WARDYŃSKI & PARTNERS

# A family foundation

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KEY INFORMATION

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# The benefits from starting a family foundation

**The Family Foundations Act, which entered into force on 22 May 2023, introduces the family foundation into Polish law as a new legal entity designed for collecting property and managing assets in accordance with the founder's will and paying benefits to beneficiaries. Therefore, the objectives of a family foundation are different from those of existing foundations, which are non-governmental organisations operating for public benefit and not for profit.**

Below we present the main advantages of a family foundation, which show that this legal form can serve diverse purposes.

The introduction of a new legal entity to manage private assets for a specific set of beneficiaries arises from the need to safeguard the founder's assets for future generations in a planned manner, consistent with the founder's intent. Until now, a testator in Poland could make a will and transfer assets to his or her heirs, but had limited options for deciding how the assets would be administered after death (e.g. a testamentary instruction). This problem is particularly relevant in the case of family businesses whose owners do not have successors prepared to continue their activity. In such case, the easiest thing to do would be to simply sell the company, but this too is not always an optimal solution from the point of view of the elders, who may treat the family business as their life's work.

Therefore, the idea of a family foundation is related to the need for succession planning, but this are not the only benefit that this legal form provides.

## Managing family assets and paying benefits to beneficiaries

A family foundation is an entity with legal personality authorised to manage the assets contributed by the founder. A founder can establish a family foundation in either a founding deed or a will, which requires the form of a notarial deed. The founder's duty is to contribute assets to the foundation to cover the founding fund with a value specified in the statute, but not less than PLN 100,000. A family foundation cannot return to the founder any or all of the property contributed to cover the initial fund unless otherwise provided by law.

The founder can have a significant influence over the activity of the foundation and how it manages its assets, both through the relevant provisions of its statute, which indicates, among other things, the purpose of the family foundation, its beneficiaries or the method of determining them, and by defining their powers or guidelines for investing the family foundation's assets. At the same time, the founder may also address comments, opinions or recommendations to the bodies of the foundation regarding its activity.

The foundation's beneficiaries, who may be members of the founder's family as well as the founder himself, but also persons unrelated to them or public-interest organisations, are entitled to receive the benefits specified in the statute. These benefits can take various forms—assets, including cash, tangible or intangible property, transferred to the beneficiaries or given to them for their use. If the beneficiaries are natural persons, the foundation may also cover their living expenses or education.

A beneficiary to whom the family foundation has provided a benefit in violation of the law or the statute is obliged to return it. The management board members responsible for making an undue benefit are liable to repay it jointly and severally with the beneficiary.

A family foundation can be an appropriate solution for preserving the family assets and ensuring their protection from imprudent decisions of the founder's potential successors, while not depriving them of the benefits associated with those assets. Through appropriate provisions in the statute, the founder can have a long-term influence on how the foundation's assets are managed and disposed of, for the purpose of preserving them for future generations, avoiding disadvantageous distributions often leading to loss of control over the assets. A family foundation can be used to secure the assets of people who cannot, for various reasons, manage them independently, e.g. wealthy people with no heirs who are incapacitated and require care. A family foundation can also provide lifelong care and maintenance for persons who are elderly, disabled or otherwise dependent and cannot rely on family support.

## A family foundation as an investment vehicle

A family foundation can acquire equity rights and make capital investments in other entities, taking advantage of tax preferences, as we discuss in more detail in the article "Taxes and the family foundation." Under the law, a family foundation is entitled to join and participate in companies, partnerships, investment funds, cooperatives and other such entities, based in Poland or abroad, as well as to acquire and dispose of securities, derivatives and rights of a similar nature.

A family foundation can also help secure proper exercise of corporate rights, among other things by ensuring unanimity in the management of shares in companies. Otherwise, as happens after the death of the testator, the decedent's stake of shares in a company may be divided among the heirs, who may have differing views when exercising corporate rights. In extreme situations, this can lead to a decision-making impasse. Another threat is the transfer of shares by some heirs seeking to cash in on their inheritance, thus introducing outsiders into what was a family company. In contrast, the transfer of shares to a family foundation results in a limited risk of capital dissipation, as they are subject to management by the foundation, and the beneficiaries' rights and duties are non-transferable (except for their claims to due benefits).

## Asset protection—the foundation's liability for the founder's obligations

The assets of a family foundation are separate from those of the founder. The founder is not liable for the family foundation's obligations, due to its separate legal personality. In this respect, the founder's legal situation is similar to that of a shareholder of a limited-liability company.

On the other hand, a family foundation will be jointly and severally liable for the founder's obligations arising prior to its establishment, limited to the value of the property contributed by the founder at the time of contribution, at the prices at the time the creditor is satisfied. This means that once a foundation is established, by operation of law, it will accede to the founder's obligations, for example under contracts. Exclusion or limitation of the family foundation's liability for such obligations is possible exclusively with the creditor's consent. The family foundation can also step into the shoes of the obligated founder, if the creditor releases the founder from the debt.

The family foundation is not liable for the founder's obligations arising after its establishment, with one exception—the founder's maintenance obligations (alimenty). In the case of maintenance obligations, arising either before or after its establishment, the foundation is jointly and severally liable with the founder, regardless of the amount of the obligation. Similar to other obligations, the family foundation is liable up to the value of the contributed property. This means that if enforcement against the founder's assets is ineffective, it is possible to pursue maintenance claims against the family foundation. Also, the act allows an action to be brought against a foundation before enforcement against the founder's assets proves ineffective.

