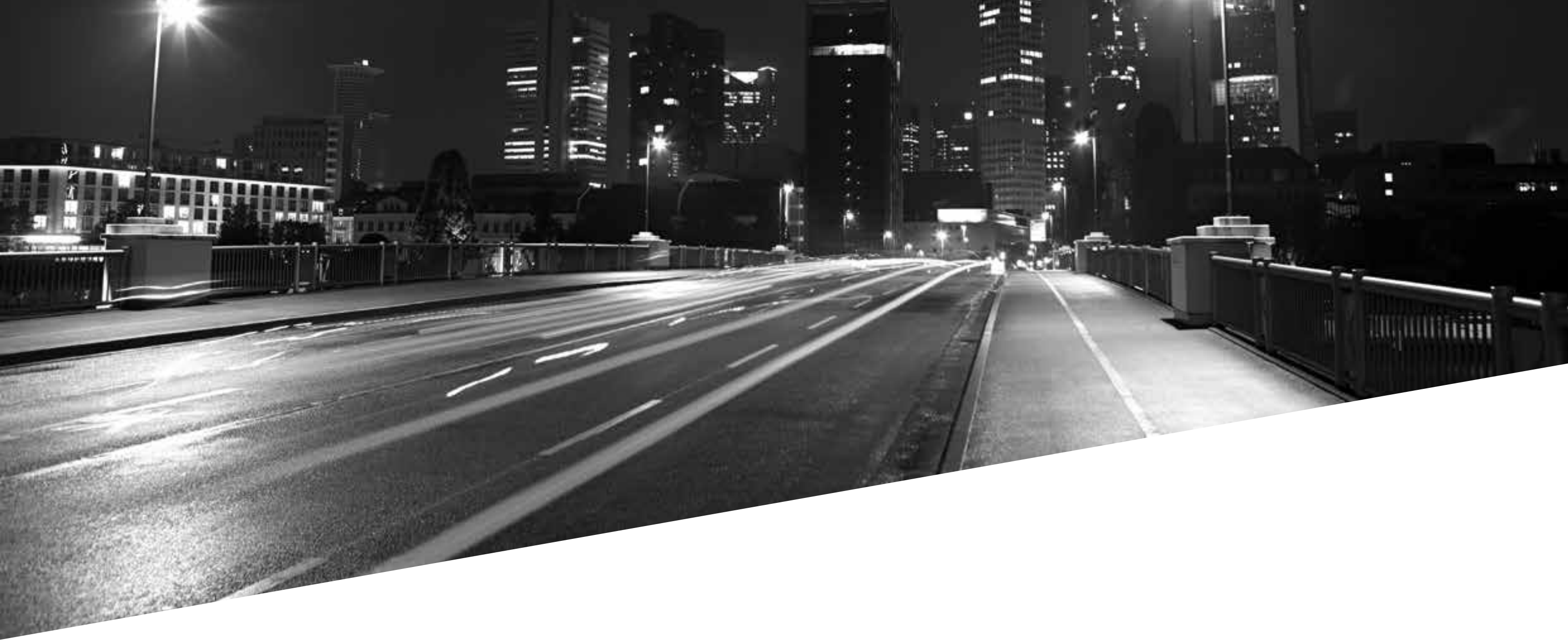

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1. Types of tax

1.1 Inheritance and gift tax

Germany has a unified inheritance and gift tax called "*Erbschaft- und Schenkungsteuer*" (*ErbSt*). *ErbSt* is imposed on any transfer of property at death or by gift (or by deemed gift). The basis of assessment is the benefit accruing to the transferee (beneficiary or donee), not the estate itself. The *ErbSt* is regulated on a federal level, although the tax revenue is assigned to the federal states (*Bundesländer*) of Germany.

The Federal Constitutional Court (*Bundesverfassungsgericht*) decided by judgment of 17 December 2014 (1 BvL 21/12) that the German Inheritance and Gift Tax Act (*Erbschaft- und Schenkungsteuergesetz*, (*ErbStG*)) and especially the regulations relating to exemptions and reliefs for business assets (see Section 4) violated German constitutional law. The legislature was required to amend the existing rules; new legislation was enacted in October 2016 and entered into force with retroactive effect from 1 July 2016. The former regulations are applicable for inheritances and donations until 30 June 2016.

Note that in the case of German family foundations, there is a deemed taxable transfer of property every 30 years, which is subject to unlimited German *ErbSt* (recurrent charge). The 30-year period starts on the date of the first transfer of property to the German family foundation.

1.2 Real estate transfer tax

The (direct or indirect) transfer of German real estate is basically subject to real estate transfer tax of between 3.5% and 6.5%, depending on the federal state in which the real estate is located. But a transfer by inheritance or gift is usually exempt from real estate transfer tax.

