

4. GERMANY

4.1. Civil Law Framework

The German foundation is, as the foundation in many other countries, an institution that can be traced back to the Middle Ages and by means of which assets of the founder are transferred to a foundation in order to maintain these assets permanently and to use the income generated by them for a defined legal purpose.

The majority of German foundations are established under private law and predominantly serve public utility purposes. There are also foundations created under public law (this is often the case of museums). The legal basis can be found in private law, which is regulated in the German Civil Code (Bürgerliches Gesetzbuch, BGB).

4.1.1. Establishment of a Foundation

A foundation is established with a foundation deed and upon recognition by the public authority responsible for the supervision of foundations (Stiftungsbehörde). A distinction can be made between two types of establishments.

Establishment of a Foundation during the lifetime of the Founder

The foundation is established with the written and binding declaration of the founder who has unlimited contractual capacity and the detailed description of the assets to be transferred. The foundation must have statutes in which

- the name,
- the registered seat,
- the purpose,
- the assets, and
- the composition of the board of directors

are stated. The foundation statutes constitute the legal basis of the foundation. While the BGB does not stipulate any minimum capital, the ability to sustainably meet the purpose of the foundation must be ensured. The majority of relevant authorities require a minimum capital endowment of EUR 25,000 or more; this amount may vary from one federal state to another.

Establishment of a Foundation as a Result of Death

Assets may also be transferred to a foundation by means of a testament. The testament must contain all necessary details on the endowment.

4.1.2. Foundation Purpose

The foundation purpose is a centrepiece of a foundation. Neither the foundation's executive bodies nor the founder may act in opposition to the foundation's purpose. The respective supervisory authority examines whether the foundation purpose is observed. Therefore, the foundation purpose as laid down in the statutes must be described as precisely as possible. In order to benefit from tax advantages granted to public utility foundations (but not to other types of foundations), foundations must meet particular requirements as to the foundation purpose. These advantages are described further below.

Private Utility Foundation

According to the German Civil Code, foundations may be established for any purpose that does not endanger public welfare.

The foundation purpose must be defined on a permanent basis, which does not mean that it has to apply forever. For example, a private utility foundation may be transformed into a public utility foundation at a later date.

The foundation statutes may also include a range of purposes which are not related to each other.

Public Utility Foundation

The public utility purpose of a foundation must be precisely worded in the statutes. Otherwise, the requirements for public utility foundations are not met and the foundation is not eligible for tax advantages. Moreover, the statutes have to describe how the purpose of the foundation is to be fulfilled. The tax exemptions only apply if the foundation meets the requirements concerning the purpose, as set forth in the German Fiscal Code (Abgabenordnung, AO).

4.1.3. Governing Bodies of the Foundation

The board of directors is the executive body of the foundation and is responsible for its management and representation. The founder can establish other bodies in addition to the board. These other bodies may also have rights and obligations which must be defined in detail to ensure that the founder's will is consistently pursued. The founder himself may be a member of one of the foundation's bodies and act in this capacity. The room for manoeuvre of the different bodies is however limited by the foundation purpose.

4.1.4. Supervision

The public supervisory authorities are responsible for protecting the foundation from itself and its executive bodies. The supervisory authority may not be the same as the recognising authority. It sees that the board of directors and the other foundation bodies comply with applicable law and observe the provisions set forth in the foundation statutes.

For example, the government supervisory authority may annul a resolution taken by the founder in its capacity as foundation body if this resolution contravenes the original foundation purpose. As a matter of nature, in such cases, the authority has to examine whether its measure is consistent with the principle of proportionality.

4.2. Tax Treatment

4.2.1. Private Utility Foundations

Foundations that do not serve a public utility purpose do not benefit from any tax advantages.

Tax Treatment of Foundation Endowments

▪ At the level of the Foundation

If a foundation is established *causa mortis*, inheritance tax applies to endowments; if it is set up *inter vivos*, gift tax is levied. These endowments are subject to taxation in the unfavourable tax class III.