The asset protection function that a family foundation can perform can also be understood in a broader context, by providing long-term planning for the management of family assets, preventing the disruptions accompanying each generational change. The division of assets between the heirs may lead to fragmentation, imprudent disposition of particular assets, or differing visions of heirs as to the purpose of family assets. The establishment of a family foundation allows for consistent, long-term management of the entirety of the assets contributed to the foundation, while ensuring that benefits are distributed systematically to its beneficiaries.

## Family foundation and succession planning

Although a family foundation is widely viewed as a succession instrument (broadly understood as a vehicle giving flexibility in the disposition and management of the founder's assets), its establishment and operation does not actually change the situation of the founder and his or her relatives from the perspective of succession law. However, in certain circumstances, the establishment of a family foundation may prove particularly helpful in adequately providing for minors.

When establishing succession plans, a significant risk is usually associated with potential claims for a forced share, which occurs if the testator omits persons entitled to a forced share in testamentary instructions or donations made during the testator's lifetime (inter vivos gifts). This follows from the general rules for determining the forced share, under which, to calculate the forced share, it is first necessary to determine the basis (substratum) for the forced share, i.e. the sum of the absolute value of the inheritance, gifts and legacies made by the testator. Thus the value of gratuitous dispositions made by the testator during his or her lifetime should also be added to the estate left by the testator. In the case of developed family companies, the value of forced-share claims is sometimes so significant that it can even lead to a forced sale of the company to collect funds to satisfy such claims by persons who received the family business from the testator.

The transfer of the company to a family foundation does not fundamentally change this situation. Such gratuitous dispositions are added to the substratum of the forced share on the same basis as any other inter vivos gifts by the testator. In turn, the family foundation itself is liable for forced-share claims in the same manner as other gift recipients are liable for these claims. In this regard, the new provisions of the Civil Code require that a family foundation be treated like any other type of entity not being an heir or entitled

to a forced share and receiving a gift from the testator. Thus, the founding fund transferred to the family foundation by the testator is always added to the substratum of the forced share, unless the contribution occurred more than ten years before the testator's death and the family foundation was not appointed to the testator's estate.

As for benefits received by the beneficiaries of the family foundation who are also entitled to a forced share from the founder, from the perspective of inheritance law the parliament instructs that they should be treated the same as any other benefits received from the testator by those entitled to a forced share. Therefore, in such cases, the beneficiaries must count the value of the benefits received from the family foundation against the forced share due to them.

Due to the ten-year restriction on adding the founding fund to the substratum of the forced share, it might seem that establishing a family foundation and naming as beneficiaries only some of those entitled to a forced share from the founder's estate might be a way to offset the risk related to a forced share. Unlike in the case of a transfer of assets directly to selected beneficiaries entitled to a forced share, in such an arrangement the designated beneficiaries would receive the benefits from the foundation, while if the founder survived ten years after the transfer of the founding fund, the value of the fund would not be added to the substratum of the forced share. Therefore, the condition is the lapse of a ten-year period since the initial fund was contributed to the foundation. Given the highly precarious nature of this condition and the analogous nature of the rules for determining the forced share with regards to the founding fund of the family foundation regarding the testator's other donations, it is impossible to conclude that the family foundation introduces instruments for limiting claims for a forced share of the founder's estate. Therefore, in this respect, the rules for determining the forced share based on the founding fund of a family foundation have only been adapted to the existing rules.

Continuing with succession law, it is worth noting the advantage of a family foundation when planning for distribution of benefits to a minor. This refers to situations in which the testator would like to transfer some assets to a minor, but at the same time does not have confidence in the minor's legal guardians, who, until the beneficiary reaches the age of majority, would manage such assets under the supervision of the guardianship court. Moreover, if the transferred asset were a company or part of a company, any decision regarding its operation would require prior authorisation from the guardianship court, which in turn would threaten to paralyse the company's ongoing

business operations. Usually, such dilemmas occur in the case of dispositions made by grandparents for the benefit of grandchildren, but with the desire to omit one of the grandchildren's parents (former or current spouse or partner of the testator's own child). Under such conditions, it would seem helpful to contribute the company to a family foundation, while at the same time appointing the minor as a beneficiary of the foundation. This would avoid the influence of the minor's legal guardians in the day-to-day management of the company and would make it unnecessary to obtain the court's permission for the company to carry out specific activities, while ensuring that adequate provision is made for the current needs of the minor.

## Summary

The above analysis shows that a family foundation can be used not only for succession planning, but also for investment purposes and as a mechanism ensuring long-term management of family assets, protecting them from fragmentation. Such a broad spectrum of application makes the family foundation a particularly attractive formula for owners of companies or wealthy individuals struggling with the dilemma of how to divide assets among children so that, on one hand, no one is harmed and, on the other hand, divisions do not arise that could disrupt the company's activity or the unity of family assets.

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# Running a business through a family foundation

**It is now possible to carry out intergenerational succession in Polish companies through the vehicle of a family foundation. This new legal entity is designed to meet the needs of business owners, who until now were condemned to relatively limited choices under general provisions, or could choose foreign jurisdictions to set up a family foundation (e.g. in Austria, Liechtenstein, Malta, or the Netherlands).**

In drafting the Family Foundations Act of 26 January 2023, the parliament created an institution distinct from other legal entities in Poland. In addition to its many advantages, business owners considering using a family foundation should also learn about its limitations, so that the process of intergenerational succession proceeds as intended.

In this article we discuss the limitations of a family foundation for running a business, as the act establishes a fixed catalogue of the types of business activities that a family foundation can conduct.

