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Private foundations and trusts: just the same but different?

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Abstract

Foundations were originally conceived in Mediaeval Europe in relation to charitable purposes: they were the first instance of 'legal persons', a concept that lies at the basis of Western corporate law. Family foundation evolved in Continental Europe over the centuries in such a way as to perform some of the functions which are typically associated with private express trusts in the English legal tradition. The practice of private foundations has evolved into three models: (i) the 'classic' family foundation that was originally codified in Liechtenstein in 1926, (ii) the Dutch foundation or 'stichting', and (iii) the common law foundation. Private foundation statutes have been recently enacted in a number of common law jurisdictions as an ingenuous combination of trust law and company law principles.

A wave of private foundation statutes has been conspicuous for the last decade in many leading trust jurisdictions as well as in some less prominent international financial centres. Interestingly, the recent addition of private foundations to the 'tool-box' of most offshore jurisdictions in the common law tradition is evocative of the attempt by a number of civil law jurisdictions to come to terms with trusts, either by way of 'recognition' under the Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on their Recognition or under equivalent private international law provisions or in some cases even by operation of special legislation purporting to create statutory equivalents to the common law trust.[1] In fact, private foundations are established legal arrangements in many areas of continental Europe, where they have performed for centuries many of the estate planning and wealth management functions which have been traditionally associated with trusts in the common law world. The very concept of a foundation, although originally for a charitable rather than a private purpose, was at the origin of the notion of legal personality, which lies at the basis of corporate law in the Western legal tradition.

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Trust law has evolved along different paths in England, in the USA, and in different areas of the Commonwealth, so that it is possible to identify different trust 'models'. Similarly, at least two 'models' of private foundations may be identified in continental Europe, one of which is more closely associated

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1. The phrase 'common law trust' is loosely used here with a view to identifying a legal tradition rather than a legal system within it. In other words, common law is mentioned in contrast to civil law and not to equity.

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with the Germanic legal tradition, and the other relies on the Dutch experience. A third model appears to result from the recent legislative experiences of a number of common law jurisdictions, where some distinctive elements of trust law and company law are combined with a view to shaping an ingenuous legal arrangement fitting the main features of its civil law reference.

From Mediaeval asset protection to German jurisprudence: foundations as 'legal persons'

The first instance of legal reasoning in relation to what would be established as a 'foundation' appears to have been conducted by a Moses, archbishop of Ravenna (Italy), who is reported to have died in 1154.[2] The learned clergyman dealt with the following legal question: who owns the property of a monastery that has been abandoned by all its monks? Far from being a purely academic issue, that question had a relevant implication in terms of what may be described in contemporary terms as 'asset protection' from the point of view of the Mediaeval monastic orders. Monks would often flee their cloisters at the perspective of a raid by Norsemen or Sarasin pirates: in the absence of a convincing alternative solution the relevant property would be seized by the papal administration in Rome as *res nullius* (nobody's property). Moses's suggested solution would rely on the idea that the buildings (or rather 'the walls') should be deemed to own the properties contained within their boundaries. A more sophisticated rendering of the same notion is credited to Sinibaldo de' Fieschi, a cardinal and distinguished professor of canon law at the University of Bologna who became pope in 1243 under the name of Innocent IV until his death in 1254. The Western legal tradition owes the legal fiction of a 'legal person', or an incorporated entity capable of owning property in its own right, to Sinibaldo de' Fieschi's ingenuous contention that the monastery should be deemed to be a person (*collegium fingatur una persona*).