2. Who is liable?

2.1 Unlimited liability

Any transfer of worldwide net property either at death or by gift (or by deemed gift) is generally subject to unlimited taxation if either the decedent (donor) or the beneficiary (donee) is considered to be resident in Germany for tax purposes. German tax residence exists if any of the following conditions apply:

- An individual has a residence or his or her habitual place of abode in Germany.
- A nonresident German citizen has been resident for tax purposes in Germany at any time within the last five years prior to a transfer at death or by gift.
- A nonresident German citizen is employed by a legal entity organized under German public law. In this case the dependents who live in the household of such German citizen have a German tax domicile as well.
- A corporation or any other legal entity or estate has its place of management or legal seat in Germany.

2.2 Limited liability

Any individual or legal entity who is not resident as aforementioned will be subject to *ErbSt* only upon the transfer of net property, which is regarded as German-situated according to German national tax law. German-situated property means:

- Real estate, agricultural and forestry property situated in Germany
- Assets pertaining to a permanent establishment of a commercial business located in Germany
- Shareholdings in German resident corporations if the shareholder owns (individually or jointly with other persons closely related to the shareholder) directly or indirectly at least 10% of the registered share capital
- Inventions, designs and topographies recorded in a German register as far as assets of a German permanent establishment
- Assets that have been leased to a commercial business operated in Germany
- Mortgages or any other receivables secured by German-situated real estate or by German-registered ships, except for such receivables for which negotiable bonds have been issued
- Claims arising from silent partnerships and profit participating loans if the debtor is situated in Germany
- Any beneficial interests (e.g., right of usufruct) in the aforementioned assets

A nonresident individual as decedent (donor) is subject to an extended limited tax liability (e.g., with regard to capital claims vis-à-vis domestic debtors or with regard to movable property abroad), provided the following conditions are met:

1. Such individual was subject to unlimited income tax liability in Germany within the last 10 years prior to a transfer at death or by gift.
2. Such individual was cumulatively a German national and subject to unlimited German income tax liability for a combined period of 5 years within a 10-year time period prior to the end of the unlimited income tax liability.
3. Such individual is resident of a low-tax jurisdiction according to the German controlled foreign company (CFC) legislation.
4. Such individual has substantial economic interests in Germany within the meaning of the German CFC legislation.

Also, if the decedent, the donor or the beneficiary is a resident of the European Union (EU) or the European Economic Area (EEA), he can choose to be treated for purposes of German inheritance and gift taxation of the respective acquisition as a German tax resident so that he can claim certain maintenance allowances that are available only to German tax residents. The Court of Justice of the European Union decided on 8 June 2016 that the availability of those maintenance allowances to only German tax residents is not in line with the EU fundamental freedoms. An amendment of these rules is subject to a current legislative procedure.

2.3 Residency

Place of residence

Under German tax law, an individual's place of residence is the place (dwelling or domicile) that he or she occupies under circumstances that indicate that he or she will retain and use it on more than a temporary basis. Residence requires an intent to stay, which must be evidenced by objective criteria. The German tax authorities' interpretation of intent to stay is quite broad: such intent will be presumed if an owned or rented dwelling is held available for the exclusive use by the owner, even if it is used only from time to time. Therefore, an individual can be resident in different places at the same time.

Habitual place of abode

The term habitual place of abode implies the location where a person is physically present under circumstances that indicate that his or her presence in that particular place is not merely temporary. As a general rule, a habitual place of abode, and thus tax residence, is deemed to exist if the individual's stay in Germany exceeds six months. In this case, he or she will be deemed resident for the entire period of his or her stay in Germany, including any brief interruptions.

Residency and double-taxation treaties

Special rules on the consequences of dual residency apply with regard to certain double-tax treaties (DTTs). For example, according to the German-US DTT, an individual who is considered a resident in both contracting states pursuant to national tax law but who is a citizen of only one of the contracting states will be deemed to have its place of residence for purposes of the DTT in that state for a period of 10 years after becoming a resident for inheritance- and gift-tax purposes in the other state.

3. Rates

The applicable tax rate depends on the tax class of the acquirer (see below) and the value of the taxable acquisition. The tax assessment basis is the taxable value of the assets transferred after exemptions and reliefs.

Taxable value of the acquisition exceeds	Acquirer in		
	Tax class I	Tax class II	Tax class III
€0	7%	15%	30%
€75,000	11%	20%	30%
€300,000	15%	25%	30%
€600,000	19%	30%	30%
€6 million	23%	35%	50%
€13 million	27%	40%	50%
€26 million	30%	43%	50%

Note that the taxable value of assets, which is excluded from tax under German *ErbSt* pursuant to a DTT, must be added to the taxable value of the transfer in order to determine the applicable tax rate (progression reserve). Thus, it is not taxable but affects the overall rate.

The tax rate and the tax to be assessed are calculated on the basis of a rolling 10-year period. All acquisitions from the same person through gift or inheritance within the last 10 years are combined to calculate the basis for the tax due, and the tax on the earlier acquisitions is credited against the tax due.