## Permitted activities

Under Art. 5(1) of the act, the business activities of a foundation are exclusively limited to:

1. Disposal of property, unless the property was acquired solely for the purpose of further disposal
2. Lease, rental or making property available for use on any other basis
3. Joining and participating in commercial companies (or partnerships), investment funds, cooperatives and entities of a similar nature, with their registered office in Poland or abroad, as well as participation in other companies, funds, cooperatives and entities
4. Purchase and sale of securities, derivatives and rights of a similar nature
5. Providing loans to:
   a. Companies in which the family foundation holds shares
   b. Partnerships in which the family foundation participates as a partner
   c. Beneficiaries
6. Trading in foreign means of payment belonging to the family foundation for the purpose of making payments related to the activities of the family foundation

7 Production of plant and animal products processed other than industrially, with the exception of processed plant and animal products obtained in the course of special units of agricultural production activities and products subject to excise tax, provided that the amount of plant or animal products derived from own culture, breeding or rearing, used in the production of a given product, constitutes at least 50% of the product
8 Forest management

Agricultural and forest activities (points 7–8) may be performed by a family foundation exclusively in relation to an agricultural enterprise.

## Conducting activities outside the permitted catalogue

As may be seen, the foregoing catalogue allows for conducting holding activity, leasing of foundation property, investment, lending, and conducting an agricultural enterprise. This demonstrates that, in principle, the parliament assumed that (except for running an agricultural enterprise) a family foundation should carry out exclusively passive activity. Since the catalogue of activities specified in Art. 5 of the Family Foundations Act is exhaustive, conducting other activities by a family foundation would violate the act.

However, the consequences of a family foundation conducting business beyond the established scope are unclear. In this regard, the law refers only to the tax consequences of carrying out such activities, e.g. imposing an increased (25%) corporate income tax rate for carrying them out (CIT Act Art. 24r(1)). We write more extensively about the taxation rules for such activity in the article "Taxes and the family foundation."

Therefore, it seems reasonable to conclude that violation of the ban on conducting other activity does not invalidate the transactions made against the ban, but only results in negative tax consequences. If such transactions were regarded as invalid, they would not be subject to taxation. Therefore, the sanction for violating the restriction on the subject of the family foundation's activity should be sought under public law, not civil law.

It can also be assumed that violation of the business ban does not always provide grounds for judicial oversight of the foundation's activity under Art. 88 and 89 of the Family Foundations Act. Indeed, the basis for such review by the registry court would be management of the family foundation in a manner obviously contrary to its purpose or the interests of its beneficiaries. Thus, if conducting business beyond the scope of Art. 5 does not violate the

purpose of the family foundation or the beneficiaries' interests, the registry court has no grounds to impose a fine or, in extreme cases, dissolve the family foundation.

These doubts call into question the purpose of Art. 5 of the act. From the beginning, the provisions on the ability of a family foundation to conduct business activity were the subject of extensive discussion. As a result, during the legislative process, the total ban on conducting business activity originally proposed was reduced to its current form. From the course of this discussion, it can be concluded that the ban or restriction of a family foundation's ability to conduct business is aimed at protecting the assets contributed to the family foundation. But if there are no civil-law consequences for violating the ban on conducting certain business activity, Art. 5 does not appear to guarantee the level of protection it was intended to provide.

Sceptics objecting to the ban on broader business activity argue that when receiving assets from the founder (and other persons), a family foundation should be able to multiply them. Only this way can the assets accumulated by older generations serve future generations for as long as possible. With the model adopted in the act, this assumption still seems feasible, as ways to operate businesses within family foundations do exist.

## Contributing a company to a foundation

Primarily, a family foundation can be a shareholder in companies (or a partner in partnerships). Thus the conduct of business by such companies will not be subject to the ban or the negative tax consequences from violating the ban. So if the founder is an owner of a company or partnership, he or she may contribute that interest to the family foundation (the shares in a company or the totality of rights and obligations of a partner in a partnership).

The contribution of such rights to a family foundation should be made with due regard to the law and internal corporate requirements for disposing of such assets. When planning for intergenerational succession through establishment of a family foundation after the death of the founder, it is necessary to appropriately review the articles of association or partnership agreements to avoid any internal restrictions of a corporate nature.

However, if an individual business operator (e.g. sole proprietor) would like to establish a family foundation, as the founder he or she can contribute the business in kind to an existing company or partnership, or convert the business

into a limited-liability company. Then the resulting shares or totality of rights and obligations in the partnership can be contributed to the family foundation.

The choice of one of these options for reorganising a business will depend on a number of factors, particularly the time available, the complexity of the business structure, the regulatory environment, the contracts to which the business is a party, and tax issues.

But it is a risky idea to contribute the business itself to a family foundation, and then contribute it in kind to a company or partnership owned by the family foundation. In such a scenario, it is necessary to transfer the same business twice to the target entity, increasing the exposure to risks associated with in-kind contribution of the business.

Accordingly, individual business operators who would like to establish a family foundation in the event of their death should first ensure that their business operates in the form of a commercial company or partnership. This will enable the family foundation to become a shareholder or partner in the entity running the business without too many problems after the founder's death.

## Summary

It is clear that the family foundation was not created as a vehicle for its founder's direct business operations. However, it is possible to continue the operations of the business under the umbrella of a family foundation. While there is a ban on direct conduct of certain business activities under the Family Foundations Act, the ban is not airtight and family foundations may attempt to exploit that leeway. However, the management boards of family foundations deciding to conduct business in violation of the ban must take care that such activities do not violate the purpose of the foundation or the interests of the beneficiaries. That could risk a fine or even lead to dissolution of the family foundation.

