



Taxation of Funds in Germany from 2018

A guide to Taxation of Foreign and German Funds in Germany from 2018 onwards

April 2020



Preface

Following the publication of the German Investment Tax Reform Act (InvStRefG) of 19 July 2016 in the Federal Law Gazette on 26 July 2016, a fundamental reform of investment taxation shall come into force from 1 January 2018 onwards. For mutual investment funds, the central elements of the new legislation are the elimination of the "transparent" taxation system through the separate taxation of investment funds and investors combined with flat-rate taxation (advance lump sum) at investor level. The existing (semi-)transparent taxation system in place until 2017 – with various modifications – will continue to apply solely to special investment funds. In addition to the German tax authorities' desire to simplify fund taxation and prevent tax arrangements, this reform was driven in particular by the risks posed by the existing legislation under EU law. The tax-exempt status of German investment funds means that domestic investment funds can receive German dividends and rental income tax-free until 2017, whereas foreign investment funds are subject to a definitive corporation tax burden of at least 15% even after any Double Taxation Avoidance Treaty (DTT) reduction.

It is common understanding in German tax literature, that the German Investment Tax Act (InvStG) in the version applicable until 2017 contravenes EU law insofar as foreign investment funds whose income from German sources is subject to limited tax liability are placed in a worse position than German investment funds.

The literature also contains analysis that the InvStG in the version applicable from 2018 onwards contravenes EU law insofar as the introduction of corporation tax for domestic and foreign investment funds required under EU law would result in relief solely for German investors due to the system of partial exemption. For German dividend and rental income received until 2017, foreign funds should file so called EU-law-claims in order to enable their investors to profit from later repayments and to avoid expiration of deadlines. For German dividend and rental income received from 2018 onwards, foreign and German funds should file so called EU-law claims to the extent they have foreign fund unit holders.

The aim of this brochure is to present the new legal situation for investment funds marketed in Germany. The brochure is taking into account the Finance Law for 2018 from 11 December 2018 (published in the Federal Law Gazette I no. 45, page 2338). In particular, it takes a closer look at the qualification of different fund products, the taxation of funds and their German investors, the duties and obligations of funds, and aspects of the post-facto examination of tax bases.

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1. Introduction

Domestic and foreign funds may be subject to the provisions of German tax law if they have German investors or generate German income.

The most important body of regulations for fund taxation is the German Investment Tax Act (InvStG), which was extensively revised with effect from 1 January 2018 by the German Investment Tax Reform Act (InvStRefG) of 19 July 2016. The InvStRefG was published in the Federal Law Gazette on 26 July 2016.

The InvStRefG makes a distinction between four independent taxation systems:

1. **Mutual investment funds (e.g. UCITS-funds, AIF which do not qualify for special funds or partnerships, exchange traded funds):** The basis is provided by a "non-transparent" taxation system for mutual investment funds that centres on the separate taxation of funds and investors in the same way as for other corporations. With the exception of special investment funds, non-UCITS partnerships and funds subject to special legislation, this system initially applies to all investment vehicles irrespective of their legal structure or investor base.
2. **Special investment funds (funds for institutional investors which are limited to a maximum of 100 investors and which comply with certain investment restrictions):** The semi-transparent taxation procedure that applies for all investment funds until 2017 will be retained for special investment funds under certain conditions.
3. **Non-UCITS-partnerships (e.g. Venture Capital funds, Private Equity Funds, Real estate funds, Ship funds, Wind farm funds provided that all these funds have the legal form of a partnership (e.g. Limited Partnerships, Lux SCS, German OHG, German KG)):** Non-UCITS funds with the legal form of a partnership are subject to the general German provisions on taxation, which provide for transparent taxation at investor level.
4. **Funds subject to specific legislation, e.g. capital investment companies in terms of the German capital investment act, REIT stock corporations and REIT corporations within the meaning of the German REIT Act.**

1.1. Overview of general provisions for the taxation of German investors

As a special type of income from capital assets within the meaning of Section 20 (1) No. 3 German Income Tax Act (EStG), income from mutual investment funds is subject to withholding tax of 25% plus solidarity surcharge of 5.5% for German fund investors, resulting in a total tax rate of 26.375%, unless the income is from an investment fund held in working capital (natural persons holding fund units as private assets). Capital income is tax-exempt up to the flat-rate savers' allowance of EUR 801 (or EUR 1,602 for married couples or life partnerships filing jointly). If the so-called assessment option is exercised, persons with low total income may be subject to a lower tax rate or may even be tax-exempt. Income from other funds (e.g. partnerships) may also constitute capital income (including in part as well as other income (e.g. rental and lease income, income from business enterprises or other income), in which case it is subject to the general progressive income tax rate based on the level of total income.

If a natural person whose domicile or habitual residence is in Germany holds fund units in working capital, the progressive income tax rate based on the level of total income is applied (from 0% if the total income is lower than the basic personal allowance to over 45% plus solidarity surcharge of 5.5% (total 47.47%) for high levels of total annual income). Income from investment shares may also be subject to trade tax.

For German corporations, income from investment funds is generally subject to corporation tax at a rate of 15% plus solidarity surcharge of 5.5%, resulting in a total tax rate of 15.825%.

Natural persons whose domicile or habitual residence is in Germany and who do not hold fund units in their business enterprises

- Income from capital assets (e.g. income and profits from investment funds in accordance with Section 20 (1) No. 3 EStG): Withholding tax of 25% plus solidarity surcharge of 5.5% = 26.375%
- Other funds not giving rise to capital income: Individual tax rate of up to 45 % plus solidarity surcharge of 5.5% or over depending on total annual income

Natural persons whose domicile or habitual residence is in Germany and who hold fund units in their business enterprises

- Individual tax rate of up to 45 % plus solidarity surcharge of 5.5% or over depending on total annual income
- Trade tax as applicable

Corporations whose domicile or management is in Germany

- Corporation tax of 15% plus solidarity surcharge of 5.5% = 15.825%
- Trade tax in principle



1.2. Overview of the tax treatment of different funds for German investors

For the taxation of funds and their investors, the above qualification in accordance with the InvStG into

- mutual investment funds,
- special investment funds,

— non-UCITS funds with the legal form of a partnership and

— funds subject to special legislation

is particularly important as there are considerable differences in the tax treatment for these categories:

(Mutual) investment funds

- 15% corporation tax for certain German income at fund level
- Fund distributions taxed at investor level
- Minimum annual taxation at investor level (advance lump sum)
- Gains on disposal taxed at investor level (less advance lump sums already taxed)
- System of partial exemption at investor level to compensate for pre-taxation at fund level

Special investment funds

- 15% corporation tax for certain German income at fund level (but transparency option if investor taxation documented)
- Fund income and profits taxed at investor level on distribution (transparency principle)
- Certain fund income and profits reinvested over a longer period taxed at investor level on reinvestment at the end of the fund's financial year

Non-UCITS funds with the legal form of a partnership

- Complete transparency for German income and corporation tax purposes
- All income and profits of the partnership taxed at the level of the German investor at the end of the financial year (partnership is transparent)
- Blocking effect of a foreign permanent establishment under DTT law may be reversed by the German International Transactions Tax Act

Funds subject to special legislation

- Taxation varies considerably depending on the type of vehicle, e.g. REIT stock corporations and their investors are taxed in accordance with the German REIT Act

2. Mutual Investment funds

2.1. Tax qualification under the German Investment Tax Act from 2018

In accordance with Section 6 ff. InvStG in conjunction with Section 1 InvStG, all

- UCITS (funds which comply with the requirements of the Directive 2009/65/EG of the European Parliament and -Council of 13 July 2009 concerning the coordination of legal and administrative provisions regarding certain undertaking for collective investment in securities (UCITS)),
 - AIFs (any collective investment undertaking, including investment compartments thereof, which raises capital from a number of investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors and which does constitute a UCITS),
 - single-investor funds and
 - tax-exempt, non-operational corporations
- are classified as mutual investment funds,

unless they are

- special investment funds,
- funds with the legal form of a partnership that do not qualify as UCITS or pension plan asset funds, or
- funds subject to special legislation.