The only exception to this rule is the family foundation. Here, the income of the foundation is considered as income of the beneficiaries for tax purposes. As a result, the foundation income may be attributed to tax class I. This favourable treatment does not apply to later donations to the foundation, which are subject to the unfavourable tax class III.

Inheritance and/or gift tax are levied on the basis of the following tax rates:

Endowments up to and including (amounts in Euro)	Rate Tax class I	Rate Tax class II	Rate Tax class III
52,000	7	12	17
256,000	11	17	23
512,000	15	22	29
5,113,000	19	27	35
12,789,000	23	32	41
25,565,000	27	37	47
above 25,565,000	30	40	50

The currently applicable inheritance tax law distinguishes between 3 inheritance tax classes; tax class I is the most favourable, tax class III the least favourable.

Degree of relationship	Tax class	Tax allowance
Spouses	I	307,000
Children, step children, children of deceased children	I	205,000
Grandchildren, parents and grandparents (in the event of inheritance)	I	51,200
Parents, grandparents (except in the event of inheritance), sibling, nephews, nieces, step-parents, parents-in-law/children-in-law, divorced spouses	II	10,300
Domestic partners	III	5,200
Other	III	5,200

Furthermore, in individual cases, other exemptions may apply. However, every 30 years, the foundation is subject to notional inheritance taxation which offsets any tax advantages it may have benefited from. Loopholes for creative taxpayers are very limited; these may establish several family foundations to optimise tax allowances.

Real estate transfer tax may be due on the transfer of real estate. In most cases, however, family foundations are set up without consideration and therefore not subject to real estate transfer tax.

▪ **At the level of the founder**

For founders, hidden reserves may be revealed upon withdrawing of assets, which would have consequences with regard to earnings tax.

▪ **Regular Tax Treatment of the Foundation**

The income of private foundations is subject to the full corporate tax rate of 15% and the solidarity surcharge of 5.5% of the corporate tax. Moreover, notional inheritance taxation on family foundations takes place every 30 years in order to ensure that the foundation assets are not parked for generations without inheritance tax being levied on them.

Payments to beneficiaries as well as the deduction of the substitute inheritance tax (Erbsatzsteuer) do not reduce the corporate tax assessment base.

Taxation of Payments to Beneficiaries and upon liquidation

▪ **At the level of Beneficiaries**

Payments by the family foundation to the beneficiaries are subject to personal income taxation as income from capital. As part of the corporate tax reform 2008, the half-income tax rule

was replaced by the final withholding tax as of 1 January 2009. Income (capital income and capital gains) is now taxed at a uniform final withholding tax rate of 25% (plus solidarity surcharge).

▪ **Upon liquidation**

Acquisition upon liquidation of the foundation is considered a gift inter vivos. In this case, as in the establishment of a foundation, family foundations benefit from tax advantages (see “Tax Treatment of Foundation Endowments”).

4.2.2. Public Utility Foundation

The meaning of “public utility” is defined in German law: To be considered as a public utility foundation, a foundation’s activities must be exclusively and directly aimed at altruistic promotion of public welfare. Support of a foreign public must result in positive impacts on the German general public.

Tax Treatment of Foundation Endowments

The transfer of assets in connection with the establishment of a public utility foundation is exempt from inheritance and gift tax as well as from real estate transfer tax.

At the foundation level, assets may be recorded at their book value if the donation is tax-deductible as a special expense at the level of the donor. For the donor, the transfer of assets has the advantage that he does not have to reveal hidden reserves as would have been the case in the event of a withdrawal of these assets.

The donor may, within certain limits, record the endowment to a public utility foundation as a special expense.

Regular Tax Treatment of the Foundation

Public utility foundations are exempt from corporate tax and value-added tax (for general welfare, events or youth welfare) or subject to a reduced value-added tax rate of 7% (for other services). Moreover, public utility foundations are exempt from tax on land and buildings.