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# Taxes and the family foundation

**Along with the provisions allowing for establishment of a family foundation, entirely new tax provisions were introduced, with attractive rules for taxation of asset transfers and foundation activities, but also a slightly too varied patchwork of tax rates.**

This article discusses the taxation of events accompanying the daily operation of a family foundation in Poland.

## Transferring property to a family foundation

Transferring property to a family foundation can take two forms:

- Contribution of initial capital to the family foundation by the founder
- Secondary transfers of property rights by the founder or other persons.

Regardless of which of these two avenues is used to enrich a family foundation, such an event does not involve the obligation for the foundation to pay corporate income tax.

## Ongoing activity of the family foundation

A family foundation enjoys a subjective exemption from corporate income taxation. In practice, the exemption applies to income that does not come from the business activity of a family foundation, or comes from such activity but has its source in:

- Disposal of property (but not commercial activity)
- Lease, rental or other provision of property for use
- Participation in and joining commercial companies (or partnerships), investment funds, cooperatives and entities of a similar nature
- Purchase and sale of securities, derivatives and rights of a similar nature
- Provision of loans to beneficiaries, companies in which the family foundation holds shares, and partnerships in which it participates as a partner
- Trading in foreign means of payment belonging to the family foundation for the purpose of making payments related to the activity of the family foundation
- Production of plant and animal products (with restrictions)
- Forest management.

Taxation of the ongoing activities of a foundation only arises in three situations.

First, the income from rental, lease or other agreement of a similar nature, the subject of which is an enterprise, an organised part of an enterprise, or assets dedicated to carrying out the activities of a beneficiary, the founder or an entity related to them or the family foundation (the threshold of ties is set at a reduced level of 5%) does not benefit from the tax exemption. The income tax rate that applies is 19%.

Second, the tax exemption does not apply to the tax on income from buildings. This means that a family foundation pays income tax if it owns buildings in Poland which have been delivered for use under an agreement and the initial value of the buildings is higher than PLN 10 million. The corporate income tax is 0.035% of their value for each month.

Third, it is taxable for a family foundation to conduct business activity not included in the foregoing statutory catalogue. The tax is 25% of the tax base, i.e. the family foundation's income from taxable activity minus deductible expenses, but only expenses proportionately attributable to the taxable activity of the family foundation. In this case, the family foundation cannot take advantage of the following exemptions and deductions:

- Subjective exemption from income tax
- Deduction of donations from the tax base
- R&D tax credit
- Prototype tax relief
- Pro-growth tax relief
- Consolidation relief
- Tax relief for execution of an initial public offering
- Tax relief for sponsors of sports, culture and education
- Discount on payment terminals
- Bad-debt relief.

The first of these taxes (on lease of an enterprise etc) has a different impact than the others on the overall taxation level of the family foundation. At the moment of making by a family foundation of transfers subject to corporate income tax, the family foundation should be able to reduce the tax on these transfers by the amount of tax already paid for the period not covered by the statute of limitations.

In the case of the other two taxes (on buildings and extraneous business), such a deduction is not possible, and the tax paid only reduces the value of

the transfers made, which may significantly increase the effective tax level of the family foundation.

## Distribution of benefits and property from the foundation

### Taxation of foundations

The foundation pays a flat-rate corporate income tax in the amount of 15% of the value transferred or made available directly or indirectly at disposal of:

- Benefits, i.e. in the case of transferring assets by the foundation to a beneficiary or giving the beneficiary use of assets in accordance with the statute and the list of beneficiaries
- Property in connection with dissolution of the family foundation
- Benefits treated as hidden profits.

While the first two categories speak for themselves, the third requires a broader commentary. Hidden profits include:

- Interest and other remuneration on a loan made to a family foundation by a beneficiary, founder, or an entity related to a beneficiary, founder or family foundation (the threshold for the existence of ties was lowered to 5%)
- Gifts or other gratuitous or partially gratuitous benefits, other than those expressly referred to in the regulations governing family foundations, provided directly or indirectly to a beneficiary, founder, entity related to the beneficiary, founder or the family foundation (the threshold for the existence of ties was lowered to 5%)
- Benefits to the beneficiary, founder, or an entity related to the beneficiary, founder or family foundation for consulting services, accounting services, market research, legal services, advertising services, management and control, data processing, employee recruitment and staffing services, guarantees and warranties and benefits of a similar nature, and all kinds of fees and charges for the use of, or the right to use, copyright or related property rights, licences, industrial property rights and knowhow (the threshold for the existence of ties was lowered to 5%)
- Profits from non-arm's-length transactions made between the family foundation and a beneficiary, founder, or an entity related to a beneficiary, founder or the family foundation
- Loans granted by the family foundation to a beneficiary, for the portion that was repayable in a given tax year and was not repaid by the deadline for filing the annual tax return

- Loans granted by the family foundation to a beneficiary for a period of 10 years or more, or for a period of less than 10 years if the final term of the agreement was at least 10 years.

The tax base is the value of the benefit or property flowing out of the foundation, with one exception. In the event of dissolution of a family foundation, the value of the property to be distributed is reduced by the tax value of the property contributed by the founder(s) (the tax-deductible costs that would have been incurred if the asset had been disposed of for payment before it was contributed to the family foundation), not exceeding its market value.

