

The Dutch private foundation: a robust but flexible tool in dynastic structuring

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Abstract

The Dutch private foundation is a robust and flexible tool for managing private wealth. Beneficiaries do not have any interest in the Dutch foundation, whilst the family may retain control over the autonomous board by various indirect means. If the assets originate from non-residents exclusively, the use of a Dutch foundation may be very tax efficient. Despite the existence of high gift and income tax rates, the use of a Dutch non-charitable, private foundation provides a flexible dynastic structure for combining charitable and private purposes in an unregulated and effectively tax free environment.

tax landscape on Dutch private foundations has dramatically changed.

A Dutch private foundation is now a very attractive device for dynastic structuring of international wealth, especially for non-resident families. Specifically, it may be used as an alternative to a charitable organization without the detailed administrative and tax oversight rules.

One can summarize the advantages of a Dutch private foundation as follows:

- a. Solid asset protection;
- b. With effective (indirect) control by the family;
- c. Without accountability towards beneficiaries;
- d. Very flexible;
- e. Effective exemption from Dutch tax when used by non-resident families.

Introduction

With the introduction of a new tax doctrine on 'segregated private capital' as of 2010, the legal and tax landscape on Dutch private foundations has dramatically changed

Before the year 2010, a Dutch private foundation was scarcely used for wealth management or estate planning purposes¹ due to adverse tax consequences in the Netherlands.

With the introduction of a new tax doctrine on 'segregated private capital' as of 2010, the legal and

Hereunder, I shall briefly elaborate on each of these aspects of the use of a Dutch foundation.

Solid asset protection: how to use a Dutch private foundation

Features of Dutch private foundations

Whilst many civil law jurisdictions and more recently, many Anglo Saxon jurisdictions have created a form of foundation law, in many instances—and especially

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1. Before 2010 however, the Foundation as a fiduciary vehicle known as 'Stichting Administratiekantoor' had been popular for a long time. Besides, a (predominantly) charitable foundation could be used for private purposes as well.

in the Anglo Saxon jurisdictions—the features of that body of foundation laws are more comparable to a trust if compared to a Dutch foundation.

The essential feature of a Dutch foundation is that it is a legally autonomous entity with rights and obligations but without any owner or persons with an interest therein. It is without members and its purpose, with the aid of funds intended for such purpose, is to realize the objects set out in its articles of association (Book 2 Article 285 (1) of the Dutch Civil Code). Accordingly, we may call the foundation a ‘purpose fund’.

The Dutch foundation law is extremely flexible and only contains a few compulsory rules. It therefore has been implemented in practice in various forms, which all have different tax qualifications.²

More specifically, Dutch civil law provides for the following features of a private foundation:

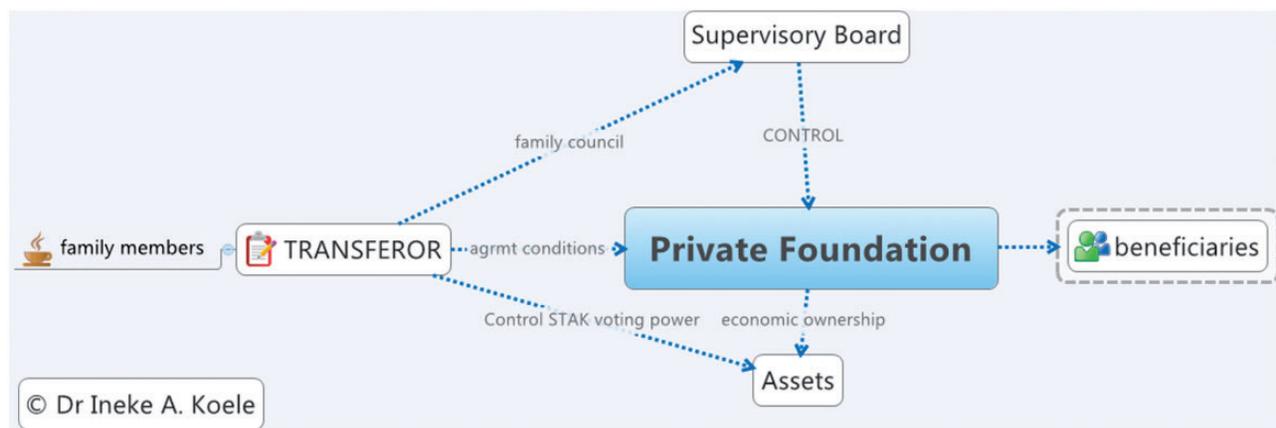
- I. A Dutch private foundation is fully independent from the founder; the founder has no special or reserved founder’s rights and accordingly, there are no ‘controlling rights’ whatsoever that can be assigned to third parties;
- II. The group of beneficiaries that would normally be mentioned in the purpose and activities of the foundation as set out in the articles of association, does not have any interest in the assets of a private foundation nor does there exist any right of information on the foundation assets or reporting towards this group. However, it is possible to assign specific rights or entitlements to designated beneficiaries in the governing documents of a private foundation;
- III. The board of the foundation has no fiduciary duties, but it is the representative of the full ownership of the assets similar to the board of a company. If a board member is acting in breach of his duties, he is liable towards the foundation (the foundation is required to act in the sole interest of its stated purpose, which in the case of a private foundation is to serve the interest of private purposes such as the pursuit of interests of family members). In case of mismanagement by the board of the foundation vis à vis the foundation, any interested person (including a beneficiary) is able to apply to the Court to dismiss the board member(s). Dutch law does however not know an enforcer that is able to enforce statutory objectives.
- IV. In practice, it is perfectly possible (and desirable, see III) for a family to retain control through a Family Council that acts as a Supervisory Board to the private foundation with strong controlling powers including the right to appoint and dismiss board members in general and the right to full information on the assets and activities as well as reporting of the private foundation. Family control may eventually be increased by a family representation in the board of directors.
- V. Apart from the articles of association, a foundation may have one or more regulations in place that regulate the activities of the foundation and its respective organs in greater detail; the contents of these regulations remain fully confidential.
- VI. Not the founder is important to a Dutch private foundation, but the person who transfers assets into the foundation (the transferor). The transferor enters into a separate (transfer or gift) agreement with the private foundation, which may contain various reserved powers, stipulations, and conditions as to the transfer to the foundation. Typically, exit scenarios are provided for in this agreement. Nonetheless, this does not deprive the board members of the foundation of their autonomy over the overall operations of the private foundation. Needless to say that the stipulations in the transfer agreement should not exceed a certain level that in effect would deprive the board of its autonomy.
- VII. Rather than transferring the full ownership to the private foundation, it is possible for the family to retain voting power over the

2. In Dutch practice, we distinguish at least 5 possible tax qualifications of a foundation depending on its practical application.

transferred assets, by using a combination of a private foundation and a fiduciary foundation (Stichting Administratiekantoor) that only has the voting power over the assets, the latter being managed by the family members. The interplay of various of these possibilities enhances to the governance of the structure.

Balancing the independence of board members and the control by the family

The balance between the independence of the board and the control by the family can be depicted as follows:



Structured with caution, a Dutch private foundation offers a very solid asset protection structure, which is apt for tailor-made family governance design. Family members that are defined in the statutory purpose of the private foundation as beneficiaries do not have any interest in the family foundation or its controlling body unless the governing documents would provide so specifically. The board of directors may be controlled by a supervisory family council and staffed by family members if desirable, and may be bound by the stipulations in a transfer agreement, whilst at the same time the board of directors has ultimate autonomy over the operations of the foundation.

With Dutch private foundations there is no inherent conflict of interest between settlor, trustee(s), protector and various beneficiaries that is inherent to an Anglo-Saxon irrevocable discretionary trust and 'look alike' foundations in offshore jurisdictions

With Dutch private foundations there is no inherent conflict of interest between settlor, trustee(s), protector and various beneficiaries that is inherent to an Anglo-Saxon irrevocable discretionary trust and 'look alike' foundations in offshore jurisdictions. This inherent conflict of interest makes dynastic structuring with discretionary trusts highly vulnerable to contentious litigation between the various interested

parties and consequently to stagnation at the level of operation of the trust. In my view, too many families are struggling with these effects of discretionary trusts which lead to excessive administration costs and an absolute lack of flexibility.

Combining dynastic structuring with altruistic purposes

A Dutch private foundation may hold shares in active business corporations, in passive investment funds, in art collections etc. and therefore may be suitable for dynastic structuring of important assets of families.

There is one legal issue relating to private foundations used for dynastic structuring that has raised some debate in the Dutch legal doctrine since 2010. One of the few compulsory provisions in the Dutch Civil Code prohibits the purpose of the foundation to include making payments to its founders, to persons who constitute its organs, or to others unless the payments have an altruistic or social character. This prohibitive condition is aimed at using the foundation as an alternative to the legal form of a commercial corporation. It is therefore arguable that this prohibition does not apply to family foundations that do not carry on an enterprise. In addition, the objective to pay distributions to family members (including founders or persons who are staffing the organs of a foundation) for appropriate purposes (study, maintenance, health treatments) qualifies as 'social'. It can therefore be said that the prohibition aims to avoid the objective of a foundation creating a 'selfish' foundation. Moreover, where the transferor wishes that the board of the foundation makes distributions to designated family members or for designated purposes, the transferor can stipulate these wishes in the contractual 'gift' agreement with the foundation.