It is worth mentioning that these analytical discussions were not the subject matter of judged cases but found their way into the academic commentaries to Justinian's Corpus Iuris Civilis. This is perhaps another marking difference between the common law and the civil law tradition, insofar as the former evolved by way of judge-made law dealing with real-world cases and circumstances while the latter relied on the doctrinal discussion of how to solve hypothetical issues on the grounds of the general principles of Justinian's code.[3]

The doctrine of legal personality was further developed in the 19th century by the German scholar Friederich Carl von Savigny, a leading representative of the 'Pandectists', a scholarly movement that purported to resume the scientific study of the *Pandects*, a compilation of passages by Roman legal writers arranged by subject matters, which was commissioned by the Emperor Justinian and published in 533 AD and retained statutory force in some areas of Mediaeval Europe throughout the Middle Ages. In his *System of the Modern Roman Law*[4] of 1840, Savigny conceived of two categories of legal persons: (i) *Korporationen*, or corporations, consisting of a plurality of individual members acting together as a single body, and (ii) *Stiftungen*, or foundations, that exist by reason of a purpose for which they were established.[5] This leads to another fundamental notion in relation to foundations, that of *Zweckvermögen*, which is often rendered in English as a 'special purpose fund and is also credited to a leading Pandectist scholar, Aloysius von Brinz, in the first volume of his *Handbook of Pandects*.[6] A 'special purpose fund', or in more usual civilian

2. For a detailed account of the historical development of foundations in the civil law tradition cf R Feenstra, 'Foundations in Continental Law since the 12th Century: The Legal Person Concept and Trust-like Devices' in R Helmholtz and E Zimmermann (eds), *Itinera Fiduciae, Trust and Treuhand in Historical Perspective* (Duncker & Humblot 1998).

3. Incidentally, this is also the reason why the 'Academia' plays such a prominent role in the legal tradition of continental Europe.

4. FC von Savigny, *System des heutigen Römischen Rechts* (Veit und Comp 1840).

5. In this connection it may be fascinating to note that the German word *Stift*, which clearly relates to the verb *stiften* (to found) is commonly used in Austria to describe a monastery.

6. A von Brinz, *Lehrbuch der Pandekten* (Deichert 1869).

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terms a 'dedicated patrimony', is still the core of the statutory definition of a foundation under Liechtenstein law:[7]

> A foundation . . . is a legally and economically independent special-purpose fund which is formed as a legal entity (juristic person) through the unilateral declaration of will of the founder. The founder allocates the specifically designated foundation assets, stipulates the purpose of the foundation, entirely non self-serving and specifically designated, and also stipulates the beneficiaries.

A similarity to trusts may be drawn in the definition above. Of course, trusts and foundations are quite different concepts: the former are relationships which 'do not exist' as persons, whereas the latter are 'legal persons' that can hold property in their own name and are capable of acting, suing, and being sued. However, the validity of a foundation, at least in its classic version resulting from continental European practice and German legal scholarship, appears to require the same 'ingredients' that are traditionally referred to as 'the three certainties' of a trust.[8] More precisely, a foundation comes into existence by means of the appointment of a 'subject matter' (a fund or 'patrimony', *Vermögen*) to an 'object' (or purpose, *Zweck*), which may amount to making provision for certain beneficiaries. The dedication of assets to such a purpose or purposes is the result of the founder's 'intention' or 'unilateral declaration of will'.

From *piae causae* to private foundations

The establishment of foundations as legal persons in Mediaeval Europe allowed wealthy gentlemen with fear of God to endow monasteries and other organizations pursuing religious or charitable purposes (*piae causae*) with land and properties, possibly in perpetuity. The same purpose would be achieved in England by transferring the relevant property to the abbot, or quite often to somebody else with no ecclesiastical affiliation, for them to hold it on trust (or rather, at that time, on 'use') for the relevant charitable objects.

A related practice was recorded in the Dutch United Provinces in post-reformation time in the form of foundations (*stichtinge*n) granting stipends to deserving students or food and shelter for needy people belonging to a specified religious confession.[9]

A further, natural evolution of the same legal arrangement was the appointment of assets for the benefit of the members of a specified family by the incorporation of a 'family foundation' (*Familienstiftung*). This practice was particularly common in Germany, where it can be said that during the Imperial era, family foundations played the same role in preserving and bequeathing the wealth created under the industrial revolution as trusts in Victorian Britain. The importance of foundations is witnessed by their regulation under the German civil code (*Bürgerliches Gesetzbuch*, BGB) which came into force as of 1 January 1900.[10] Some German family foundations have been in existence since the last decades of the 19th century and still control prominent manufacturing groups.[11]