### Taxation of beneficiaries and others

The benefit to natural persons and the release of property to them in connection with the dissolution of a family foundation are subject to personal income tax and constitute income from "other sources." The regulations provide important preferences for the founder and his/her closest relatives:

- The founder and persons covered by the exemption from inheritance and gift tax (the "zero" group), i.e. spouse, descendants, ascendants, stepchildren, siblings, stepfather or stepmother (these persons must be beneficiaries to benefit from the exemption in the case of benefits paid), is exempt from income tax
- 10% tax is paid by persons who are classified in the Inheritance and Gift Tax Act in tax group 1 or 2 in relation to the founder, i.e. sons-in-law, daughters-in-law and parents in-law, descendants of siblings, parents' siblings, descendants and spouses of stepchildren, spouses of siblings and siblings of spouses, spouses of spouses' siblings, and other descendants' spouses
- 15% tax is paid by others.

In the context of the foregoing benefits, the origin of contributions to the family foundation is of strategic importance. When the founders (understood as the founder together with his/her spouse, descendants, ascendants or siblings) or the foundation itself (understood as any others) contribute property to a family foundation, an inventory of this property is made, together with an indication of the proportion of contributions. This proportion determines the extent to which the aforementioned tax exemption and preferential 10% tax rate can be applied.

Additionally, the foregoing provisions should be applied taking into account any tax treaties that may be applicable, subject to presentation of a certificate of tax residence, which can often result in non-taxation of foreign beneficiaries in Poland.

Taxpayers are not required to pay social insurance, health insurance contributions or the solidarity levy.

The Personal Income Tax Act does not contain a reference to benefits qualifying as hidden profits, which means that such donations may be subject to income tax or inheritance and gift tax under the general rules.

Inheritance and gift taxation of beneficiaries

The receipt of a benefit from a family foundation and the receipt of property in connection with dissolution of a family foundation are not subject to inheritance and gift tax. Therefore, it can be inferred that this tax could be applied to some of the gains from hidden profits.

**Opodatkowanie beneficjentów podatkiem od spadków i darowizn**

Otrzymanie świadczenia z fundacji rodzinnej oraz otrzymanie mienia w związku z rozwiązaniem fundacji rodzinnej nie podlegają podatkowi od spadków i darowizn. Można zatem wnioskować, że podatek ten mógłby znaleźć zastosowanie wobec niektórych spośród przysporzeń z tytułu ukrytych zysków.

## VAT

The explanatory memorandum to the draft Family Foundations Act indicates that the VAT consequences in terms of transactions and events carried out in connection with the establishment and operation of a family foundation are determined under the specific factual situations based on existing VAT provisions, taking into account the regulations arising from the VAT Directive and other EU provisions. The Family Foundations Act did not make any changes in this regard.

## Liability of the foundation for tax obligations of the founder, and liability of third parties for the tax obligations of the foundation

A family foundation is jointly and severally liable with the founder for his/her tax and social insurance arrears incurred before establishment of the foundation. The scope of liability is limited to the value of the assets contributed by the founder to the family foundation.

Members of the governing bodies of the family foundation are jointly and severally liable for arrears with all their assets, and the provisions governing the liability of members of the management board of companies apply accordingly.

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# The role of the founder and bodies of a family foundation

**In previous articles, we have outlined the advantages of establishing a family foundation, the scope of business activities permitted for foundations, and tax issues. Now we turn to the rights and obligations of persons involved in the operation of a family foundation. The foundation operates through its bodies (management board, supervisory board, and assembly of beneficiaries), but it cannot be established and function without the founder and beneficiaries. The Family Foundations Act regulates the tasks and powers of all of these entities, giving the founder relatively wide latitude to set the rules for the foundation's bodies in the statute. This allows these policies to be tailored flexibly to suit the foundation's operations and purposes.**

## Founder

Every family foundation must have at least one founder. Only a natural person with full legal capacity can become a founder. Therefore, legal entities (e.g. companies or cooperatives) cannot become founders, but, for example, there is no obstacle to foreigners being founders. Also, the act does not preclude a foundation from having several founders, with theoretically unrelated individuals also able to become founders, creating a single family foundation for several individuals or families.

The source of each family foundation is the founder. Therefore, the act assumes a special role for this person. First of all, the founder is obliged to establish the foundation in either the foundation deed or the founder's will, in either case in the form of a notarial deed. In turn, the founder should:

- Establish the statute of the family foundation (also in the form of a notarial deed), including in particular its specific purposes
- Draw up an inventory of property to cover the founding fund
- Establish the bodies of the family foundation (unless the statute provides otherwise, the founder retains the right to appoint and remove members of the management board and supervisory board until his or her death)
- Contribute property to a family foundation to cover the founding fund with a value specified in the statute, but not less than PLN 100,000.

Additionally, the act provides for the founder's power to challenge resolutions of the family foundation's bodies. The basis for challenging a resolution may be its inconsistency with the law or with the statute or purpose of the foundation.

Otherwise, the founder's rights and obligations are determined by the statute of the foundation, and in this regard it should be assumed that the provisions of the statute are limited only by law. Thus, the founder can decide to what extent and in what capacity he or she wants to participate in the activities of the foundation.

The founder's rights and obligations are strictly personal in nature, making them non-transferable. However, in the statute the founder may delegate the exercise of his or her powers to another person. It seems that the entrustment of powers remains effective only during the founder's lifetime, as in the event of his or her death the founder's powers are assumed by the competent bodies of the foundation (e.g. the power to appoint and dismiss members of the foundation bodies).