In addition to securities funds defined and regulated by the supervisory authority (UCITS) and alternative funds (AIF), this means that the definition of (mutual) investment funds is initially extended to include single-investor funds and tax-exempt, non-operational corporations and then limited to exclude funds with the legal form of a partnership that do not qualify as UCITS or pension plan asset funds and funds that are subject to special legislation:

(Mutual) Investment funds	Other funds or vehicles
<ul style="list-style-type: none"> — AIFs — UCITS — As well as: <ul style="list-style-type: none"> - Single-investor funds - Tax-exempt, non-operational corporations 	<ul style="list-style-type: none"> — Special Investment Funds — Partnerships that do not qualify as UCITS or pension plan asset funds — Funds subject to special legislation, e.g. certain holding companies, certain pension providers, certain public institutions, certain equity investment companies, public capital investment companies, REIT stock corporations

2.2. Taxation

2.2.1. Taxation at fund level

From 1 January 2018, certain German income of both German and foreign funds will be subject to corporation tax in accordance with Section 6 InvStG, namely

- dividends from German corporations,
- certain compensation payments for such German dividends,
- rental and lease income from German properties (land, buildings, residential property and land rights),
- gains on the disposal of German properties and
- certain other income from German sources.

For German dividends and any other income subject to withholding at source, the corporation tax liability is settled when the tax is withheld. Including the solidarity surcharge of 5.5% of the corporation tax, the corporation tax and withholding tax amount to 15% exactly (corporation tax of 14.218% plus solidarity surcharge of 0.782%).

Rental income and gains on the disposal of German properties are generally assessed for income tax purposes, meaning that any costs in connection with the property can be deducted, for example. In this case, the corporation tax rate is 15% plus solidarity surcharge of 5.5% = 15.825%.



2.2.2. Taxation at investor level

(year) in which the distribution is paid to or reported by the investor.

2.2.2.1. Taxable transactions

In accordance with Section 16 InvStG, the following income from (mutual) investment funds is taxable for German investors:

- **Distributions** from the investment fund in accordance with Section 2 (11) InvStG

The investor has taxable income in the amount distributed to the investor from the investment fund in the assessment period

- **Advance lump sums** in accordance with Section 18 InvStG

In the case of investment funds that reinvest (rather than distributing) or that distribute less than the minimum annual taxable basic income of the investor, the investor is taxed at least in the amount of the advance lump sum. The advance lump sum is the amount by which the dividends of an investment fund within a calendar year fall below the basic income for that calendar year. Basic

income is calculated by multiplying the redemption price for the investment share at the start of the calendar year by 70% of the base rate in accordance with Section 18 (4) of the InvStG. Basic income is limited to the excess of the last redemption price for the calendar year over the first redemption price for the calendar year plus the distributions during the calendar year. In the year in which the investment shares are acquired during the year, the advance lump sum is reduced by one-twelfth for each full month preceding the month of acquisition. The advance lump sum is deemed to have accrued

on the first working day of the following calendar year (usually 2nd January).

- **Gains on the disposal** of (mutual) investment fund units in accordance with Section 19 InvStG

The gain on disposal is the difference between the proceeds on disposal and the acquisition cost less advance lump sums declared during the period of ownership (as these have already been taxed but are still included in the proceeds/redemption price on disposal).

2.2.2.2. Overview

Distribution	Advance lump sum	Gain on disposal
<ul style="list-style-type: none"> — Timing: Taxable in year of distribution — Amount: Amount of distribution 	<ul style="list-style-type: none"> — Timing: Taxable on 2 January of the following calendar year — Amount: 70% x base rate in accordance with Section 18 (4) InvStG x redemption price at the start of the calendar year – distributions during the calendar year (or increase in the value of the fund units during the calendar year, if lower) 	<ul style="list-style-type: none"> — Timing: Taxable on disposal of fund units — Amount: Proceeds on disposal - acquisition cost - advance lump sums during period of ownership

2.2.2.3. System of partial exemption

In accordance with Section 20 InvStG, distributions, advance lump sums and gains on disposal in connection with fund units are tax-exempt to a certain extent depending on the fund category and investor type (**partial exemption**).

For private investors and life and health insurance companies invested in equity funds and banks holding fund units in their trading book, 30% of the income is tax-exempt (**partial exemption for equity funds**). For natural persons holding investment shares in their working capital, the partial exemption for equity funds amounts to 60%. For investors subject to the German Corporation Tax Act (KStG), the partial exemption for equity funds amounts to 80%.

Half of the partial exemption for equity funds is applied in the case of mixed funds (**mixed fund exemption**).

60% of the income from real estate funds is tax-exempt if the investment conditions state that at least more than 50% of the value of the investment fund is permanently invested in real estate or real estate companies; this increases to 80% of the income if the investment conditions state that at least more than 50% of the value of the investment fund is permanently invested in foreign real estate and foreign real estate companies. Foreign real estate companies are real estate companies that invest solely in foreign real estate (**partial exemption for real estate funds**).

The system of partial exemption can be illustrated as follows:

Investor	Equity fund (more than 50% equities)	Mixed fund (at least 25% equities)	Real estate fund with focus on German real estate	Real estate fund with focus on foreign real estate	Bond fund, money market fund, mixed fund with < 25% equities, alternative investment fund, derivative fund, ETF with or without synthetic replication
Private investor	30%	15%	60%	80%	0%
Life or health insurance company	30%	15%			
Bank (in trading book)	30%	15%			
Natural person (in working capital)	60%	30%			
Corporation	80%	40%			

2.2.2.4. Practical examples

Examples:

An investment fund qualifies as a bond fund. The redemption price at 1 January 2018 is EUR 1,000 per unit and the interest rate in accordance with Section 18 (4)

InvStG, is 14,2857%, so the base rate comes to 10%¹. The assumed interest rate under Section 18 (4) InvStG is not realistic and was only chosen for this example for simplification reasons. A German investor acquires a unit in the investment fund for EUR 1,100 on 1 October 2018. On 31 December 2018 and 1 January 2019, the redemption price per unit is EUR 1,200. The fund did not make any distributions in 2018. On 31 March 2019, the fund distributes EUR 50 per unit. The German investor sells his unit for EUR 1,300 on 3 January 2020.

2 Jan. 2019	Taxable advance lump sum: $\frac{3}{12} \times 10\% \times 1,000 =$	EUR 25
31 Mar. 2019	Taxable distribution:	EUR 50
2 Jan. 2020	Taxable advance lump sum: $10\% \times 1,200 - 50 =$	EUR 70
3 Jan. 2020	Taxable gain on disposal: $1,300 - 1,100 - 25 - 70 =$	EUR 105

¹ The German Ministry of Finance fixed the interest rate under Section 18 (4) InvStG for the year 2019 on 0,07%. According to Section 18 (1) InvStG the base rate for 2019 amounts to 0,049%.