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7. Liechtenstein, *Personen- und Gesellschaftsrecht* (PGR), art 552 s 1(1) (official English version).
8. *Knight v Knight* (1820) 3 Beav 148.
9. Some more details can be found in Feenstra (n 2). The *Godkameren* in Utrecht's Bruntenhof—which have preserved their original form until present days—are the result of a foundation (*stichting*) created by the Catholic lawyer Frederik Brunten in 1621 and they were originally intended to provide dwellings for destitute Catholics.
10. Germany, BGB, s 80ff.
11. An often-quoted example is the *Carl-Zeiss Stiftung*, which was created in 1889 and controls a glass, lens, and optical tool-manufacturing group that employs some 30,000 people.

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The first codification of a family foundation—or more generally a foundation pursuing purely private purposes—was the result of a visionary approach by Wilhelm Beck, a leading scholarly and political figure in post-World War I Liechtenstein, who conceived with his cousin Emil the 'Law on Persons and Companies' (*Personen- und Gesellschaftsrecht*, PGR) which came into force in 1926. The relevance of Liechtenstein's PGR to the offshore financial industry cannot be overstated. In fact, offshore finance was effectively 'invented' under this path-breaking piece of legislation, which was the strategic endeavour of a small, poor, land-locked country lacking natural resources which had lost its main geopolitical ally, the Austrian–Hungarian Empire, in the aftermath of the Great War. Wilhelm Beck's ingenuous idea was to set out an attractive legal environment for wealthy foreigners looking for a safe harbour for their wealth. The new legal tools made available by the PGR proved to be very helpful during the troubled years preceding World War II in German speaking Europe. By all means, foundations were the most successful legal arrangement under the PGR but they were not the only innovation: a new notion of legal person was created under the name of *Anstalt*, or 'establishment',[12] and a pioneering attempt to codify trusts in a civilian legal environment (*Treuhand*) alongside with an ingenuous notion of 'trust enterprise' or 'Trust Reg' (*Treuunternehmen*) with or without legal personality were equally contemplated under the PGR.[13]

Three models of private foundations

A list of civil law private foundation jurisdictions is provided under Appendix A to this article while common law jurisdictions are listed in Appendix B.

In the same way as trust jurisdictions may be grouped under different 'models' such as the original English model, an offshore or Caribbean model, and possibly a US model and a civil law one,[14] it is possible to identify at least three distinct models of private foundations. A 'classic' model was developed on the basis of the German tradition and was primarily codified under the Liechtenstein PGR. A separate model took shape as a result of the distinctive experience of the Dutch United Provinces. Finally, an individual model appears to result from the recent legislative experiments of many common law offshore jurisdictions.

A 'classic' model was developed on the basis of the German tradition and was primarily codified under the Liechtenstein PGR

The Liechtenstein private foundation (*Privatstiftung*) was built upon the Germanic tradition of family foundations with an increased degree of flexibility. For instance, a more prominent role was accorded to founders than under the traditional German doctrine of *Familienstiftungen* by way of statutory powers of revocation and amendment[15] as well as the opportunity for founders to be beneficiaries of the foundation.

The result was the 'classic' model of private foundations,[16] which was successfully followed in Panama under the law of 12 June 1995 regulating 'private interest foundations' (*fundaciones de interés privado*) as well as in Austria, where a Private Foundation Law (*Privatstiftungsgesetz*) was enacted in 1993. In turn, some of the subsequent developments in Austrian law were followed in the 'total revision' of Liechtenstein foundation law which came into force as of 1 April 2009.