A founder can combine different roles in the foundation's bodies. For example, he or she may serve as the sole member of the foundation's management board. Additionally, the act provides that the founder can also be a beneficiary of the foundation. The possibility of combining the management and control competencies in the hands of the founder, and the ability to benefit from the foundation's assets, strengthens the attractiveness of establishing a family foundation during the founder's lifetime.

## Management board

The management board is a mandatory body of a family foundation. Its main task is to manage the affairs of the foundation, represent it, and pursue the purposes indicated in the statute. The management board may have one or more members, and may include the founder, beneficiaries, and also persons unrelated to the founder who will ensure proper management of the foundation's assets, provided they have full legal capacity. It seems that it is precisely due to the possibility of appointing the founder or beneficiaries to the management board that the parliament expressly allowed this function to be performed without remuneration as well.

In the case of a multi-member management board, the family foundation is represented by two members acting jointly, although the method of representation may be specified otherwise in the statute. In principle, the term of office

of a management board member is three years, but the act also leaves this to the discretion of the founder, and this issue may be regulated differently in the statute. A member of the management board of a family foundation can be removed at any time. Also, in the statute the founder may specify who is authorised to appoint and remove the management board, for example the founder, the supervisory board (if established) or the assembly of beneficiaries.

The drafters of the act intended the management board to serve as an intermediary between the family foundation and its beneficiaries. Like other legal entities, a family foundation operates through its bodies. Therefore, the actions of the management board are the actions of the family foundation. In particular, the duties of this body include ensuring the foundation's financial liquidity and solvency, as well as distributing benefits to the beneficiaries entitled to receive them. The management board is also responsible for maintaining a current inventory of property managed by the family foundation. The beneficiaries and the founder are entitled to address comments, opinions or recommendations to the management board.

The management board has the duty to create, maintain and update the list of beneficiaries. Because this involves processing the beneficiaries' personal data, the management board is obliged to maintain the confidentiality, integrity, completeness and availability of the personal data.

At the same time, the management board of a family foundation will usually have extensive knowledge of the foundation's activities, resulting not only from access to the documents of the foundation itself but also from the possibility of receiving information intended for the foundation as a partner or shareholder of companies in which the family foundation has an interest. As a result, every member of the management board is obliged to keep confidential the information obtained in relation with his or her function, even after the member's term of office ends. Due to the nature of the family foundation as an instrument to preserve the founder's assets, the concept of family foundation secrecy is broader than that of business secrecy, and includes, among other things, information regarding the investment policy, organisational or other information of economic value, as well as information regarding beneficiaries.

The members of the foundation's management board have an obligation to act loyally towards the family foundation and to exercise due care. A member of the management board of a family foundation may be liable to the foundation for damage caused by an act or omission contrary to the law or the statute, unless he or she is not at fault. To release a member of the management board from liability, it must be demonstrated, in particular, that he or she

acted within the bounds of reasonable economic risk, a concept that should be understood in line with the business judgment rule for members of the management board of companies. This issue is discussed more extensively in our article "The business judgment rule."

In addition to liability for the foundation's obligations borne by a member of the management board under generally applicable provisions (e.g. the Bankruptcy Law or the Tax Ordinance), members will also be obliged to reimburse the foundation for benefits they have provided to beneficiaries in violation of the law or the statute, jointly and severally with the beneficiary who received the undue benefit.

## Supervisory board

The supervisory board is an optional body of a family foundation. However, when the number of foundation beneficiaries exceeds 25 persons, the foundation must appoint a supervisory board. Until then, there will be a supervisory board only if expressly provided for in the statute of the foundation.

Interestingly, the supervisory board may consist of as few as one member. Otherwise, it seems that the structure and purpose of the supervisory board can be compared to supervisory boards in companies. In short:

- A member of the supervisory board may be a natural person with full legal capacity who has not been convicted of any crimes specified in the Family Foundations Act
- The members of the management board are appointed for maximum 5-year terms by the founder, or after his or her death by the assembly of beneficiaries
- The same person cannot serve on both the management board and the supervisory board
- The supervisory board oversees the activities of the management board in terms of compliance with the law and the statute, and may, in particular, request any information, documents, reports and explanations from the management board
- The supervisory board represents the family foundation in contracts or disputes with a member of the management board
- The members of the supervisory board are bound by the principle of due care in the performance of their duties, the duty of loyalty to the foundation, and the duty to preserve the secrets of the foundation (also after their term ends).

However, due to recent amendments to the Commercial Companies Code, the powers of the supervisory board of a family foundation are not as broad as in the case of companies. This is important, as the scope of liability of a member of the supervisory board of a family foundation for damage caused to the foundation is the same as the scope of liability of members of the supervisory boards of companies. This raises the question of whether the members of the supervisory board of a family foundations will be able to properly perform their duties, since they are not expressly granted, for example, the right to seek the assistance of advisors of their choice, as members of the supervisory boards of companies can do (under certain conditions).

## Beneficiaries and the assembly of beneficiaries

By definition, a family foundation should act in the interests of its beneficiaries and distribute specific benefits to them. At the same time, the foundation's beneficiaries may include the founder, the founder's family members, as well as unrelated persons and public benefit organisations.

The beneficiary's rights and obligations are non-transferable, which does not apply to the beneficiary's claims against the foundation for benefits due to the beneficiary. However, beneficiaries may waive their rights, which requires written form with a notarised signature. Waiver of all rights by a beneficiary is equivalent to waiver of beneficiary status.