Variation: The fund is an equity fund (more than 50% equities):

Private investors, life or health insurance companies, banks with fund units in their trading books:

2 Jan. 2019	Taxable advance lump sum: $3/12 \times 10\% \times 1,000 \times 70\% =$	EUR 17.50
31 Mar. 2019	Taxable distribution: $EUR 50 \times 70\% =$	EUR 35.00
2 Jan. 2020	Taxable advance lump sum: $(10\% \times 1,200 - 50) \times 70\% =$	EUR 49.00
3 Jan. 2020	Taxable gain on disposal: $(1,300 - 1,100 - 25 - 70) \times 70\% =$	EUR 73.50

The investor is a natural person holding the fund unit in their working capital:

2 Jan. 2019	Taxable advance lump sum: $3/12 \times 10\% \times 1,000 \times 40\% =$	EUR 10
31 Mar. 2019	Taxable distribution: $EUR 50 \times 40\% =$	EUR 20
2 Jan. 2020	Taxable advance lump sum: $(10\% \times 1,200 - 50) \times 40\% =$	EUR 28
3 Jan. 2020	Taxable gain on disposal: $(1,300 - 1,100 - 25 - 70) \times 40\% =$	EUR 42

The investor is another type of corporation:

2 Jan. 2019	Taxable advance lump sum: $3/12 \times 10\% \times 1,000 \times 20\% =$	EUR 5
31 Mar. 2019	Taxable distribution: $EUR 50 \times 20\% =$	EUR 10
2 Jan. 2020	Taxable advance lump sum: $(10\% \times 1,200 - 50) \times 20\% =$	EUR 14
3 Jan. 2020	Taxable gain on disposal: $(1,300 - 1,100 - 25 - 70) \times 20\% =$	EUR 21

Variation: The fund is a real estate fund with a focus on foreign real estate (more than 50% foreign real estate):

2 Jan. 2019	Taxable advance lump sum: $3/12 \times 10\% \times 1,000 \times 20\% =$	EUR 5
31 Mar. 2019	Taxable distribution: $EUR 50 \times 20\% =$	EUR 10
2 Jan. 2020	Taxable advance lump sum: $(10\% \times 1,200 - 50) \times 20\% =$	EUR 14
3 Jan. 2020	Taxable gain on disposal: $(1,300 - 1,100 - 25 - 70) \times 20\% =$	EUR 21

2.2.2.5. Implications under EU law

It is common understanding in German tax literature, that the InvStG in the version applicable until 2017 contravenes EU law insofar as foreign investment funds whose income from German sources is subject to limited tax liability are placed in a worse position than German investment funds. Several claims are currently pending

at the Federal Tax Court (case number I R 1/20 and I R 2/20). The literature also contains analysis that the InvStG in the version applicable from 2018 onwards contravenes EU law insofar as the introduction of corporation tax for domestic and foreign investment funds required under EU law would result in relief solely for German investors due to the system of partial exemption.

The further development of these discussions should be carefully observed by foreign investment funds in particular. For German dividend and rental income received until 2017, foreign funds should file so called EU-law-claims in order to enable their investors to profit from later

repayments and to avoid expiration of deadlines. For German dividend and rental income received from 2018 onwards, foreign and German funds should file so called EU-law-claims to the extent they have foreign fund unit holders.

2.3. Tax Duties and obligations

2.3.1. Tax duties of the fund

If the investment fund has taxable income in Germany that is subject to withholding at source (especially withholding tax) at a rate of 15% (corporation tax of 14.218% plus solidarity surcharge of 5.5%), as is the case e.g. for German dividends, the tax liability is generally settled when the tax is deducted, meaning that there is no further obligation to submit a tax return. In exceptional circumstances, however, the mutual investment fund may be able to reduce this tax rate under the terms of a double taxation convention between its country of residence and Germany; in this case, it must submit a corresponding claim for reimbursement to the German Federal Central Tax Office in Bonn.

If the investment fund has taxable income in Germany that is subject to a rate of 15.825% (corporation tax of 15% plus solidarity surcharge of 5.5%) and for which an annual tax assessment is required to be conducted, the investment fund must prepare an annual corporation tax return including this income and the associated costs and submit it to the tax office in whose territory the fund's assets are substantially located.

2.3.2. Investor reporting

Mutual investment funds are required to communicate fund prices/redemption prices to the central German data provider WM Datenservice on each valuation date. Banks and investors require this information to calculate the advance lump sum in accordance with Section 18 InvStG (70% x interest rate in accordance with Section 18 (4) InvStG x redemption price at start of year – distributions) and the gain on disposal in accordance with Section 19 InvStG (proceeds on disposal – acquisition cost – advance lump sums already taxed during period of ownership). Mutual investment funds are also required to inform WM Datenservice of the amount of their distributions in accordance with Section 2 (11) InvStG. For the purposes of the system of partial exemption in accordance with Section 20 InvStG, all mutual investment funds are additionally required to inform WM Datenservice as to whether the fund is an equity fund, a mixed fund, a real estate fund with an investment focus on Germany, a real estate fund with a foreign investment focus, or another type of fund (money market fund, bond fund, alternative fund etc.).

Investor reporting by mutual investment funds via WM Datenservice

On each valuation date: Redemption price

On distribution: Amount of distribution

On fund launch or start of marketing: Fund qualification

2.4. Tax audit by the German tax authorities

In accordance with Section 5 InvStG, the responsible tax authority is authorised to examine the tax situation of the mutual investment fund and the bases for tax assessment of the investor, including the possibility of an on-site external tax audit. In particular, this includes examining the fund's qualification as a mutual investment fund and the appropriate taxation of the mutual investment fund in terms of corporation tax on domestic income. For German investment funds, the responsible body is the tax office in whose territory the asset management company is managed (Section 4 (1) InvStG). For foreign investment funds, the responsible body for domestic income not subject to withholding (e.g. rental income from domestic real estate) is the tax office in whose territory the investment fund's domestic assets are substantially located.

The German Federal Central Tax Office in Bonn is responsible for all other income of the investment fund as well as the question of qualification as an investment fund. Due to the principle of territoriality, it is evident that the German tax authorities cannot conduct an on-site audit of foreign investment funds. In certain cases, however, foreign authorities may be able to provide administrative assistance. In addition, Section 90 (3) AO states that German taxable entities have an increased duty to cooperate and keep records in the case of investments abroad. Any breach of this duty may result in an external tax audit or the application of a less advantageous base for tax assessment.

3. Special investment fund

3.1. Tax qualification under the German Investment Tax Act from 2018

In accordance with Section 26 ff. InvStG, all UCITS, AIFs, single-investor funds and tax-exempt, non-operational corporations are classified as special investment funds unless they are non-UCITS funds with the legal form of a partnership or funds subject to special legislation and

- the purpose of the fund is limited to the investment and management of the funds for joint account of the investors,

- its assets are not entrepreneurially managed to a material extent, and
- the fund complies with certain investment provisions defined in Section 26 InvStG.

(Mutual) investment funds	Special investment funds
<ul style="list-style-type: none"> — AIFs — UCITS — As well as: <ul style="list-style-type: none"> - Single-investor funds - Tax-exempt, non-operational corporations — But not: <ul style="list-style-type: none"> - Partnerships that do not qualify as UCITS or pension plan asset funds - Funds subject to special legislation, e.g. certain holding companies, certain pension providers, certain public institutions, certain equity investment companies, public capital investment companies, REIT stock corporations 	<ul style="list-style-type: none"> — All of the conditions for (mutual) investment funds — Investment purpose — No material entrepreneurial management — Compliance with and documentation of the investment provisions set out in Section 26 InvStG

In addition to the conditions for mutual investment funds, a special investment fund must therefore satisfy the following conditions:

- Investment purpose, i.e. the purpose of the fund is limited to the investment and management of the funds for joint account of the investors.
- No material entrepreneurial management of the fund assets, i.e. the fund is not entrepreneurially active to a material extent.
- Compliance with and documentation of the investment provisions set out in Section 26 InvStG.