Donees or heirs not in tax class I who acquire agricultural or forestry or other business assets, interests in a partnership and substantial shareholdings (direct participation of more than 25% of the registered share capital) in a corporation resident in Germany, in the EU or in the EEA can, under certain conditions, benefit from a reduction of the tax rate. This reduction is the difference between the amounts of inheritance tax calculated on the basis of the tax class to be applied pursuant to the actual relationship to the donor (decedent) and on the basis of tax class I. Note that, with regard to this benefit, the anti-abuse rules mentioned below also apply (see Section 4.2 below).

The applicable tax rate depends on both the relationship of the donee to the donor (decedent) and the value of the taxable acquisition. Donees are divided into three tax classes:

Tax class I:

- Spouse and partners of a registered same-sex partnership under German law
- Children and stepchildren
- Descendants of children and stepchildren
- Parents and ancestors (acquisition by death only)

Tax class II:

- Parents and ancestors (acquisition by gift)
- Siblings
- Nephews and nieces
- Stepparents
- Sons-in-law and daughters-in-law
- Parents-in-law
- Divorced spouse and partners of a dissolved registered same-sex partnership

Tax class III:

- All other individuals and legal entities (including donations to foundations)

4. Exemptions and reliefs

There are several asset and purpose-related exemptions and personal exemptions. Furthermore, there are certain categories of tax-favored assets.

4.1 Asset and purpose-related exemptions

- Household and personal effects up to a value of €41,000 and other movable property up to a value of €12,000 if acquired by a person in tax class I (see Section 3)
- Household, personal effects and other movable property up to a value of €12,000 if acquired by a person in tax classes II or III (see Section 3)
- Real estate (including parts of real estate), art items, collections of art and scientific items, archives or libraries, if there is a public interest in preserving such items because of their importance to art, history or science, and if the annual costs associated with those items normally exceed the income generated from such items. It also helps to make assets accessible to the public. The tax exemption for collections of art and scientific items is 60%, and includes parts of real estate. It amounts to 85% of the market value or total exemption if further conditions are met.
- Donations for a commonly acknowledged purpose (such as birthday presents, wedding, Christmas), but only if at an appropriate value with respect to the occasion
- Donations to registered religious communities, to Jewish cultural communities and to charitable organizations
- Donations to political parties
- Donations to the Federal Republic of Germany, the German states or municipalities and certain charitable foundations
- The acquisition of the family home for the owner's use is tax free if it is gifted to the spouse or to the partner of a registered same-sex partnership *inter vivos*. The tax exemption also applies if the family home is passed to the aforementioned acquirers upon death, provided that the acquirer uses the family home for his or her own purposes for a period of 10 years after the acquisition. If there are pressing reasons why the acquirer cannot use the real estate for his or her own purposes (e.g., in the event that the acquirer requires health care), this tax-free status remains unaffected.
- Children and stepchildren, as well as children of deceased children or stepchildren, can acquire the testator's family home by reason of death without paying tax if the acquirer uses the family home for his or her own use immediately and as far as the living space does not exceed 200 square meters. The portion exceeding 200 square meters is liable to tax. The exemption is lost if the acquirer does not use the family home for his or her own purposes for a period of 10 years after the acquisition.

4.2 Agricultural, forestry or business assets

A tax exemption can be claimed for certain tax-privileged assets in transfers of agricultural, forestry or other businesses, interests in trading or professional partnerships or substantial shareholdings (direct participation of more than 25% of the registered share capital) in corporations resident in Germany, in the EU or in the EEA (in the following eligible assets). The privilege amounts to 85% or 100% of the fair market value or FMV (*gemeiner Wert*) of the tax-privileged assets. For smaller business properties, an allowance of up to €150,000 can be granted additionally to the privilege of 85% on the tax-privileged assets. Under certain conditions, which are difficult to meet, family businesses can apply for a further 30% reduction of the tax base.

To gain the 85% privilege, the beneficiary or the donee has to keep the eligible assets during a five-year period after the inheritance or donation, and the direct wage costs during this period have to amount to 400% of the average wage costs in the last five years before the tax accrues. To gain the privilege of 100%, the assets have to be kept for seven years and the direct wage costs during this seven-year period have to amount to 700%. Facilitations for smaller businesses apply.

If the prerequisites for tax-privileged treatment are no longer met, the 85% or 100% privileges are abolished with retroactive effect on a *pro rata* basis that triggers supplementary taxation.

However, the 85% privilege is only granted if eligible assets are transferred and the ratio of the value of non-privileged, non-operating assets (*Verwaltungsvermögen*) to the total value of the eligible assets (*Verwaltungsvermögensquote*) at the time of the transfer does not exceed 90%. In the case of the 100% privilege, such ratio may not exceed 20%. Furthermore, the privilege of 85% or 100% is not applied in view of non-operating assets (*Verwaltungsvermögen*) that have been kept for a period of less than two years (*Junges Verwaltungsvermögen*).