The beneficiaries may address comments, opinions or recommendations to the bodies of the family foundation regarding its activities. On the other hand, not every beneficiary will necessarily be a member of the assembly of beneficiaries, as this right extends only to beneficiaries granted the right to participate in the assembly in the statute. The statute must identify at least one beneficiary entitled to participate in the assembly of beneficiaries. This way, the founder can exclude from decision-making power any beneficiaries the founder deems unsuitable to adopt resolutions on the foundation's key issues, but without depriving them of the right to receive certain benefits from the foundation's assets. The members of the assembly of beneficiaries are obliged to exercise due care in carrying out their duties.

The assembly of beneficiaries adopts resolutions on key issues for the foundation. In particular, a resolution of the assembly of beneficiaries is required for:

- Consideration and approval of the family foundation's financial statements for the previous financial year

- Discharge of the members of the family foundation's bodies for performance of their duties
- Deciding on distribution or coverage of the net financial result
- Selection of an audit firm, when the financial statements of the foundation are subject to mandatory audit under the Accounting Act
- Appointment and removal of members of the management board in the event of the founder's death and the absence of a supervisory board, unless the statute provides otherwise
- Appointment and removal of the management board after the founder's death, unless the statute provides otherwise
- Appointment of an attorney-in-fact to represent a family foundation with no supervisory board to conclude a contract between the foundation and a member of the management board, and in a dispute between the foundation and a member of the management board
- Appointment of an audit firm or team of auditors to perform an audit of the management of the family foundation's assets, and incurring and fulfilment of private and public liabilities, in terms of regularity, reliability and compliance with the law and the purpose and documents of the family foundation
- Dissolution of the family foundation for important reasons other than those specified in the statute or the act, which requires a unanimous resolution of the assembly of beneficiaries
- Determination of the manner of representation of the family foundation during the liquidation period, if not provided for in the statute or a ruling of the registry court
- Approval of the liquidation opening balance of the family foundation drawn up by the liquidators, as well as approval of the liquidators' activity report and financial statements following each financial year during the liquidation
- Transfer of immovable property to a buyer of the liquidators' choice in the course of liquidation and indication of the price at which this may take place
- Approval of the liquidation report as of the day prior to the release of the assets remaining after satisfying or securing the foundation's creditors
- Other matters specified in the act or the statute.

Therefore, in the statute the founder may also specify other activities for which the approval of the assembly of beneficiaries is required.

If the act requires a resolution of the assembly of beneficiaries to perform a legal act, the legal act performed without the required resolution is invalid. On the other hand, a legal act performed without the approval of the competent body of the family foundation, required exclusively by the statute, is valid, but this does not preclude the liability of management board members to the family foundation for violation of the statute.

As a rule, the assembly of beneficiaries is convened by the management board, unless the statute provides otherwise. Also, it is permissible to indicate in the statute the cases when the beneficiaries may request the management board to convene an assembly of beneficiaries. Then, such a request should specify the proposed agenda for the meeting of the assembly of beneficiaries.

Unless otherwise provided in the statute, the assembly of beneficiaries is valid regardless of the number of votes represented, except for resolutions on appointment or removal of the management board or supervisory board, when participation of at least half of the assembly's members is required. Resolutions of the assembly of beneficiaries are adopted by a simple majority of votes, unless the statute provides otherwise. Each beneficiary entitled to participate in the assembly holds one vote, unless the statute provides otherwise, and therefore it is permissible to privilege certain beneficiaries by granting them a larger number of votes.

Meetings of the assembly of beneficiaries are held at the foundation's premises, unless the statute provides otherwise. Beneficiaries may also participate in meetings via telecommunications, unless otherwise provided in the statute.

Beneficiaries may participate in the assembly of beneficiaries and exercise their voting rights in person or by proxy. A proxy to participate in the assembly of beneficiaries and exercise voting rights must be made in "document" form to be valid. Document form does not require "written" form. It is enough to submit a declaration of will in the form of a document enabling identification of the person making the declaration, in a medium enabling examination of the contents.

The set of powers of the assembly of beneficiaries shows that it is a body authorised to make key decisions for the foundation in certain situations, such as election of members of other bodies or dissolution of the family foundation for important reasons other than those indicated in the statute or the act. From this perspective, it is important to indicate in the statute which beneficiaries will be entitled to participate in the assembly of beneficiaries, what number of votes they should have, and what majority will be required to adopt resolutions on particular matters.

## Summary

To a large extent, the scope of powers of the family foundation's bodies, their control and cooperation can be shaped by the founder, to whom the parliament has left relatively broad freedom to introduce relevant provisions in the statute. Therefore, the founder can exclude certain beneficiaries from the decision-making process, without depriving them of specific benefits from the foundation's assets. This allows solutions to be tailored to the needs of the particular foundation, including family relationships, the extent of the assets managed by the foundation, and its anticipated activities.

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# Reducing the risks of setting up a family foundation

**Like any other legal form, a family foundation may also involve the risk that the management of assets will be delegated to incompetent persons, the foundation will act in a manner contrary to its stated purpose or the interests of its beneficiaries, or it will conduct business activity in areas not permitted for a family foundation. However, in the Family Foundations Act, the Polish parliament has provided certain tools to prevent such situations.**

With all the advantages of a family foundation, it should be remembered that a lot depends on the individual solutions adopted in specific cases, i.e. on the wording of the foundation's statute, the designated beneficiaries, their powers, the structure of the foundation's bodies, and the persons elected to these bodies. If the foundation's statute is poorly worded, the contribution of assets to a family foundation may result in a loss of direct control over the assets, or the risk of mismanagement or intentional abuse.