To summarize, in practice this restriction is overcome by a combination of a tailor-made drafting of the constitutional documents and the gift agreement between the transferor and the foundation.

It is beyond doubt, that the private foundation is very suitable to combine dynastic family purposes and 'altruistic' purposes. Due to the special tax regime in the Netherlands (as referred to hereunder), it is irrelevant whether these altruistic purposes would qualify as charitable or not.

Effective exemption from Dutch tax on the set up of Dutch private foundations and their maintenance for non-resident families

The introduction of the new Segregated Private Capital regime (hereinafter 'APV'³) was inspired by

the wish to disregard foreign purpose funds like trusts, establishments (Anstalten), private foundations being used to 'shelter' funds and to impose tax upon the original owners or their beneficiaries with a view to the structured funds therein. In order, however, for such legislation to remain 'EU-proof', an abstract definition—independent of place of registration and legal form—was introduced: the APV. Consequently, private foundations registered in the Netherlands also qualify as an APV.

This APV doctrine has introduced the fiction that all income and assets of all 'Segregated Private Capital' will be attributed for tax reasons to the transferor alone or, after his or her passing away, to the respective heirs. Furthermore and as a consequence of the above, the tax laws treat all transfers to and from legal vehicles that qualify as Segregated Private Property as non-existent solely for Dutch tax purposes.

A private foundation is not qualifying as an APV to the extent that it has issued or designated specified entitlements to third parties against the transfer of property into the foundation. The APV regime therefore only applies to the extent that there is no interested party in relation to the assets and the income of the foundation that may be subject to tax on it. Also, charitable foundations and foundations that pursue social interests are excluded from the scope of the APV regime.

The consequence of qualifying as an APV is that the funds separated therein and the income and outgoing payments generated thereunder are, for the purposes of the Income Tax Act 2001 and Dutch gift and inheritance tax, fictitiously attributed to the transferor/donor

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3. Afgescheiden Privaat Vermogen (APV), introduced in art 2.14a Income Tax Act 2001.

donor. After the death of the contributor these are *fictionally* attributed to his or her heirs in proportion to the share of the total estate that each beneficiary is entitled to under applicable inheritance laws. There is only a liability to Dutch income tax if the contributor or his heirs is or are tax subject in the Netherlands in respect of the attributed funds or the income derived thereunder.

Unless the APV acquires Dutch situs assets that submit the transferor and his family to non-resident taxation in the Netherlands, there will be no Dutch income tax involved presumed that the transferor or his/her beneficiaries/ heirs would not take up residency in the Netherlands in the future.

Distributions by Dutch private foundations that qualify as APV will not be subjected to Dutch gift tax in these circumstances, since the beneficiaries are deemed to have acquired their benefit directly from the transferor (who is not subject to Dutch gift tax) or, after his/her decease, the respective heirs

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For the purposes of gift and inheritance tax liability the separation of funds within an APV is disregarded and accordingly, payments made from an APV

foundation are deemed to have been acquired from the person or persons to whom the funds of the APV are attributed for the purposes of levying income tax.

In the Act and in the parliamentary records the term 'separation of funds' has been given a very broad definition. It includes disposals and the separation within companies held by individuals is also deemed to be founded on the private interest served by the APV and accordingly the separation can be followed through to the underlying shareholders of a 'separated' company.

Although the Dutch tax legislation does not specifically refer to the transparency of the APV, this in fact may be said to be the purpose and aim of this legislation.

Summary

The Dutch private foundation has recently developed into a robust but very flexible tool to manage private wealth. Beneficiaries do not have any interest in the Dutch foundation, whilst the family may retain control over the autonomous board by various indirect means. If the assets are acknowledged to be originating from non-residents exclusively, the use of a Dutch foundation may be very tax efficient. Despite the existence of high tax gift and income tax rates, the use of a Dutch non-charitable, private foundation provides a flexible dynastic structure for combining charitable and private purposes in an unregulated and effective tax free atmosphere for non-Dutch families that refrain from taking up tax residence in the Netherlands.

Dr Ineke A. Koele is a Netherlands attorney and tax lawyer specializing in international tax, estate, foundation, trust, and charity matters. She has been partner of a large Dutch law firm for more than a decade before founding Koele Private Clients & Charity. She regularly speaks and publishes on selected topics in the above areas. E-mail: ineke@koelepc.com; Website: www.koelepc.com.