

Luxembourg private foundation

A new tool for private wealth management

On July 22nd 2012, the Luxembourg Chamber of Deputies lodged a draft law n°6595 in relation to the creation of a patrimonial foundation (the “Draft Law”) whose purpose is to enlarge the current panel of wealth management instruments with an *ad hoc* vehicle already existing in neighboring countries: the so called “private foundation” (“*fondation patrimoniale*”). The draft law is expected to be enacted soon.

This new vehicle shall constitute an orphan entity (i.e. without shareholders) that would allow the founder to achieve simultaneously the following objectives:

- Planning the succession of the family estate: in particular, maintaining unity of the estate while guaranteeing continuity of its management;
- Preserving privacy of the family by limiting disclosure of the patrimonial foundation to the public.

1. Setting-up of the patrimonial foundation

The patrimonial foundation shall be founded by one or more individuals or patrimonial entities in charge of the management the estate belonging to one or several individuals (e.g. a trust or another patrimonial foundation) for a definite or indefinite duration.

Even though no license or administrative authorization will be required, the patrimonial foundation shall be set-up before a Luxembourg notary and be contributed with a minimum of 50,000 euro. It will have legal personality as of its incorporation and shall have its registered seat in Luxembourg. In this context, while trusts have no distinct legal personality, the patrimonial foundation, being a separate entity, holds an estate separate from its founder, directors or beneficiaries. As such, patrimonial foundations offer an effective **asset protection** mechanism.

2. A flexible vehicle

(i) Flexible investment structure

A patrimonial foundation will be entitled to hold any **movable or immovable assets**. For instance, it may hold shares in commercial companies, hold a life-insurance contract or be the settlor of a trust. However it shall be prohibited from engaging in any commercial or industrial activity, such as managing its participations in companies.

As an **orphan entity**, it has no shareholder or member. However, it may issue nominative “certificates” to any individual or patrimonial entity (such as defined by the Draft Law). Those

certificates are linked to the patrimonial foundation's assets and represent rights deriving from those assets making those certificates comparable to an interest in possession trust. They shall be registered by the patrimonial foundation and only transferable to the founder or other beneficiaries (or their patrimonial vehicles and successors), while being exchangeable against the certified asset. This system shall constitute an effective allocation system of the flow of revenues or proceeds from one or more specific assets to one or more specific beneficiaries.

As an additional protection to the beneficiaries, the patrimonial foundation shall be prohibited from disposing the certified assets, unless otherwise provided for in the deed of incorporation or any extra statutory regulation.

(ii) Flexible structure of management

The structuring of the management of a patrimonial foundation remains one of the main points of attractiveness of such a vehicle. The Draft Law leaves maximum leeway to the deed of incorporation to organize the management of the vehicle.

The private foundation shall be managed by one or several directors, being individuals or entities, vested with the power to carry out all acts necessary or useful in furtherance of the object of the patrimonial foundation. The directors are appointed and revoked by the founder(s). Absent any provision to this effect, they are appointed by the supervisory board (if any), by cooptation of the other directors in office, or by a court decision.

As an additional means of protection of the beneficiaries, a supervisory board composed of at least 1 individual must be set-up in case either the assets of the patrimonial foundation exceed 20 million euro or the patrimonial foundation counts more than 5 beneficiaries. If both the above thresholds are met, the supervisory board is increased to 3 individuals. This supervisory board is in charge of controlling the management of the patrimonial foundation.

Governance planning of the patrimonial foundation may be efficiently fine-tuned through the following provisions of the Draft Law:

- in case of vacancy of one or more directors, the deed of incorporation may contain a clause pursuant to which the founder(s) are entitled to establish a list of directors that would take office in case of vacancy of the originally appointed directors.
- Representation of the patrimonial foundation may be restricted to several directors, acting jointly and the daily management of the patrimonial foundation may be vested with one director or a third party.
- the powers of the supervisory board are freely defined in the deed of incorporation and, absence of a supervisory board, control of the management may be granted to the founder(s).