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12. Liechtenstein, PGR (n 7), art 534ff.
13. ibid, art 897ff and *Treuunternehmensgesetz* 1928, now PG, art 932a.
14. An English, an 'international', and a 'civilian' model of trusts were recognized by M Lupoi, *Trusts* (Giuffrè 1997). Cf also D Hayton, 'Anglo-Trusts, Euro-Trusts and Caribbo-Trusts: Wither Trusts?' in D Hayton (ed), *Modern International Developments in Trust Law* (Kluwer 1999).
15. Liechtenstein, PGR (n 7), art 552 s 30.
16. The proposition that the Liechtenstein version of private foundations law, combined with some developments in Austrian and Panamanian law, is the 'classic' model of civil law private foundations is developed in some detail in P Panico, *Private Foundations. Law and Practice* (OUP 2014).

It is important to point out that the 'classic' model of private foundations was expressly intended to be influenced by trust law. Article 554 section 4 of the Liechtenstein PGR, in its original 1926 version, provided that the rules on 'trust enterprises' (*Treuunternehmen*) with legal personality should apply to private foundations insofar as the statutory rules on foundations or the constitutive documents of a particular foundation would not provide otherwise. This default reference to 'trust enterprises' was particularly relevant in respect of the foundation 'participants', ie the founder, foundation officers, and beneficiaries. For some reason the original Article 554 section 4 was repealed under the 'total revision' of 2009, which introduced a self-standing codification of foundation law featuring, among other things, a detailed description of various kinds of beneficial interests. This was a welcome clarification in many respects but it is submitted that a general reference to the principles of trust law—or more precisely the trust 'model' codified and enforced in Liechtenstein under Article 932a of the PGR—would have provided a helpful guidance for the fiduciary duties of foundation officers and the general functioning of a foundation. However the repeal of the 1926 version of Article 552 section 4 is consistent with the deliberate legislative choice of a number of common law jurisdictions to create a statutory entity, the foundation that performs a similar function to trusts but is not governed by the rules of equity.

In a simplistic way the 'classic' model of private foundation, which is the result of a centennial experience of family foundations, may be described as a trust-like device that allows the founder to retain a more prominent role than a trust settlor and at the same time restricts the rights and powers vesting in the beneficiaries in a more effective way than under ordinary principles of trust law. Some similarities may be recognized with the special trust alternative regime (STAR) of the Cayman Islands, where the beneficiaries are denied the ability to enforce the trust. This is perhaps one of the reasons why the Cayman Islands together with the BVI are the only relevant trust jurisdictions that have not yet enacted a foundation statute.

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On the other hand the 'Dutch model' of private foundation (*stichting*) places less emphasis on the founder's role or on beneficial interests. No statutory powers are reserved to the founder under the Dutch Civil Code and Article 285:3 of the Code expressly prohibits foundations that carry on a commercial activity from distributing their profits to the founder or to the beneficiaries. Private foundations that do not engage in business activities are not subject to such restrictions[17] but the Dutch model of foundation does not rely on a set of statutory rights and powers for founders and beneficiaries as in the Germanic experience.

The 'Dutch model' of private foundation (stichting) places less emphasis on the founder's role or on beneficial interests

Some degree of flexibility in relation to family wealth management arrangements may be achieved by a careful drafting of contractual obligations. Furthermore, the Dutch and Belgian practice of *Stichting administratiekantoor* (StAK) achieves a result that is functionally equivalent to an interest in possession trust. Under such an arrangement a foundation issues asset-backed notes or 'certificates' linked to some underlying assets (usually corporate shareholdings) so that the holders of such certificates are entitled to the income resulting from such underlying assets (eg dividends). The title to such assets vests in the foundation and the functional outcome may be described as if the foundation held them on trust for

17. More details on private foundations in the form of Dutch stichtingen are provided in Ineke Koele's article in this Journal.

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the certificate holders. The Dutch expression reads that the assets are held by the foundation *ten titel van beheer* (literally 'by way of administration'), which is often rendered in English as 'on trust' for the certificate holders.