Tax-privileged assets, in principle, include the following assets, so long as they are not expressly defined as non-operating assets (see below):

- Operating assets in Germany (individual companies or interests in partnerships) or foreign operating assets that serve a permanent establishment in the EU and EEA
- Proportionate operating assets of German corporations and corporations in the EU and EEA in which the decedent or donor held a direct share of more than 25% or — in the event that these are shareholdings of less than 25% — if the shares are subject to a pooling agreement and can only be disposed of according to certain rules set out in such pooling agreement or can only be transferred to other shareholders being or becoming pool members upon the share transfer, and the voting rights vis-à-vis shareholders not bound by the pooling agreement can only be exercised unanimously
- German operating assets of agricultural or forestry businesses, as well as corresponding foreign assets that serve a permanent establishment in the EU and EEA

Non-operating assets (*Verwaltungsvermögen*) include the following assets, so long as they exceed 10% of the eligible assets:

- Real estate, portions of real estate, rights equivalent to real estate rights and buildings provided to third parties for use
- Shares of 25% or less in a subsidiary corporation
- Securities and comparable receivables
- The FMV of the amount of currency, (bank) money and other claims if it exceeds 15% of the FMV of the business assets after deduction of liabilities (regulation is not applicable for finance companies within groups and for certain assets of other financial institutions)
- Collections of art, art items, precious metals, precious stones (gems), coin collections, libraries, archives, scientific collections and other items serving a private lifestyle

In the case of group structures, the ratio of privileged to non-privileged assets for calculating the tax-exempt amount and the thresholds mentioned above is determined on a consolidated basis.

In the case of an acquisition by death, non-operating assets can become privileged assets retroactively on the basis of a reinvestment into privileged assets within two years.

The exemption is, in general, limited to a value of transfers from one donor (decedent) to one acquirer of €26 million in a rolling 10-year period. Acquisitions above €26 million are subject to a decreasing exemption reaching 0% at an acquisition value of €90 million.

Alternatively, for acquisitions above a value of €26 million, the acquirer can file for an assessment of "need for tax relief," in which he or she only has to pay inheritance or gift tax in the amount of 50% of the non-privileged assets acquired, plus 50% of the assets owned by him or her before the acquisition, which would not be subject to a tax privilege if transferred. However, in the case of a further acquisition by gift or inheritance of non-privileged assets within the next 10 years, the relief is cancelled. Then a new filing for a relief is possible, taking into account an additional 50% of the non-privileged assets acquired by the further gift or inheritance.

4.3 Personal exemptions

In addition to the asset- and purpose-related exemptions, personal allowances as described below are available upon taxable acquisitions. Please note that these allowances will be granted only once within a 10-year period in each transferor/transferee relationship.

Beneficiary or donee	Allowance
Spouse and the partner of a registered same-sex partnership	€500,000
Children, stepchildren and children of deceased children	€400,000
Children of living children	€200,000
Other persons in tax class I	€100,000
Persons in tax class II	€20,000
Other persons and entities in tax class III	€20,000

An additional allowance of up to €256,000 is granted to the surviving spouse and the surviving partner of a registered same-sex partnership, provided that the surviving spouse or the surviving partner of a same-sex partnership is not entitled to pension payments upon the death of the spouse or the partner of a registered same-sex partnership. If so, the allowance is reduced by the net present value of such pension claims. An additional allowance of up to €52,000 is granted to surviving children (up to age 27) depending on their age. Any entitlement to pension and similar payments reduces the allowance in the same way as described for the spouse or the partner of a registered same-sex partnership.

For any transfer that is subject only to limited tax liability, a restricted personal allowance of only €2,000 is granted once every 10 years in each transferor/transferee relationship, regardless of the personal relationship between the transferor and transferee. As a reaction to a judgment of the Court of Justice of the European Union, an option to choose unlimited taxation under *ErbSt* has been implemented. Making use of this option leads to an unlimited taxation of all assets and liabilities being transferred along with the assets subject to limited taxation, including transfers within a time period beginning 10 years prior to the transfer for which the option has been used and ending 10 years after such transfer. On the other hand, personal allowances are determined on the basis of the actual personal relationship between the parties. An amendment of these rules is subject to a current legislative procedure.

5. Filing procedures

Generally, on any transfer of property subject to *ErbSt*, the German financial authorities must be notified within three months of the transfer by the recipient. In the case of *inter vivos* transfers, the transferor also has a reporting obligation. There are, however, certain exceptions to this notification obligation if, for example, the acquisition is evidenced by a deed certified by a German court or by a German notary public. In the case of a donation certified by a German notary public, a notification is not required.

Upon notification of a transfer subject to *ErbSt*, the German financial authorities may request the filing of an inheritance- or gift-tax return from any person involved in the transfer. The time frame for the filing must be at least one month, but an extension is generally granted upon request.

An assessment is subsequently sent to the taxpayer for any tax due, which is then normally payable within one month after receipt.