The **investment provisions** set out in Section 26 InvStG can be summarised as follows:

- The investment fund or its manager is subject to the **regulation** of its assets held for collective investment in its country of domicile. This condition is considered to be met for investment funds managed by AIF capital management companies.

Investors may exercise their right to return or redeem their units, shares or equity interest at least once a year.

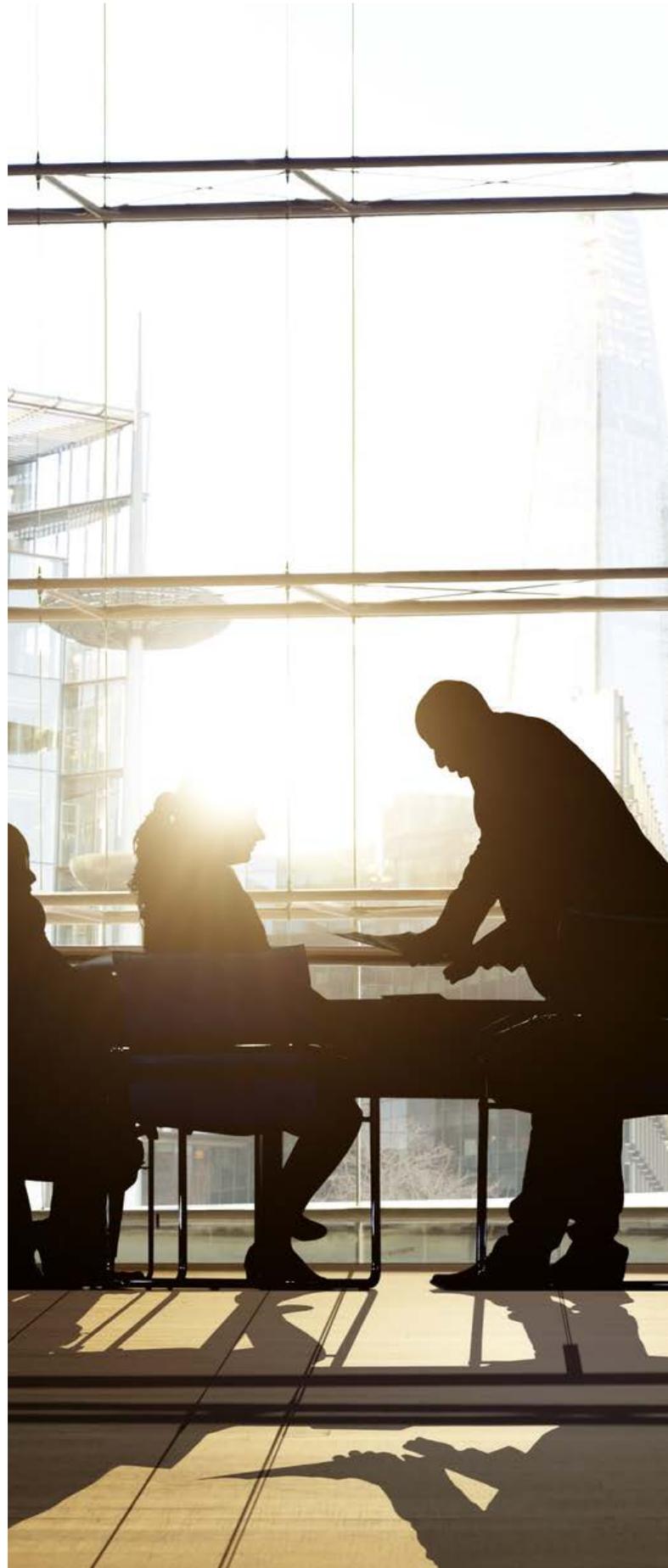
- The fund assets are invested in accordance with the principle of **risk diversification**. Risk diversification is generally considered to exist if the fund assets are invested in more than three assets with different investment risks. The principle of risk diversification is considered to be fulfilled if an investment fund holds units in one or more other investment funds to a not insignificant extent and these other investment funds are invested in accordance with the principle of risk diversification, either directly or indirectly. At least 90% of the value of the investment fund must be invested in the following **assets**:
 - a) Certain (e.g. listed) securities and other investment instruments,
 - b) Money market instruments,
 - c) Derivatives,
 - d) Bank balances,
 - e) Land, land rights and similar rights under the laws of other countries,
 - f) Investments in certain real estate companies,
 - g) Operating and certain other management facilities,
 - h) Units in domestic and foreign undertakings for collective investment in transferable securities (UCITS) and domestic and foreign investment funds fulfilling the criteria of Section 26 InvStG,
 - i) Special investment fund units,

- j) Certain investments in PPP project companies if the market value of these investments can be determined,
 - k) Precious metals,
 - l) Unsecured loans and
 - m) Investments in corporations if the market value of these investments can be determined.
- A maximum of 20% of the value of the investment fund may be **invested in corporations** that are not admitted for trading on, or included in, a stock exchange or another organised market. Investment funds whose investment conditions require that they invest at least 51% of their assets in real estate or real estate companies may invest up to 100% of their value in real estate companies. Investments in companies acquired prior to 28 November 2013 may also be held subject to the 20 % limit.
 - The level of the direct or indirect interest in a corporation held via a **partnership** may not exceed 10% of the capital of the corporation. This does not apply for investments of an investment fund in
 - a) Real estate companies,
 - b) PPP project companies and
 - c) Companies whose purpose is the generation of renewable energies in accordance with Section 5 No. 14 of the German Renewable Energies Act.
 - **Loans** may only be taken out on a short-term basis and up to an amount equivalent to 30% of the value of the investment fund. Investment funds whose investment conditions require them to invest their assets in real estate may take out short-term loans up to an amount equivalent to 30% of the value of the investment fund as well as loans up to an amount equivalent to 50% of the market value of the properties they hold, either directly or indirectly.
 - No more than **100 investors** may participate in the investment fund via partnerships, either directly or indirectly. Natural persons may only invest in an investment fund if

