



Family Foundations Act promulgated

On 21 February 2023, the Family Foundation Act was promulgated, which means that it will come into force on 22 May 2023.

The aim of the Act is to introduce to the Polish legal system the family foundation – an entity created for the purpose of accumulating assets and managing them in the interests of the beneficiaries and providing benefits for the beneficiaries. The intention of the Act's authors is for the family foundation to be a tool created primarily with a view to facilitating the succession process in Polish family businesses.

Key legal aspects of the creation and operation of a family foundation

Legal personality

Family foundations will have legal personality and will be based in the territory of Poland. Family foundations will be registered with the register of family foundations.

Founder

The entity setting up a family foundation will be the founder or founders. A founder can only be an individual with full legal capacity. Therefore, a family foundation cannot be established by a commercial company or other legal persons.

Setting up a family foundation

A family foundation can be set up both during the founder's lifetime, based on a deed of formation drawn up by a notary, and after the founder's death, based on a will drawn up by the founder. If a family foundation is created on the basis of a will, it can have only one founder. A family foundation will acquire legal personality when it is registered with the register of family foundations.

Family foundations – purpose and operating principles

The purpose of a family foundation is to accumulate and manage the founder's assets in the interests of the beneficiaries and to provide benefits to the beneficiaries.

The main and key document governing a family foundation will be its statutes. The family foundation's statutes should set out the specific aims of the family foundation and its operating principles in order to ensure that the founder's intent is carried out in the future. Importantly, on a number of issues the law leaves it up to the founder to regulate them in the family foundation's statutes, including the issue of the rules for amending the statutes themselves.

Family foundation activity

A family foundation will only be able to carry on business activity to the following limited extent:

- to dispose of property, provided the property was not acquired solely for the purpose of further disposal,
- to lease, rent or make available property for use on any other basis,
- to join and participate in commercial companies, investment funds, cooperatives and entities of a similar nature based in Poland or abroad, and to participate in such companies, funds, cooperatives and entities,
- to buy and sell securities, derivatives and rights of a similar nature,
- to extend loans to entities specified in the Act,
- to trade in foreign means of payment belonging to the family foundation for the purpose of making payments related to the activities of the family foundation,
- production of plant and animal products on the rules laid down in the Act,
- forest management.

A total ban on family foundations conducting business activity was a significant flaw in the previous bill. The current wording of the Act already offers this possibility, but to a limited extent. On the other hand, the possibility of foundations joining companies paves the way for considering the use of foundations as a controlling entity for the holding of a family firm.

Family foundation assets and beneficiaries

The assets of a family foundation are contributed to it by its founder. The value of the assets contributed to the family foundation will be specified by the founder in the statutes – the minimum value of the assets will, however, be PLN 100,000. In addition, the foundation's assets may come from donations, bequests and legacies, as well as from the foundation's business activity.

It is worth noting that the foundation statutes may, inter alia, indicate the rules for investing the family foundation's assets.

Family foundation beneficiaries

The statutes will specify the beneficiaries of the family foundation. Beneficiaries may be individuals and non-governmental organisations, as well as the founder him/herself. Beneficiaries will be entitled to receive from the family foundation the benefits specified in the statutes or to receive the foundation's property in the event of its dissolution. The benefits to which a beneficiary is entitled will be decided by the founder at his/her discretion. A benefit from a family foundation may be granted either on a condition or subject to a time limit, e.g. on reaching a certain age or completing education.

Family foundation bodies

As in the case of capital companies, the family foundation envisages the functioning of bodies, i.e. the management board, mandatory in each case, which will manage the foundation's affairs, the supervisory board, which will perform supervisory functions, and the beneficiaries' assembly, which is also given a number of important powers.

Unless otherwise provided for in the statutes, management board members will be appointed and recalled by the founder and, after the founder's death, by the supervisory board, if one has been established. In the event of the death of the founder and the absence of a supervisory board, members of the management board will be appointed and recalled by the beneficiaries' assembly. In addition, unless the statutes provide otherwise, the power to appoint and recall supervisory board members is vested in the founder and, after the founder's death, in the beneficiaries' assembly.

It is worth noting that, when planning the use of a family foundation in succession, it is important to consider the staffing aspect of the family foundation's management and supervisory board and their competences, given that these are the bodies that will take control of the foundation's affairs after the founder's death.

Liability of a family foundation

A family foundation will be jointly and severally liable with the founder for the founder's liabilities that arose prior to its establishment and it is not possible to exclude this liability without a business partner's consent. In practice, this means that the founder's business partner can claim payment from both the founder and the family foundation.

However, the limit on a family foundation's liability will always be the value of the assets the foundation receives from the founder. The aim of these regulations is to protect the founder's creditors so that their situation does not deteriorate even though the founder transfers his/her assets to the foundation.