## Risk of losing control over the foundation and its assets

The founder can significantly reduce the risk of losing control over the assets primarily through proper construction of the family foundation's statute, the powers of the foundation's bodies, and the rules of their cooperation and control. Particularly, it will be important for the founder to indicate the objectives of establishing the family foundation and the guidelines for managing and investing the assets. Also, the founder may establish a supervisory board whose approval is required to perform acts specified in the statute and act as a controlling body (if there are more than 25 beneficiaries, establishment of a supervisory board is mandatory). Also, the founder may address comments, opinions or recommendations to the bodies of the foundation regarding its activities.

The members of the management board and supervisory board of a family foundation are obliged to act loyally towards the foundation, and are also liable for damage caused by an act or omission violating the statute (among other things), unless they are not at fault. Therefore, violation of the statute by a member of the foundation's bodies may result in the member's liability.

Also, the founder may specify activities for which approval of the assembly of beneficiaries is required. In this case, the founder may decide through appropriate provisions in the statute which beneficiaries have the right to participate in the assembly of beneficiaries.

To reduce the risk of the foundation acting contrary to the founder's intentions, it is also worth detailing the rules for amending the statute. In this regard, the founder may establish certain requirements in the statute, for example a qualified majority of votes at the meeting of beneficiaries needed to make such changes or the need to obtain additional approval from the foundation's supervisory board, or some other procedure as appropriate.

It should be remembered that management of the assets of a family foundation is subject to mandatory audit. The assembly of beneficiaries appoints an audit firm or team of auditors to examine the management of the assets of the family foundation, incurrence and performance of obligations and public charges, for regularity, reliability and compliance with the law and the purpose and documents of the family foundation.

The audit team may include auditors, tax advisors, advocates or attorneys-at-law. The auditors must be independent, i.e. only persons who during the period covered by the audit and during the audit:

- Are independent of the family foundation
- Did not and do not participate in the decision-making process of the family foundation
- Have not provided and do not provide audit or consulting services to the family foundation.

An audit must be carried out at least once every four years, while the statute may provide that it is to be conducted more frequently. In the case of a family foundation whose financial statements are subject to mandatory audit under the Accounting Act, the audit is to be conducted annually before approval of the financial statements. The audit report is submitted to the management board, and the management board then presents it to the supervisory board, or if there is no supervisory board, to the assembly of beneficiaries at the next meeting.

Therefore, a mandatory audit assessing the proper management of assets of a family foundation is one of the control mechanisms for preventing abuse and eliminating irregularities.

## Restrictions on conducting business activity

While a family foundation may conduct business activity, the regulations provide an exhaustive catalogue of permissible activity. Therefore, it is not feasible to contribute directly to a family foundation every enterprise that might be pursued, due to the unfavourable tax consequences in the event of conducting activities not allowed for foundations (an increased 25% corporate tax rate). From this perspective, it is more efficient to conduct activity in the form of a commercial company (or partnership), where the shares are contributed to the foundation. If the founder wishes to contribute to the foundation an undertaking previously carried out in the form of an individual business that does not fall within the scope of business allowed for family foundations, it may be necessary to first convert it into a company or partnership. In this context, it should be noted that a business operator who is a natural person conducting activity in his or her own name can transform the business into a single-shareholder company.

Thus, when planning to contribute a business to a family foundation, the first thing to consider is whether an appropriate corporate structure should be created beforehand. For more on this topic, see the article "Running a business through a family foundation."

## The possibility of dissolving a family foundation—sometimes against the founder's will

The assumption is that a family foundation is set up on a long-term basis to protect the assets for future generations. However, the parliament provides for the possibility of dissolution and liquidation of a family foundation, creating a risk of losing control over its assets.

A family foundation may be dissolved for various reasons, including as a result of the occurrence of circumstances indicated in the statute, in particular when the duration for which the foundation was established has elapsed, when the purpose of the foundation has been fulfilled, or when the foundation is managed in a manner contrary to its purpose or the interests of its beneficiaries, or for other valid reasons it is no longer purposeful to continue the foundation's activities. In either case, a decision by the competent authority of the family foundation or the registry court is required. By contrast, the dissolution of a family foundation for other valid reasons requires the unanimity of the assembly of beneficiaries.

In the course of liquidation, a family foundation must first perform its obligations to entities other than its beneficiaries. Only after these obligations are fulfilled can the benefits to the beneficiaries be paid and the assets distributed. The liquidators' duties include winding up of current business, collection of debts, and fulfilment of the family foundation's obligations.

To protect against the negative consequences of dissolution and liquidation of a family foundation, the founder may regulate in the statute the circumstances justifying its dissolution and the use of the property remaining after liquidation. If a family foundation is liquidated during the founder's lifetime, he or she is solely entitled to receive the property remaining after liquidation, unless otherwise provided in the foundation's statute. Also, the entities entitled to the assets of a family foundation after its dissolution may be selected beneficiaries, but also persons outside this group, depending on the founder's intention expressed in the statute. In the event of the founder's death and the lack of any beneficiary entitled to the property, the assets of the family foundation go to the founder's heirs.

## Summary

Certainly, a family foundation has many advantages over the previous forms of succession planning or effective management of family assets provided for in Poland. Due to the favourable tax arrangements, it can also be used as an investment vehicle. However, when deciding on a family foundation to manage assets, it is important to ensure that not only the objectives, but also the interests of the founder and the foundation's beneficiaries are properly safeguarded, in particular through the wording of the foundation's statute. As with other legal forms, the success of a family foundation depends on an effective structure, but also on selection of the right people to manage the foundation.

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