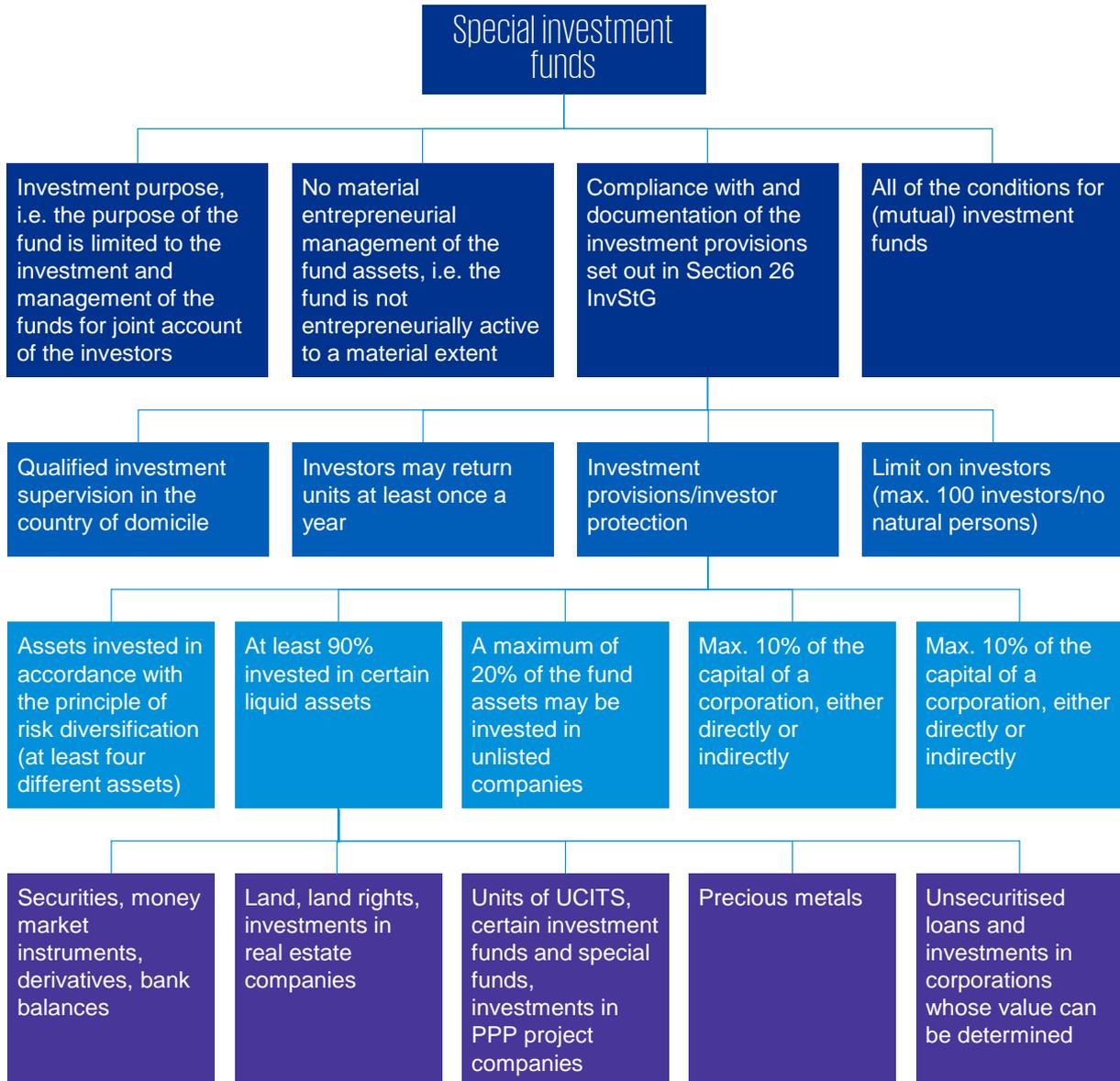
- a) their special investment fund units are held in working capital,
- b) investments by natural persons are required for regulatory reasons or
- c) an indirect investment in a special investment fund was acquired by the natural person prior to 9 June 2016.

The grandfathering provision set out under Point c) applies until 1 January 2020 for investments acquired on or after 24 February 2016 and until 1 January 2030 for investments acquired prior to 24 February 2016. The grandfathering provision set out in Point c also applies to the universal successors of natural persons.

- The special investment fund has a **special right of termination** if the permitted number of investors is exceeded or the investors include persons not fulfilling the criteria of the before mentioned points a) to c).
- The investment provisions are derived from the investment conditions.



The above conditions for qualification as a special investment fund can be illustrated as follows:



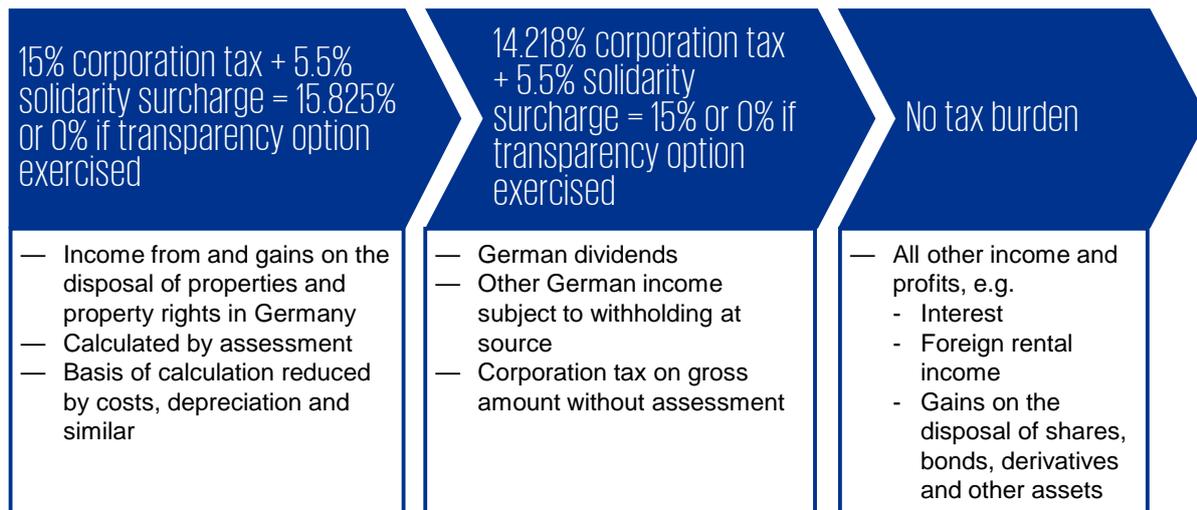
3.2. Taxation

3.2.1. Taxation at fund level

In the same case as for (mutual) investment funds, the following domestic income is taxable for special investment funds:

- German dividend income,
- compensation payments for German dividend income,
- certain other German income subject to withholding at source in Germany, and
- rental income from and gains on the disposal of German properties and property rights.

Unlike a (mutual) investment fund, however, the special investment fund has a so-called **transparency option**, i.e. it may refrain from paying corporation tax if it can demonstrate that the corresponding income is taxed at the level of the German investor in Germany.



3.2.2. Taxation at investor level

In accordance with Section 34 InvStG, the following income from special investment funds is taxable for German investors:

3.2.2.1. Distributed income in accordance with Section 35 InvStG

Distributed income comprises the income calculated by the special investment fund in line with the principles of cash-based accounting for tax purposes in accordance with Sections 37 to 41

InvStG where this income is used by the fund for distributions, and in particular:

- net income from investments, e.g. interest, dividends,
- gains or losses on the disposal of investments, e.g. gains on the disposal of bonds, gains on forward transactions and derivatives, gains on the disposal of equities,
- rental income,
- gains on the disposal of real estate.

3.2.2.2. Dividend equivalents in accordance with Section 36 (1) InvStG

Dividend equivalents are considered to be accrued by the special investment fund investor at the end of the fund's financial year and comprise the following income generated by the special investment fund during the respective financial year (net income):

- interest,
- dividends,
- rental income,
- gains on the disposal of real estate and
- the positive balance of undistributed gains on the disposal of equities/equity interests, gains on forward transactions/derivatives and capital claims/bonds for the last 15 years.

The special investment fund may exercise the so-called transparency option, i.e. it may decide that German income that would ordinarily be taxable at fund level (particularly dividends from German corporations and rental income from/gains on the disposal of German real estate) should not be taxable at the level of the special investment fund, but instead solely at investor level. In this case, this income is considered to be accrued directly to the German investor and hence does not form part of the dividend equivalents (which are only considered to be accrued to the investor at the end of the fund's financial year).

3.2.2.3. Gains on the disposal or return of special investment fund units in accordance with Section 49 InvStG

The gain on disposal is the difference between the proceeds on disposal and the acquisition cost less dividend equivalents declared during the period of ownership (as these have already been taxed but are still included in the proceeds/redemption price on disposal). As in the past, special investment funds will continue to calculate

- the portion of the gain on disposal that is attributable to the equities and equity interests in corporations held by the fund and that therefore may be subject to preferential tax treatment at the level of the investor in accordance with Section 8b KStG (**equity gains**),
- the portion of the gain on disposal that is attributable to gains or income generated by the fund that are tax-exempt at the level of the investor (subject to progression as applicable) under the terms of a double taxation convention (**DTT gains**) and
- additionally from 2018, the portion of the gain on disposal that is attributable to mutual target fund units held by the fund for which the investor would be subject to partial exemption in the case of a direct investment (**partial exemption gains**).