Tax due on the acquisition by death of tax-privileged agricultural, forestry or other business assets may, under certain conditions, be deferred up to seven years (interest-free in the first year) upon request.

Tax due on the acquisition by death of real estate used for residential purposes may, under certain conditions, be deferred up to 10 years (interest-free in the first year) upon request.

6. Assessments and valuations

The tax assessment basis for the German *ErbSt* is the FMV of the transferred asset. The key principles are set out below.

Real estate

The decisive factor in the valuation of real estate is the type of land to be valued. The value of undeveloped real estate is based on the real estate value, considering the plot size and the most recent standard land values issued by the local committee of experts (*Gutachterausschuss*).

The value of developed real estate is determined using the following methods:

- Sales comparison approach (for apartments, part-ownership, semi-detached and detached houses): The sales comparison approach involves determining the market value of real estate based on actual purchase prices paid for real estate that is comparable in terms of location, use, layout, type and age of the building.
- Capitalized earnings method (for rented residential property, commercial and mixed-use real estate): The value includes both the value calculated for the buildings on the basis of the earnings (building earnings value) and the land value, which is calculated in the same way as for undeveloped real estate. The building earnings value is calculated using the net annual rent less facility management costs and the interest on the real estate value multiplied by a factor that depends on the property yield and the remaining useful life.
- Cost approach (for apartments, part-ownership, semi-detached and detached houses in the absence of comparative values): Using the cost approach, the value comprises the total production costs for the installation on the real estate, as well as the real estate value (plot size × standard land value).

Business assets and company shares

Business assets are valued using uniform valuation methods, regardless of the legal form of the business. The FMV of listed shares is generally calculated based on the share price. Unlisted shares are valued using the following methods, which also have to be used to value partnerships and individual companies.

Sales comparison approach

The FMV of operating assets is derived primarily from sales among third parties that have taken place no earlier than one year before the date of taxation.

Capitalized earnings method

If there are no sales within the last year before the date of taxation, the fair market value must be estimated by taking into account earnings prospects or another recognized method that is also customary in ordinary business for non-tax purposes. The method used should be the one that an acquirer would use as a basis for assessing the purchase price. A frequently used capitalized earning method is laid out in IDW S1, issued by the Institute of Public Auditors in Düsseldorf, Germany (*Institut der Wirtschaftsprüfer in Deutschland e.V.* or IDW).

If the capitalized earnings method is used, the companies can also choose the simplified capitalized earnings method, which is set out in the German Tax Valuation Act (*Bewertungsgesetz*).

The business value calculated using the simplified capitalized earnings value breaks down as follows:

- Capitalized earnings value of the operating assets
  + FMV of the non-operating assets less the economically related liabilities
  + FMV of interests in partnerships and shares in corporations
  + FMV of the assets contributed within the two years prior to the transfer less the economically related liabilities

The capitalized earnings value of the operating assets is calculated using the following formula:

- Annual earnings that can be achieved on a long-term basis × the discount factor.
- The annual earnings that can be achieved on a long-term basis are derived from the average earnings over the last three fiscal years prior to the valuation date. The discount factor has been set to 13.75 in 2016 and can be adjusted by the Federal Ministry of Finance in accordance with the development of the term structure of interest rates.
- Intrinsic value method: The minimum value disclosed is the FMV of all individual assets less the liabilities.

7. Trusts, foundations and private purpose funds

7.1 Trusts

German civil law does not contain specific provisions for trusts, and Germany has not ratified the Hague Convention on the Recognition of Trusts dated 20 October 1984.

For example, a foreign trust with German-situated property set up by a will is invalid from a German civil law perspective. Any trust that is created will be assimilated to the legal arrangement under German civil law that most closely resembles the provisions of the trust (e.g., foundation, aggregation of property, nominee agreement, execution of a last will).

Taxation of the trust

The German tax authorities classify a trust basically on the basis of the following criteria:

- *Revocable trust:* The ownership of the assets is regarded as not being transferred to the trust. Income and assets of the trust remain taxable in the hands of the settlor.
- *Irrevocable trust:* The ownership of the assets is regarded as being transferred to the trust. The trust itself with its income and assets is subject to tax.

Taxation of the endowment with capital — inheritance and gift tax

The German tax treatment of a trust created under a foreign jurisdiction depends mainly on the economic substance of the foreign settlement. The basic criterion for determining whether the formation of a trust does constitute a taxable event under German tax law depends on whether the settlement involves a final and irrevocable disposal of ownership of the transferred assets. The transfer of assets to a trust is only subject to gift tax if the trust is then factually and legally able to freely dispose of the assets. According to the German Supreme Tax Court, the review of this criterion should be limited to the civil law position. The ruling stated that the party to whom the assets are attributable from an economic perspective is irrelevant. Consequently, the structure must be deemed a revocable trust and not constitute a transaction subject to gift tax if the settlor has reserved the following rights under the trust's constitution:

- To amend the constitution at any time
- To revoke the trust at any time
- To issue instructions to the trustee

Accordingly, the creation of a grantor's trust is, as a rule, not subject to gift tax if the settlor of a grantor's trust reserves the right to issue wide-ranging instructions to the trustee that extend to revoking the trust.

