

MUNI
LAW

Relationship and tension between succession law and foundation law

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I. Objective of succession law

- management of transfer of the estate (assets and obligation) to legal successor
- substantive law: *who* shall be entitled to the estate?
- procedural law: *how* shall the estate be acquired?

II. Stakeholders in succession law

- Stakeholders in the field of succession:
 - Owner of estate (testator)
 - Heirs and legatees
 - Persons entitled to a compulsory share
 - Creditors of the deceased
 - General public

- Colliding interest between stakeholders

II. A. Owner of the estate (testator)

- interested in to decide on to whom the estate shall be transferred (picking the legal successors)
- interest is protected by testamentary freedom (part of private autonomy)
- guaranteed by the fundamental right of property
- protected by Art 1 of Additional Protocol of the Convention for the Protection of Human Rights, Art 17 of the European Charter of Fundamental Rights, national constitutions (e.g. Art 14 German „Grundgesetz“, Art 5 Austrian „Staatsgrundgesetz“)

II. B. Heirs and legatees

- interested in free decision on to accept or reject the estate or the legacy
- protected by private autonomy: no one has to accept (and obligations!) against his or her will
- in case of acceptance: interest in acquisition of the assets of the deceased
- protection of this interest is not very strong
- „take it or leave it“

II. B. Heirs and legatees

- no protection against wasteful spending of the deceased before his/her death
- no protection against donation the deceased has made
- if there is little left (or nothing left), the heirs (and legatees) will go out empty

II. B. Heirs and legatees

- interested in unrestricted usage and disposition of the assets
- protection of this interest is not very strong
- heirs and legatees in general are bound by restrictions imposed on them by the testator
- e.g. administration of estate by an executor, subsequent succession, conditions, imposition of a burden on how to use (or not to use) the estate etc
- however: can we justify that the will of the deceased („rule of the dead hand“) prevails against the interest of the living for an indefinite period of time?

II. B. Heirs and legatees

- private autonomy of the testator and private autonomy of legal successors have to be balanced
- as a result: binding force of the will of the testator may be restricted by time limits in many legal systems
- E.g. 30 year period for a permanent execution in German law (or until the death of the heir, § 2210 BGB),
- subsequent succession cannot be claimed by a person who was not yet alive at the time when the testator died (Czech law?)

II.C. Persons entitled to a compulsory share

- entitlement to a compulsory share for close family members is protected by fundamental rights in Germany (Art 6: protection of marriage and family, Art 14 protection of property), decision of the Constitutional Court (Bundesverfassungsgericht) 19.4.2005
- protection by fundamental rights less clear in other countries
 - would legislation be allowed to abolish compulsory shares completely?
 - are there any convincing reasons for compulsory shares in modern societies?

II.C. Persons entitled to a compulsory share

- interested in a legal position which cannot be taken away by the free will of the testator
- protection of this interest is strong:
- claim to a compulsory share may be taken away only for severe reasons defined by law (crimes against testator, falsification of a will etc)

II.C. Persons entitled to a compulsory share

- interested not only in a formal legal position, but also in the acquisition of the assets the deceased had owned during lifetime
- interest is protected by a certain share of the estate
- however: if nothing is left, the persons entitled to a compulsory share will receive nothing
- private autonomy of the testator and acquisition interest of the persons entitled to a compulsory share have to be balanced

II.C. Persons entitled to a compulsory share

- no protection against wasteful spending of the testator during lifetime
- however: persons entitled to a compulsory share are protected against donations of the testator during lifetime (donation *inter vivos*) in many legal systems
 - e.g. § 2325 BGB: „Pflichtteilsergänzung bei Schenkungen“ (augmentation of compulsory shares in the event of gifts)
 - § 782 ABGB: „Hinzurechnung von Schenkungen unter Lebenden“ (addition [to the estate] of gifts *inter vivos*)
 - Art 475, 527 ZGB: Herabsetzung von Schenkungen
 - Art 921 Code civil: réduction des disposition entre vifs

II.C. Persons entitled to a compulsory share

- some kinds of gifts are excluded from being taken into account
 - e.g. depending on the time they were made (10 years before the death of the testator in Germany, 5 years in Switzerland, 2 years/indefinite in Austria)

- the way the augmentation of the compulsory share works
 - there is no obligation of the recipient of the gift to return the gift as such to the estate
 - the value of the gift is added to the value of the estate
 - the claim of the person entitled to a compulsory share is calculated on the basis of the sum
 - the augmented compulsory share will be satisfied from the estate
 - as a consequence the amount of the estate which is open for dispositions of the testator is reduced

II.C. Persons entitled to a compulsory share

- the heirs receive less if the estate (assets minus obligations) cannot satisfy the claim for the augmented compulsory share the recipient of the gift is liable for the rest („claw-back“)
- protection of the recipient having received the gift in good faith

- no such protection of persons entitled to a compulsory share in Czech law?