Equity gains, DTC gains and partial exemption gains must be calculated individually for the respective investor.

Distribution	Dividend equivalents	Gain on disposal
<ul style="list-style-type: none"> — Timing: Taxable in year of distribution — Amount: Net income of the special investment fund calculated in accordance with Sections 37 to 41 InvStG where used by the fund for distributions to investors 	<ul style="list-style-type: none"> — Timing: Taxable at the end of the special investment fund's financial year — Amount: Certain net income of the special investment fund for the current year (interest, dividends, rental income, gains on the disposal of real estate) or the last 15 years (realised gains on capital claims/bonds, equities/equity interests and forward transactions/derivatives) if undistributed. — If the special investment fund has exercised the transparency option, the income can be allocated directly to the investors and hence no longer forms part of the dividend equivalents calculated by the fund. 	<ul style="list-style-type: none"> — Timing: Taxable on disposal of fund units — Amount: Proceeds on disposal - acquisition cost - dividend equivalents during period of ownership — Taking into account investor-specific equity gains and real estate gains

3.3. Tax duties and obligations

3.3.1. Tax duties of the fund

In the same way as for mutual investment funds, a foreign special investment fund may reduce its level of German withholding tax if this is permitted under a corresponding double taxation convention and it is subject to corporation tax in the form of withholding tax due to the absence of a transparency option (see the information on mutual investment funds under 2.3.1 above). In the same way as for mutual investment funds, special investment funds may also be required to submit an annual corporation tax return for income not subject to withholding (e.g. rental income from German real estate) if it cannot pass this taxation on to the investor by exercising a transparency option (see the information on mutual investment funds under 2.3.1 above).

3.3.2. Investor reporting

Special investment funds must provide information on their

- distributions and dividend equivalents,
- certain income recognised on a pro rata basis for the period of ownership,
- equity gains (Sections 39, 40 und 48 InvStG),
- partial exemption gains (Sections 40, 43 und 48 InvStG) and
- real estate and DTC gains (Sections 40, 43 und 48 InvStG)

broken down into the relevant income components. In the case of special investment funds, the capital management company (or the German investor in the case of foreign special investment funds, although this is largely impracticable) must also submit a uniform and separate annual statement illustrating the determination of the bases for tax assessment for German investors (Section 51 InvStG).

3.4. Tax audit by the German tax authorities

The German tax authorities are authorised to examine special investment funds and conduct external tax audits in the same way as for mutual investment funds. In accordance with Section 5 (2) No. 2 InvStG, the German tax authorities

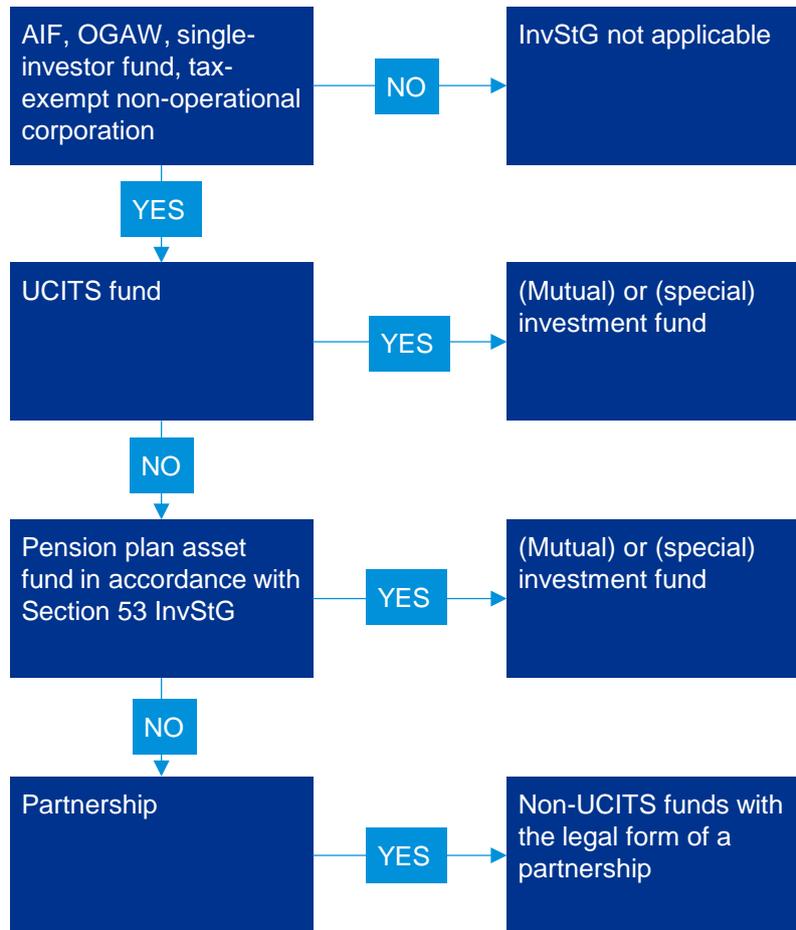
may also examine the conditions for the tax qualification of the fund as a special investment fund (see the information on special investment funds under above).

4. Non-UCITS funds with the legal form of a partnership

4.1. Tax qualification under the German Investment Tax Act from 2018

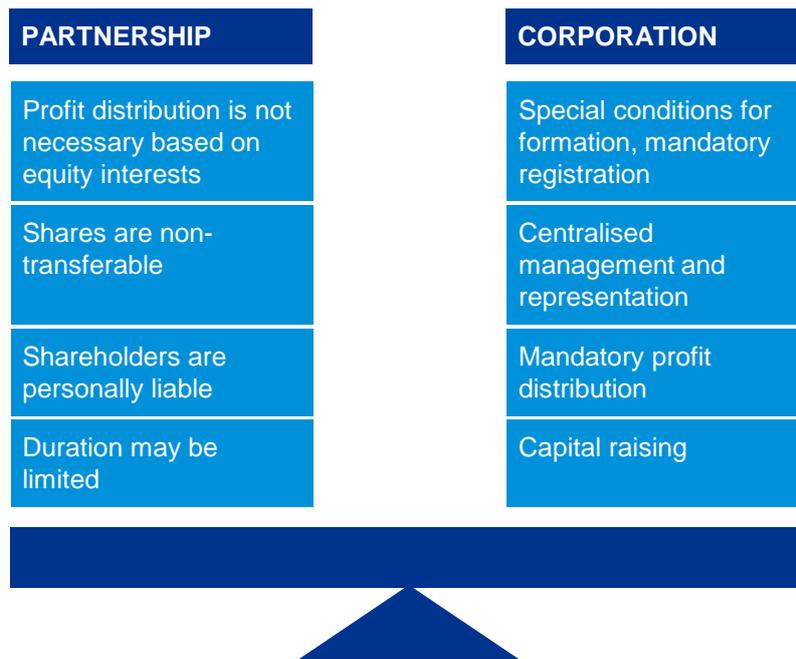
In accordance with Section 1 (3) No. 2 InvStG, partnerships are not considered to be investment funds unless they are UCITS funds or pension plan asset funds in accordance with Section 53 InvStG.