(iii) A stable vehicle

As an orphan vehicle, the patrimonial foundation is deprived from general meeting of shareholders. As such, the founder(s) is vested with the power to amend the deed of incorporation and the deriving extra statutory regulation.

This power may be vested with the board of directors (in conjunction with the supervisory board, if any). But, in such instance, and as an additional measure of stability of the vehicle, decisions pertaining to (i) the amendment of the object, (ii) dissolution of the patrimonial foundation before its

term, (iii) change of the beneficiaries (or the rules of determination) or the objectives (or their rules of determination) of the patrimonial foundation must be expressly set forth in the deed of incorporation and may only be adopted for serious reasons (motifs graves) by unanimous consent of the directors (on proposal of the supervisory board, if any). The Draft Law gives examples of such reasons, such as impossibility to carry out the objective of the patrimonial foundation or absence of existing or determinable beneficiaries.

3. Restricted information available to the public

While being registered with the Luxembourg register of commerce and companies (but not being considered as having a commercial activity), only limited information shall be made available to the public. In particular, in order to protect the privacy of the family, no information on the founder, the beneficiaries or the contribution shall be disclosed.

In addition, simplified annual accounts shall be drafted but no filing with the Luxembourg register of commerce and companies will be required.

However, information relating, inter alia, to the annual accounts, the deed of incorporation of the patrimonial foundation (including the name of the founder) and the identity of the beneficiaries shall be kept at the registered office of the patrimonial foundation and made available to the founder, the directors, supervisors (if any) and the beneficiaries (subject to the provisions of the incorporation deed) of the patrimonial foundation. In this context, in order to be compliant with the recommendations of the Financial Action Task Force, the identity of the effective beneficiaries of the patrimonial foundation shall be available either at its registered office or at any other location in Luxembourg.

4. Tax aspects

From a tax point of view, the patrimonial foundation can be implemented as a very efficient vehicle.

Direct tax aspects

The patrimonial foundation will in principle be fully subject to the standard Luxembourg corporate income tax and municipal business tax applicable to resident taxpayers (2014 standard combined corporate tax rate for companies located in Luxembourg City: 29.22%).

However, income derived from securities, i.e. in particular dividend or interest income, and capital gains realized on the assets generating such income, as well as capital gains on any other movable assets held for a period of more than 6 months, shall be exempt from corporate income tax and municipal business tax. Moreover, the face amount and the cash surrender value of a personal life insurance policy contracted by the founder and transferred to the private foundation shall be exempt from corporate income tax and municipal business tax. A patrimonial foundation will be also be exempt from net wealth tax.

Allocations of any kind to the founder or the beneficiaries shall not be subject to Luxembourg withholding tax. Non-resident founders and beneficiaries will not be taxable in Luxembourg on allocations derived from the foundation while Luxembourg resident founders and beneficiaries will benefit of a tax exemption of 50% of the allocations derived from the foundation.

Indirect tax aspects

Transfers of movable or immovable property by the patrimonial foundation to the beneficiary(ies) during the lifetime of the founder are subject to the general proportional donation duties (1.8% to 14.4% depending on the family kinship of the beneficiary(ies) and the founder) as applicable in the same manner as if the transfer had been made directly between the founder and the recipient beneficiary; the same principle applies in case the private foundation is liquidated or dissolved during the lifetime of the founder and the movable or immovable property that was part of the estate of the private foundation is transferred to the beneficiary(ies).

The transfer of the movable or immovable property to the beneficiary(ies) upon the death of the founder will be subject to inheritance tax. However, in case the founder was non-resident in Luxembourg, only the transfer of real estate situated in Luxembourg to the beneficiary(ies) is subject to inheritance tax. In either case the applicable inheritance tax rate varies depending on the family kinship between the founder and the beneficiary (0% applies e.g. to transfers to the founder's spouse, partner, or ascendants or descendants in direct line, 12% apply e.g. to transfers to the brother or sister of the founder and 40% apply in the absence of any family kinship between the founder and the beneficiary(ies).

For further information, feel free to contact the following persons:

Franck CERA fcera@ammclaw.com

Xavier HUBAUX xhubaux@ammclaw.com

James O'NEAL joneal@ammclaw.com