The main defining element of the Dutch model foundation is its corporate nature as a legal person, as opposed to the Germanic and 'classic' reliance to the enforcement of the founder's 'unilateral declaration of will'. For this reason, Dutch foundations are often referred to as 'orphan corporate entities', ie ownerless incorporated legal persons, and as such they may be used in corporate arrangements such as securitization transactions, off-balance sheet collaterals, and top holding structures.

A third model of private foundations, which may be referred to as the 'common law model', has emerged out of the legislative experience of the past decade in a number of offshore financial centres, including several leading trust jurisdictions. A pioneering experiment to this effect was the St Kitts Foundations Act 2003, which was more or less extensively imitated or at least used as a first reference in nearly all the subsequent instances of private foundation legislation.[18]

A third model of private foundations, which may be referred to as the 'common law model', has emerged out of the legislative experience of the past decade in a number of offshore financial centres

The salient features of common law foundations may be traced to the 'classic' civil law model, in its Panamanian variant as well as in its Liechtenstein original form. A number of aspects of common law foundations, in turn, build upon the corresponding rules of local trust and company law. For instance, section 14(3) of the St Kitts Foundations Act 2003 provides that the foundation 'councillors' owe their duties to the foundation alone, which corresponds to section 74(3) of the St Kitts Companies Act 1996, providing that the directors of a company owe their fiduciary duties to the company and not to individual shareholders. At the same time section 20(9) of the foundation statute provides a limitation of liability for the 'guardian' of a foundation which is almost identical to section 25(11) of the St Kitts Trusts Act 1996 in relation to trust protectors.

Nevertheless, in spite of some direct references to trust law for some specific matters, the main purpose of common law private foundation legislation is to create a statutory arrangement that is 'not quite like a trust'. In particular, as far as beneficiaries are concerned, Article 25(1) of the Foundations (Jersey) Law 2009 expressly provides that:

> A beneficiary under a foundation
>
> a. has no interest in the foundation's assets
> b. is not owed by the foundation or by a person appointed under the regulations of the foundation a duty that is or is analogous to a fiduciary duty.

In other words, the 'quasi-proprietary' nature of beneficial interests, which has been the main obstacle to the reception of trusts in civil law jurisdictions, is removed in relation to private foundations. A beneficiary has at most a personal right to specific performance enforceable against the foundation but nothing resembling an 'equitable interest' in the foundation property. Furthermore a foundation beneficiary under the common law model is not owed fiduciary duties by the foundation or by its officers. Accordingly, the management board of a common law foundation—which is usually referred to in the statutes as the 'foundation council'—is placed outside the scope of the inherent, equitable jurisdiction of the court over all fiduciary offices, with the sole exception of some statutory provisions granting the court a power to enforce the proper management of a foundation.[19]

18. Part VI of the Liberian Associations Law, as amended in 2002, is in fact chronologically earlier than the St Kitts statute but it may be described as an attempt to recreate Austrian foundations in a common law context rather than to work out an original model.

19. For example, Anguilla, Foundations Act 2008, s 35.

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The available case law is minimal because of the very recent enactment of common law private foundation legislation. It remains to be seen to which extent the competent courts will rule out any references to trust law, and more generally to fiduciary law, in relation to private foundations to rely purely on statutory provisions in the same way as civil law judge would do.

A concluding word of caution: enforcement and recognition

The typical advertising material on private foundations, regardless of the jurisdiction concerned, tends to represent them as 'just the same as trusts but better'. For instance, private foundations are often represented as legal arrangements that can achieve the same purposes of trusts but at the same time allow the founder to enjoy a higher degree of 'flexibility' than the average trust settlor.

These are oversimplified representations and, as it is almost invariably the case, they should be considered carefully and acted upon only on the grounds of appropriate legal advice.

In truth, private foundations in many cases are 'just the same as trusts but different'. They are different from a structural—one would be tempted to say 'ontological'—point of view because they are legal persons and they are creatures of statute, not of equity. They are also different among themselves, as it was highlighted in the preceding, brief discussion of the 'three models'.