Qualification as a non-UCITS fund with the legal form of a partnership can be illustrated as follows:



As German investors in a partnership are subject to special provisions on taxation, qualification as a partnership is of particular importance. In Germany, partnerships include companies constituted under civil law (Gesellschaft bürgerlichen Rechts, GbR), general partnerships (offene Handelsgesellschaft, oHG) and limited partnerships (Kommanditgesellschaft, KG) in particular. A for-

foreign fund vehicle is considered to be a partnership if it corresponds to the ideal of a German partnership based on a comparison of the respective legal forms. For the purposes of this comparison, the tax authorities have developed the criteria described below. The more criteria of the ideal of a partnership and the fewer criteria of a corporation it fulfils, the more likely a foreign company is to be considered as a partnership:



As decisions based on a catalogue of comparative criteria often involve substantial judgements and normative questions that may pose a barrier to legal certainty in individual cases, the German tax authorities issued a circular by the Federal Ministry of Finance on the application of double taxation conventions to partnerships

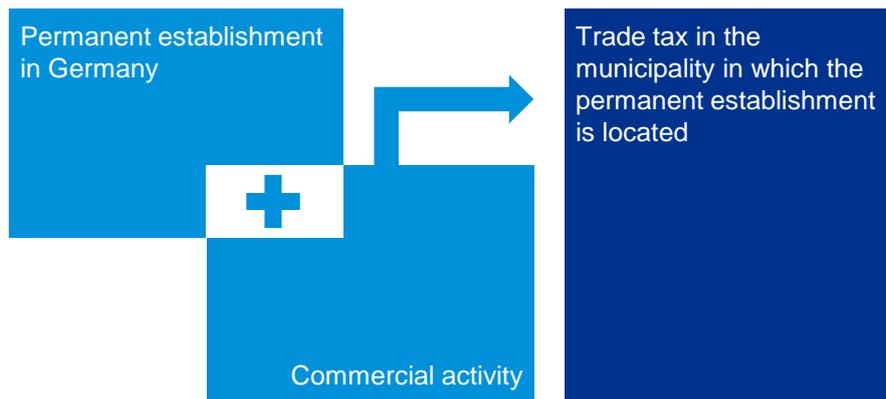
on 26 September 2014 in which it analysed various foreign vehicles to determine whether they constitute partnerships from its perspective. For example, limited partnerships (e.g. in the USA, the UK, the Cayman Islands, Australia), CVs (in the Netherlands) and SCSs (in Luxembourg) are typically considered to be partnerships.

4.2. Taxation

4.2.1. Taxation at fund level

As a partnership is not considered to be a corporation for the purposes of German tax law, no income tax or corporation tax is incurred at the level of the partnership itself.

As domestic business enterprises are taxable for trade tax purposes, German commercial partnerships or foreign partnerships with a permanent establishment in Germany may be subject to trade tax for this establishment in the municipality in which the establishment is located.



4.2.2. Taxation at investor level

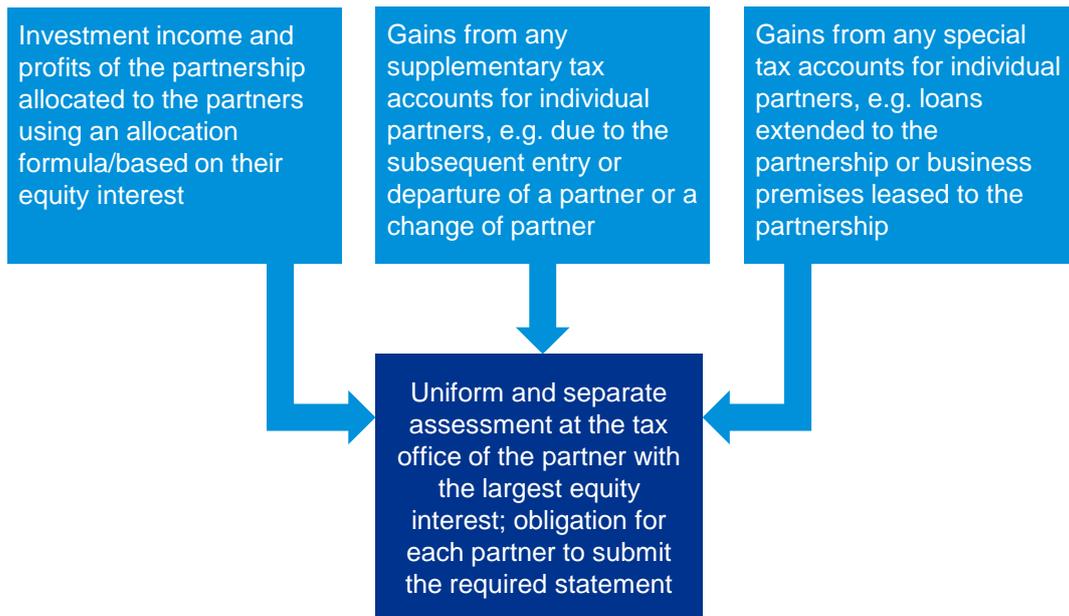
In terms of German investors, partnerships are fully transparent for income tax and corporation tax purposes, i.e. income is taxed directly at the level of the German investors (partners in the partnership).

If multiple German investors are partners in the partnership, the income is assessed uniformly and separately by the tax office of the investor with the largest equity interest in the partnership (Section 180 of the German Fiscal Code (AO)). At the request of this primary tax office, each German partner in the partnership may be obliged to submit a uniform and separate statement illustrating the determination of the bases for tax assessment effective for all of the investors. In practice, the investors will oblige the partnership to prepare this annual statement and submit it directly to the tax office.

The income generated by the partnership during the financial year, i.e. investment income (e.g. income from agriculture and forestry, income from business enterprises, dividends, interest, other capital income, rental income) and gains on the disposal of investments, is allocated directly to the investors at the end of the financial year in proportion to their respective interest in the equity of the partnership. If the investors invested in the partnership at different times, they

will generally have different costs for the individual fixed assets of the partnership. In the case of investors who invest in a partnership at a later date, this is reflected in the preparation of an "Ergänzungsbilanz" (supplementary tax accounts for individual partners) containing positive/negative corrections for fixed assets for which the investor had higher/lower costs. In addition to cases in which an investor invests in a partnership at a later date (where the original investors sell a share of their interest in the partnership to the new partner), this is also relevant for cases in which an investor withdraws from a partnership (where the investor sells its proportionate interest in all of the fixed assets of the partnership to all the other existing partners) and cases in which a change of partner takes place in return for payment (where a partner sells its interest in all of the fixed assets of the partnership to a new partner, typically at market value).

In the case of commercial partnerships, loans taken out by partners in order to finance their equity interest in the partnership and assets, e.g. business premises, that are leased to the partnership are treated as special business assets and included in a "Sonderbilanz" (special tax accounts for individual partners) for the respective partner, thereby ensuring that they are assigned to the partnership for tax purposes.



4.3. Tax duties and obligations

4.3.1. Tax duties of the fund

As partnerships are transparent for the purposes of German income tax and corporation tax, they do not have any tax duties as a matter of principle. As an exception, it may be necessary to submit a trade tax return for permanent establishments located in Germany. If foreign investors generate income with limited tax liability via a partnership in Germany, e.g.

- income from German agriculture and forestry,
- income from a German permanent establishment,
- dividends and certain gains on the disposal of German corporations,

these foreign investors may be required to submit a tax return in Germany (for German income not subject to withholding) or to apply for the partial reimbursement of income subject to withholding under the terms of a double taxation convention.

4.3.2. Investor reporting

The following distinction is made with regard to the tax duties of non-UCITS funds with the legal form of a partnership:

1. If there is only one German investor, this investor is obliged to include all income and profits of the partnership, including any profits or income from the supplementary or special tax accounts it is required to prepare, in its annual income tax or corporation tax return.
2. If there are multiple German investors, a uniform and separate statement illustrating the determination of the bases for tax assessment for all the German investors must be submitted to the tax office of the partnership or the partner with the largest equity interest. At its discretion, the tax office may request that each of the German investors submit such a uniform and separate statement in accordance with Section 180 AO.