Tax class III is applied to foreign trust transfers and subjected to gift tax.

Taxation of the beneficiaries

Establishing a foreign trust leads to income tax consequences. There are certain risks with regard to pre-immigration trusts, as follows:

- If it is possible for the settlor to revoke the trust and unconditionally reclaim the assets (a revocable trust), and if the settlor has substantial influence on the investment decisions of the trustee, then the items of income (*Einkünfte*) and assets of the trust will most likely be taxed as items of income and assets of the settlor (viewed as a nominee arrangement).
- Irrevocable trusts of which more than 50% of the beneficiaries or remaindermen are relatives of the settlor are treated as foreign "family foundations" and are subject to the German CFC legislation, i.e., if the settlor is a resident in Germany, the items of income of the trust will be directly attributed to him or her and be subject to German income tax irrespective of whether there is a distribution to the beneficiaries.
- If the settlor is a nonresident, but one beneficiary or remainderman is resident in Germany, the items of income and assets of such an irrevocable trust will be attributed proportionally to such beneficiary or remainderman and will be subject to German income tax irrespective of whether there is a distribution to such person.
- If the income from the trust fund is kept in a lower-tier company in which the trust (if applicable with a related party) holds more than 50% (1% in the case of certain investment income), and on which the general CFC rules apply, the items of income of such company will be attributed to the settlors or beneficiaries proportionally as well.
- The aforesaid rules do not apply if the trust or its management is domiciled in an EU/EEA Member State. Nevertheless, the beneficiaries of the income of the trust must additionally provide evidence that they have legally and factually been deprived of the power of disposal over the trust assets.
- If the income from an irrevocable trust is distributed to beneficiaries residing in Germany, it is taxable in Germany provided that there has been no taxation according to German CFC legislation. Thus, the German CFC law takes priority over the German income tax law.

Furthermore, any distribution by a trust to a German tax resident is subject to German gift tax.

This tax impact can be mitigated by the use of alternative entities or vehicles familiar to German civil law, which may achieve the intended economic result. For example:

- *Provisional and reversionary heirs* (*Vor- und Nacherbschaft*): Appointment of a spouse as the provisional heir (broadly speaking, giving full ownership for their remaining lifetime, but subject to certain safeguards that can partially be released by the testator) and children as reversionary heirs (full ownership at the death of the provisional heir).
- *Usufruct/life interest* (*Nießbrauch*): The donor can either retain the usufruct and transfer the asset subject to the usufruct, or retain the asset subject to the usufruct and transfer the usufruct. If an asset subject to a usufruct is transferred, only the value of the asset reduced by the value of the usufruct is subject to tax. If the usufruct ends upon the death of the usufructuary, this is not subject to tax.

7.2 Foundations

According to German civil law, a foundation (*Stiftung*) is an organization whose assets are dedicated to promoting a special purpose set by the founder. Usually, the capital of the foundation needs to be preserved and only the income is spent for the defined purpose. A foundation has its own statutes regulating its organizational structure and codifying the purposes set by the founder. A foundation has no members or shareholders and is formed as a legal entity.

The foundation is formed as a legal entity by way of a unilateral declaration of intent (*Stiftungsgeschäft*) of the founder and the approval of the supervising local authority (*Stiftungsaufsichtsbehörde*). The founder declares to establish the foundation, gives the statutes and endows the original capitalization. The statutes set out the purpose and regulations for the organization of the foundation.

It is also possible to set up a so-called dependent foundation, which is not a legal entity but based on a fiduciary arrangement. The following does not apply to a dependent foundation.

Taxation of the foundation

The foundation itself is subject to tax. Charitable foundations exclusively pursue special charitable purposes according to the German General Fiscal Code and enjoy tax shelter. If the only purpose of the foundation is the provision of benefits to the founder's family members (*Familienstiftung*), the foundation is not tax privileged.

Taxation of the endowment with capital — inheritance and gift tax

The endowment with capital of a foundation — either by the first endowment or by an external donation — is a gift because the founder or donor does not receive anything in return (like a share or membership right). If a foundation inherits capital, the inheritance is regarded as an acquirement by reason of death according to the German Inheritance and Gift Tax Act. Such endowments are generally subject to inheritance and gift tax provided that the foundation is factually and legally able to freely dispose of the assets endowed to it by the founder.

If the endowment with capital is subject to inheritance and gift tax, the higher tax rate of tax class III is applicable. For a foundation that is established mainly to foster the interests of one family or specific families in Germany, tax class I or tax class II applies depending on the degree of relationship of the furthermost beneficiary and the founder according to the deed of foundation. In addition, these foundations (*Familienstiftung*) are subject to a special inheritance tax every 30 years (*Erbersatzsteuer*).