Private foundations in many cases are 'just the same as trusts but different'. They are different from a structural—one would be tempted to say 'ontological'—point of view because they are legal persons and they are creatures of statute, not of equity. They are also different among themselves, as it was highlighted in the preceding, brief discussion of the 'three models'

Of course, foundations are alien to the common law tradition in the same way as trusts or trust-like arrangements have only recently found their way into the civil codes of some continental jurisdictions. Nevertheless the presence of different models of private foundations may warrant unexpected results, such as the lack of recognition of certain types of foundations in certain civil law jurisdictions whose legal system do not contemplate a particular 'model'. For instance, in a reported decision of 2008, the Spanish authority in charge of the land register denied a Panamanian foundation the right to register Spanish properties in its name because Spain recognizes only charitable or public interest foundations.[20] Similarly, in a decision of 29 June 2009 the Regional Appeal Court (*Oberlandesgericht*) of Stuttgart refused to enforce the terms of a Liechtenstein foundation because of the extent of the powers retained by the founder.[21] This should not be entirely surprising: it is not inconceivable that a STAR trust governed by Cayman law or some form of US 'directed trust' may not be enforceable as a trust in England or in some other 'traditional' Commonwealth jurisdictions such as Australia or India.

A discussion of private foundations, in close comparison to trusts, and an appreciation of their intrinsic differences may encourage mutual understanding—and enjoyment—of different legal systems, which is one of the most extraordinary achievements of The International Academy of Estate and Trust Law.

Appendix A—private foundation legislation—civil law jurisdictions

- **Germany**, BGB (1 January 1900), section 80ff, reformed under the Modernization Law of 1 September 2002.
- **Switzerland**, Civil Code (1907), Article 80ff.
- **Liechtenstein**, *Personen- und Gesellschaftsrecht* (PGR), 26 January 1926, reformed 1 April 2009.
- **The Netherlands**, Dutch Civil Code (1992), Book 2, Part 6: *stichting*.

20. *Dirección General de los Registros y del Notariado, Resolución N. 2635 de 24 de enero de 2008.*
21. OGH Stuttgart 29/06/2009 5 U 40/09. In that case, the founder had entered into an agency agreement with the Liechtenstein corporate service provider to the effect that the foundation officers would carry out the founder's directions. Of course, the presence of such an arrangement was fatal to the foundation's case.

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- **Austria**, *Privatstiftungsgesetz* (PSG), September 1993 (partial reform 30 December 2010).
- **Panama**, *Ley de 12 de Junio de 1995 por la cual se regulan las Fundaciones de interés privado* (LFIP).
- **The Netherlands Antilles**, National Ordinance regarding Foundations (1998), since 2004 Book 2 of the Netherlands Antilles Civil Code: *stichting particulier fondsc* (SPF) in force in **Curaçao** and **St Maarten** since the dissolution of the Netherlands Antilles as of 10 October 2010 (reformed as of 1 January 2012).
- **Belgium**, *Loi du 27 juillet 1921 sur les associations sans but lucratif etc*, reformed as of 1 July 2003 under the *Loi 2002-05-02/51 sur les associations sans but lucratif et les fondations.*
- **Malta**, Second Schedule to Civil Code, Title III (2007).

Appendix B—private foundation legislation—common law jurisdictions

- **Liberia,** Associations Law, Part VI, Chapter 60 (as amended, 2002).
- **St Kitts,** Foundations Act 2003.
- **Bahamas**, Foundations Act 2004.
- **Antigua and Barbuda**, International Foundations Act 2007.
- **Anguilla,** Foundation Act 2008.
- Foundations (**Jersey**) Law 2009.
- **Seychelles,** Foundations Act 2009.
- **Vanuatu**, Foundation Act 2009.
- **Belize**, International Foundations Act 2010.
- **Labuan**, Foundations Act 2010.
- **Isle of Man**, Foundations Act 2011.
- **Mauritius**, Foundations Act 2012.
- **Cook Islands**, Foundations Act 2012.
- Foundations (**Guernsey**) Law 2012.
- **Barbados**, Foundation Act 2012.

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