II.D. Creditors of the deceased

- interested in not losing the assets of the estate for enforcing their claims
- transfer of assets to an heir being in bankruptcy (or close to) will put them in a situation of competition with the heir's creditors and might reduce the chance of a complete satisfaction of their claims
- interest is protected by segregation of the estate from the heir's property

II.E. General public

- State as the „heir of the last resort“
 - if no one else is entitled to succession the state may claim the estate
 - protects the estate from being ownerless
- State as being entitled to a compulsory share
 - in an economic sense
 - state is stakeholder in succession process as being entitled to inheritance tax

II.E. General public

- Public interest in economic welfare
- Transfer of assets after death may put businesses (enterprises) at risk
 - Succession law divides the estates among the heirs
 - Property rights in businesses should not be divided among a group of heirs
 - Conflicts between family member might affect the development and stability of a business
 - If testator chooses one single successor to his or her business the estate (and the successor) might not have enough liquid funds to satisfy the monetary claims of the persons entitled to compulsory shares

II.E. General public

- Need for a special succession law for businesses?
 - Special succession law for agricultural estates (farms)
 - e.g. in Germany, Austria, Switzerland
 - one of the heirs will receive the farm
 - has to compensate other heirs by paying a privileged amount of money which is compatible with the continuation of the farm
- Austrian succession law:
 - payment of compulsory share may be delayed by court decision by no more than five years (10 years) by court decision if otherwise the heir would have to sell his business or if the the continuation of the business would be at risk

II.E. General public

- Swiss succession law (as being discussed):
 - Special succession law for all businesses
 - one of the heirs may succeed into the business if not otherwise directed by the testator
 - payment to other heirs may be suspended if required by lack of liquid funds

III. Principles of succession law

Substantive law:

- Testamentary freedom (private autonomy)
- Family succession
 - Intestate succession
 - Compulsory shares
- Protection of general public interests

Procedural law

- Universal succession
- entire estate is transferred to the heirs by one event (death of owner) or legal act (court decision)
- „take it or leave it“: no cherry picking by heirs
- Universal succession is mandatory law: no opting out by testament

IV. Basic elements of a foundation

- Legal person, but not a corporation
- Difference between foundation and corporation
 - Foundation does not have members or shareholders
- *Essentialia negotii* of a foundation
 - Intention of the founder to establish a foundation
 - Definition of a purpose (welfare of public benefit or beneficiaries)
 - Endowment of assets
- Some jurisdictions allow foundations to be combined with elements of a corporation
 - e.g. founder may reserve the right to change the statutes or even terminate the foundation
 - comes close to a single-member corporation

V. Foundation and succession law

- Depending on the jurisdiction the purpose of a foundation may be broader or narrower
- foundation may be restricted to public benefit purposes (like sponsoring scientific projects, running a museums, supporting homeless people or refugess etc)
- foundation may also be allowed to promote private purposes
 - e.g. „family foundation“: purpose of a foundation is to promote the welfare of the founder itself, his/her family members, children, grandchildren etc

V. Foundation and succession law

- Family foundation may be accepted only under certain conditions or without any restrictions:
- See Art 335 ZGB: family foundation may only cover the costs of education, endowment and support of family members or similar purposes
- Austrian law, Liechtenstein law: family foundation is open to any transfer of assets of the foundation to beneficiaries (whoever they may be) without any restrictions

V. Foundation and succession law

- consequence: the broader the purpose of a foundation may be defined the better a foundation can be used as an instrument of an intergenerational transfer of wealth
- foundations may serve as a functional equivalent of a will
 - „will substitute“
- foundation law may be more liberal than succession law
- foundations may be used to circumvent restrictions and principles of succession law
- see the following examples (based on Austrian law)

V. Foundation and succession law

□ Example # 1:

- succession law: the heir must be chosen by the testator in the will; choice cannot not be left to someone else (§ 564 ABGB)
- foundation law: the founder may leave to the foundation board to decide upon the beneficiaries (within the defined purpose of the foundation)

□ Example # 2:

- succession law: agreement as to succession („Erbvertrag“) may only be concluded between spouses and may cover only three fourths of the estate (one fourth must be left to disposition by testament)
- foundation law: no such restrictions exist. Foundation may be established by any two (or even more) people who can be the beneficiaries of the entire assets transferred to the foundation upon the death of the other founder

V. Foundation and succession law

□ Example # 3:

- succession law: gifts made to a person who is not entitled to a compulsory share lead to the augmentation of compulsory shares when made within two years before the death of the owner
- gifts made to a person entitled to a compulsory share lead to the augmentation of compulsory shares when made any time before the death of the owner (no time restriction)
- can compulsory shares be avoided by transferring assets to a foundation?
- foundation is not entitled to a compulsory share: two year time period applies
- however: if founder has reserved the right to terminate the foundation or to change the statutes of the foundation fundamentally, two year period will not be triggered before the founder has not waived such rights

V. Foundation and succession law

- Two years period is triggered only when founder has given up ownership of assets transferred to the foundation irrevocably („asset sacrifice doctrine“)
- Result: in theory good protection of compulsory shares
- in practice there are ways to avoid the augmentation of compulsory shares
- founder reserves the right to terminate the foundation by consent of the foundation board whose member he had chosen before
- founder did not reserve the right to terminate the foundation or to change the statutes fundamentally but runs the foundation as a factual organ (the foundation board accepts any of his decisions, authorizes him to manage and dispose over the assets etc)
- foundation law is a challenge for the protection of compulsory share

VI. Conclusion

- Tensions between foundation law and succession law because foundation may serve as a functional equivalent of a will
- Tensions cannot be overcome by means of interpretation of succession law because it is the intention of legislation that foundation law is more liberal than succession law
- However: if foundation law does not do any harm without those restrictions of succession law why not letting succession law follow the example of foundation law and make it more liberal as well?