The endowment with capital of a charitable foundation in Germany by the founder or donor is tax-exempt from inheritance and gift tax provided that the foundation maintains its charitable status for at least 10 years.

Taxation of the founder — tax deduction of donations

Donations made to charitable foundations are tax deductible up to 20% of the taxable income of the donor or up to 4% of the total of his or her sales, wages and salaries, always within the respective tax year. The precondition for a tax deduction of donations is that the income of the donor is subject to income tax and assessed to taxation.

The first endowment with capital of a foundation or an external donation to the capital of such a foundation entitles the founder or the donor to a tax deduction under the condition that the founder is not the beneficiary to the capital in case the foundation is dissolved.

This means that the founder is obliged to deprive himself or herself of the assets for good in favor of charitable purposes. Donations of individuals to the capital reserve (*Vermögensstock*) of a charitable foundation may be deductible for income or trade tax purposes up to a maximum amount of €1 million in addition to the general tax deduction for donations. Spouses who made an endowment or a donation to a charitable foundation and who are assessed jointly can together deduct up to an amount of €2 million for donations. Donations or endowments to the capital reserve of a charitable foundation can be deducted in the year of payment or in the nine years following. During this 10-year period, the maximum tax deduction of €1 million (€2 million for spouses) can only be requested once.

Taxation of the beneficiaries

The provision of benefits to the beneficiaries (*Destinatäre*) of the foundation is subject to income tax for the beneficiaries. If the benefits are, from an economic point of view, comparable to dividends distributed by a corporation, they are subject to a flat rate withholding tax (*Abgeltungssteuer*) for the beneficiaries. Under certain conditions, German law allows a tax-sheltered charitable foundation to distribute a certain amount of its profit to the founder or his or her family as (appropriate) alimony (with a maximum 30% of the foundation's annual income). These recurring payments are subject to income tax for the beneficiaries with a progressive tax rate.

Furthermore, the distribution of the funds of the foundation when it is dissolved is subject to German gift tax.

8. Grants

Grants to individuals (e.g., for maintenance) can be subject to German Income Tax and to German Inheritance and Gift Tax. Specific tax exemptions can apply.

9. Life insurance

Income from life insurance is, under certain conditions, exempt from German Income Tax. Acquisitions by the beneficiary of life insurance are regarded as a gift or inheritance from the insurance holder, if applicable.

10. Civil law on succession

10.1 Succession

Under the universal succession principle, title and possession transfers automatically at death to the heirs:

- This includes unlimited personal liability for the deceased's debts (limitation may be reached by the use of special legal provisions).
- Legatees under a will have only a personal claim against the heirs with no personal liability of the heirs and only to the extent of the disposable estate.
- The estate is not regarded as a separate legal entity.
- An appointed executor may have the sole right of disposal with regard to the estate for up to 30 years.

Heirs may refuse an inheritance via a disclaimer within six weeks from the date the heir learns of his or her inheritance.

10.2 Forced heirship

The German Civil Code provides strict forced heirship rules enabling certain persons to claim a share of an estate if they are excluded from succession by the decedent's last will.

The descendants, the spouse, the partner of a registered same-sex partnership and the parents of the decedent may claim an amount of up to one-half of their intestacy share (see Section 10.5). Please note that the claim is for cash only and will not entitle the (partially) excluded claimant to any property *in specie* that forms part of the estate.

The forced heirship claim amounts to a cash value equivalent to the share of the FMV of the estate on intestacy:

- Less the FMV of any *inter vivos* gifts from the decedent to the claimant, if at the time of donation the donor stipulated that the gift should be credited against the mandatory share.

- Plus the FMV of any *inter vivos* gift from the decedent to a third person within the 10-year period prior to the death of the decedent. The addition is reduced by one-tenth for each year following the earlier bequest provided the succession takes place on or after 1 January 2010.

According to a ruling of the German Supreme Court with regard to a previous version of the respective provision, the 10-year period will not begin unless the donor gives up any economic use with respect to the gift (e.g., the 10-year period will not begin if a right of usufruct is retained by the donor).

German citizens can avoid these rules only by a pre-death waiver by the potential claimant. Such waiver may, in some events, require separate counsel for the claimant and will be valid only if performed by notarial deed.

10.3 Matrimonial regimes and civil partnerships

German family law distinguishes between three marital property regimes:

- Statutory marital property regime (*Zugewinngemeinschaft* — community of accrued gain): According to this regime, spouses and partners of a registered same-sex partnership hold their assets as separate property during their marriage or partnership, although there are partial restraints on management and disposal. Upon divorce or death, the gain accrued on the property of the spouses or the partners of a registered same-sex partnership during the marriage or the partnership is to be shared. Note that the determination of the claim for such division is subject to a rather complex procedure, which is beyond the scope of this publication. The statutory regime may be modified (within certain limits) by a marriage contract or by a contract between the partners of a registered same-sex partnership (see Section 10.4).