In practice, the partnership prepares an "Ertragnisaufstellung" (statement of expenses and income) for the investor in cases where the partnership has a single investor and the annual statements illustrating the determination of the bases for tax assessment for the tax office in cases where the partnership has multiple German investors, as the investors do not generally possess the necessary information and expertise.

4.4. Tax audit by the German tax authorities

In the case of non-UCITS funds with the legal form of a partnership, the German tax authorities may examine the nature, amount and taxation of the income of the partners/investors of the partnership that is subject to limited tax liability in Germany in accordance with Section 193 ff. AO. This relates in particular to income from German permanent establishments and income (and any profits) from German real estate. In the case of income subject to withholding, e.g. dividends paid by German companies or stock corporations, an examination at the level of the withholding agent responsible for withholding the tax, e.g. the last German paying agent in the custody chain, is permitted (Section 193 (2) No. 1 AO).

The separate and uniform statement illustrating the determination of the basis of tax assessment for all investors that is required to be prepared and submitted by the partnership or its tax advisor in the case of partnerships with multiple German investors is generally also subject to an external tax audit. If a foreign partnership has only one German investor, the bases of tax assessment for the partnership may be included in the scope of a tax audit of the investor.

Due to the principle of territoriality, the German tax authorities cannot conduct an on-site audit of foreign investment funds. In certain cases, however, foreign authorities may be able to provide administrative assistance. In addition, Section 90

(3) AO states that German taxable entities have an increased duty to cooperate and keep records in the case of investments abroad.

Any breach of this duty may result in an external tax audit or the application of a less advantageous base for tax assessment.



5. Funds subject to special legislation

5.1. Tax qualification under the German Investment Tax Act from 2018

Certain funds that are subject to special legislation, e.g.	— certain public capital investment companies and
— certain holding companies,	— REIT stock corporations,
— certain pension providers,	are not covered by the provisions of the InvStG, but rather by special legislation or the general provisions of the German Income Tax Act (EStG) or the German Corporation Tax Act (KStG).
— certain public institutions,	
— certain equity investment companies,	

5.2. Taxation

For German investors, there may be significant variations in the tax treatment of funds that are not classified as investment funds on account of being subject to special legislation.

Examples include REIT (Real Estate Investment Trust) stock corporations and REIT corporations that are not classified as investment funds on account of meeting the criteria of the German REIT Act.

Profit distributions and gains on the disposal of such REITS in accordance with the German REIT Act constitute taxable capital income for German private investors (persons holding REIT shares in their private assets) that is subject to

withholding tax of 25% (plus solidarity surcharge of 5.5%, resulting in a total tax rate of 26.375%) unless they constitute commercial income in accordance with specific provisions.

For investors holding REIT shares in their working capital, distributions and gains on disposals are generally subject to income tax (natural persons) or corporation tax (corporations) as commercial income. The 40% tax exemption for natural persons in accordance with Section 3 No. 40 EStG and the "de facto 95% tax exemption for corporations" in accordance with Section 8b KStG only apply if corporation tax was actually deducted within the REITs.

5.3. Tax duties and obligations

As the tax duties of funds subject to special legislation can be extremely varied and complex,

they must be carefully analysed and examined on a case-by-case basis.

5.4. Tax audit by the German tax authorities

The possibility of conducting a tax audit depends on the specific qualification of the fund.

6. Summary

6.1. Tax Qualification of funds

The tax qualification of funds under the InvStG can be summarised as follows:

(Mutual) investment funds	Special investment funds	Non-UCITS-partner-ships	Funds subject to specific legislation
<ul style="list-style-type: none"> — UCITS — AIFs — Single-investor funds — Tax-exempt, non-operational corporations — Not special investment funds — Not: Partnerships that do not qualify as UCITS or pension plan asset funds — Not: Funds subject to special legislation, e.g. certain holding companies, certain pension providers, certain public institutions, certain equity investment companies, public capital investment companies, REIT stock corporations 	<ul style="list-style-type: none"> — All of the conditions for (mutual) investment funds — Investment purpose — No material entrepreneurial management — Compliance with and documentation of the investment provisions set out in Section 26 InvStG 	<ul style="list-style-type: none"> — Legal form of a partnership in accordance with the German tax authorities criteria — Not a UCITS — Not a pension plan and fund 	<ul style="list-style-type: none"> — Vehicle is subject to a lex specialis which overrides the Investment Tax Act 2018

As a result, the InvStG 2018 makes a distinction between four independent taxation systems:

1. **(Mutual) investment funds:** The basis is provided by a "non-transparent" taxation system for mutual investment funds that centres on the separate taxation of funds and investors in the same way as for other corporations. With the exception of special investment funds, non-UCITS partnerships and funds subject to special legislation, this system initially applies to all investment vehicles irrespective of their legal structure or investor base.
2. **Special investment funds:** The semi-transparent taxation procedure that applies for all investment funds until 2017 will be retained for special investment funds under certain conditions.
3. **Non-UCITS-partnerships:** Non-UCITS funds with the legal form of a partnership are subject to the general German provisions on taxation, which provide for transparent taxation at investor level.
4. **Funds subject to specific legislation,** e.g. equity investment companies, capital investment companies, REIT stock corporations and REIT corporations within the meaning of the German REIT Act.

6.2. Tax of funds and investors

The taxation of funds and their German investors in Germany can be summarised as follows:

(Mutual) investment funds

- 15% corporation tax for certain German income at fund level
- Fund distributions taxed at investor level
- Minimum annual taxation at investor level (advance lump sum)
- Gains on disposal taxed at investor level (less advance lump sums already taxed)
- System of partial exemption at investor level to compensate for pre-taxation at fund level
- Annual tax return for German real estate income
- Withholding tax for German dividends may be claimed for reimbursement under a DTT where applicable
- Redemption prices, distributions and fund qualification reported to WM Datenservice
- Audit by the tax office in whose territory the fund's German assets are substantially located or the German Federal Central Tax Office where applicable

Special investment funds

- 15% corporation tax for certain German income at fund level (but transparency option if investor taxation documented)
- Fund income and profits taxed at investor level on distribution (transparency principle)
- Certain fund income and profits reinvested over a longer period taxed at investor level on reinvestment at the end of the fund's financial year
- Annual calculation of distributions and dividend equivalents
- Annual tax return for German real estate income
- Withholding tax for German dividends may be claimed for reimbursement under a DTT where applicable
- Audit by the tax office in whose territory the fund's German assets are substantially located or the German Federal Central Tax Office where applicable

Non-UCITS funds with the legal form of a partnership

- Complete transparency for German income and corporation tax purposes
- All income and profits of the partnership taxed at the level of the German investor at the end of the financial year (partnership is transparent)
- Blocking effect of a foreign permanent establishment under DTT law may be reversed by the German International Transactions Tax Act
- Annual submission of tax return for German real estate income by partners
- Annual submission of uniform and separate statement illustrating determination of bases for tax assessment by partners taxable in Germany if multiple partners; otherwise: mandatory statement of expenses and income for partner
- Audit by the tax office in whose territory the fund's German assets are substantially located, the tax office responsible for uniform and separate determination or the investor's tax office or by the German Federal Central Tax Office where applicable

Funds subject to special legislation

- Taxation and the opportunities for audit and examination available to the German tax authorities vary considerably depending on the type of vehicle, e.g. REIT stock corporations and their investors are taxed in accordance with the German REIT Act

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