  Upon formal agreement (by marriage contract or by a contract between the partners of a registered same-sex partnership), which has to be implemented by notarial deed, the spouses and the partners of a registered same-sex partnership may elect one of two contractual matrimonial property regimes, which may be further modified (within certain limits) by the contract as well.
- Separation of property (*Gütertrennung*): Under this regime, each spouse or partner of a registered same-sex partnership holds his or her property independently in separate ownership. Management and disposal are not subject to any limitations deriving from the marital status.
- Community of property (*Gütergemeinschaft*): Under this regime, all assets become the joint property of the spouses or the partners of a registered same-sex partnership (common property). Immediate joint ownership is also presumed for any assets acquired by each spouse or partner of a registered same-sex partnership during the marriage or the partnership while this property regime is in force. Assets that cannot be transferred by legal transaction do not become common property (*Sondergut*). Within the marriage contract or the contract between partners of a registered same-sex partnership, the spouses or the partners can agree to exclude certain assets from common property (*Vorbehaltsgut*). Assets acquired on inheritance at death or by gift are also excluded if so stipulated by the decedent or the donor.

10.4 Intestacy

A will is a legal document that regulates an individual's estate after his or her death. Germany will normally accept the formal validity of a will drawn up under the laws of the deceased's domicile, nationality and place of residence at the time the will is made or at the time of death. Whether an individual has the personal legal capacity to make the dispositions in a will is generally governed by the law of the deceased's citizenship.

If there is no valid will at his or her death, the deceased's estate passes under predetermined rules known as intestate succession. Where there are cross-border issues, the conflicts-of-law provisions will be relevant.

A system of succession *per stirpes* governs intestate succession that divides the possible intestate heirs into different orders depending on the relation to the decedent, while the closest applicable order excludes the more distant orders.

1st order	Spouse or partner of a registered same-sex partnership and children
2nd order	Parents and their descendants
3rd order	Grandparents and their descendants
4th order	Great-grandparents and their descendants
Further heirs	More distant relatives and descendants
No heirs	State

Within the first three orders, a system of *per stirpes* distribution and lineal heirs applies. Note that the intestacy rules are partially influenced by the matrimonial property regime. To simplify the depiction, "spouse" refers to "spouse or partner of a registered same-sex partnership" in the following table.

Statutory regime	Spouse and 1 child* survives	Spouse and 2 children* survive	Spouse and 3 children* survive
Community of accrued gain	Spouse: one-quarter + one quarter	Spouse: one-quarter + one quarter	Spouse: one-quarter + one quarter
	Child: one-half	Children: one-quarter each	Children: one-sixth each
Separate property	Spouse: one-half	Spouse: one-third	Spouse: one-quarter
	Child: one-half	Children: one-third each	Children: one-quarter each
Community of property	Spouse: one-quarter	Spouse: one-quarter	Spouse: one-quarter
		Children: three-eighths each	Children: one-quarter each

**Children of a predeceased child of the intestate parent take their parent's share.*

In the event that only the spouse or the partner of a registered same-sex partnership survives (no children), the surviving spouse or the partner of a registered same-sex partnership is entitled to one-half of the estate if relatives of the second order or grandparents of the decedent are still alive at that time, and is entitled to the whole estate if only more distant relatives of the decedent are alive.

10.5 The EU Succession Regulation (EU-*Erbrechtsverordnung*)

Succession planning for people who take up residences abroad and own assets that are located in various jurisdictions is a very complex subject because of the diversity of both the substantive inheritance law rules and the conflict-of-law rules.

The EU Succession Regulation, which is binding for Germany, subject to very few exemptions, harmonizes the conflict-of-law rules on cross-border successions of 24 EU Member States and is by law directly applicable to all deaths on or after 17 August 2015. The United Kingdom, Denmark and Ireland, along with Switzerland and other countries which are not part of the EU, are not directly bound by it but may also be affected.

The regulation aims to enable EU citizens to organize succession matters in advance.

From a German perspective, the applicable law on successions on or after 17 August 2015 is basically the law of the state in which the deceased had his or her habitual residence at the time of death.

Testators are entitled to make a choice of law and determine the law applicable to their succession. This choice of law is, however, restricted to the law of nationality of the deceased at the time of making the choice or at the time of death and should be made expressly in the form of a disposition of property upon death.

11. Estate tax treaties

11.1 Unilateral rules

Foreign tax on the acquisition of certain foreign assets by death or gift, which is comparable to the German Inheritance and Gift Tax, can be credited against the *ErbSt* falling to the acquisition of these assets.

11.2 Double-taxation treaties

Germany has concluded estate, inheritance and gift tax treaties with the following countries: Denmark, France, Greece (applies only to inheritance tax regarding movable property), Sweden, Switzerland (applies only to inheritance tax; corresponding application to gift tax only for business assets and very specific cases) and the United States.