Dissolution of a family foundation

The Act provides for several cases in which a family foundation may be dissolved, e.g. for reasons specified in its statutes or for the purpose of achieving the foundation's objective. In this case, the foundation is dissolved in connection with a resolution of the competent foundation bodies. Also, the registration court has gained the power to rule on the dissolution of a foundation, subject to the occurrence of certain circumstances indicated in the Act. The list of entities entitled to dissolve a foundation appears to be broad and the circumstances are vague, which may raise concerns about the risk of dissolving the foundation in a manner contrary to the founder's intent. In this sense, the Act does not necessarily give a full guarantee of the permanence of the existence of a family foundation.

Family foundation and legitim

The legitim entitlements provided in Polish law for individual family members often pose an obstacle to the freedom to dispose of assets by the owner of a family business to those family members who are interested in continuing the business. The Act will bring certain changes in this respect.

First of all, it should be noted that the assets contributed by the founder as the foundation's initial fund will not be added to the legitim if the founder dies no earlier than ten years after making the transfer to the family foundation. In this case, the contribution to the foundation will be excluded from legitim claims. In addition, the benefits received from the family foundation by the beneficiary entitled to a legitim will reduce the value of his/her legitim.

The Act will also make it possible to request deferral of payment of a legitim and to divide it into instalments or, in special cases, to reduce it, which will be decided by the court.

In addition, the Act explicitly confirms the possibility of an agreement being concluded with a family member to waive a legitim. However, the decision to enter into such an agreement is entirely voluntary for both parties.

Key tax aspects of the operation of a family foundation

Taxation of foundation income

A family foundation is generally exempt from income tax until the assets are distributed to the foundation's beneficiaries or the foundation is liquidated. The exception is if the family foundation carries out activities beyond those envisaged for a family foundation.

In light of the law, the exemption of a family foundation from taxation will apply to the foundation's property increments such as:

- receipt of assets from a founder or in the form of donations from other persons,
- dividends received from subsidiaries,
- income from the sale of shares (and from any restructuring activities concerning shares in joint-stock companies),
- income from securities and financial instruments,
- interest on loans extended to beneficiaries or subsidiaries of a family foundation,
- income from rent and lease,
- income of an agricultural undertaking (on certain conditions).

However, a family foundation conducting activities other than those indicated above, e.g. operating activity and disposal of property that was acquired by the family foundation solely for resale, will be subject to income tax at 25%.

In light of the final version of the Act (following the Senate's amendments), tax exemption for the sale of shares in limited liability companies and of all the rights and obligations in partnerships by a family foundation is debatable. A literal interpretation of the provisions indicates that the income from the sale of these rights will be subject to the 25% tax indicated above, so a change in succession plans after the contribution of these assets to the family foundation may involve punitive taxation of these new plans.

Taxation of payments to beneficiaries

A payment from a family foundation to a beneficiary is first subject to taxation for the foundation itself at 15% of the amount paid out or of the assets placed at the beneficiaries or the founder's disposal.

In the case of the liquidation of a family foundation, the payout of the foundation's assets is also taxed as above, but in this case, the foundation can include in the tax base (as opposed to a payout to the beneficiary without liquidation) the tax costs incurred by the founder in handing over the assets. As a result, taxation in this case may be lower.

In contrast, a family foundation beneficiary who is a member of the founder's immediate family and the founder him/herself will generally be exempt from taxation on the benefits received from the family foundation. This principle may be disrupted depending on how the foundation acquires the assets. This issue therefore needs to be structured accordingly.

Other beneficiaries (other than immediate family members) will be taxed on the payments received from the family foundation at 15%. This taxation will also occur in the case of payments by the foundation to beneficiaries who are the closest person to the founder of a benefit not derived from property contributed by the founder.

At the same time, at the parliamentary work stage, the idea of entities that are directly or through their shareholders related to family foundations being subject to Estonian CIT finally collapsed.

Regulations allowing the transfer to Polish family foundations of the assets of foreign foundations under preferential tax conditions for the beneficiaries were not accepted either.

Information obligations to tax authorities

Under the Act, a family foundation is obliged to submit to the National Revenue Administration authorities certain information about the foundation and its beneficiaries, i.e. a list of beneficiaries, an inventory of property (this inventory contains information on persons contributing property to the family foundation and the type and value of the property components) and information on benefits or property transferred in connection with the dissolution of the family foundation.

Foundation's liability for the founder's tax liabilities

A family foundation will be jointly and severally liable for the tax liabilities of the founder. This liability is limited to the value of the assets contributed to the foundation without the possibility of it being limited, which may introduce uncertainty regarding the actual value of the family foundation's assets and their security. In comparison, when shares or stocks are donated to family members, they are not liable for the donor's tax arrears, much less for those undisclosed at the time of the donation.

Initial assessment of family foundation Act

Family business owners should consider establishing a family foundation; however, they should not treat this solution as a priori ideal for their situation. Determining whether a family foundation will prove to be a useful mechanism for a given family business will depend on a number of aspects, e.g. the vision of the planned succession held by the doyens and the group and the engagement in the family business of the successors, who could become beneficiaries of the family foundation in the future.

Nevertheless, a family foundation can be a useful succession tool in particular because it will allow the status of its beneficiary to be separated from the manager of the family's assets. It is worth noting, moreover, that the Act gives the founder the flexibility to define the objectives of the family foundation and the rules of its operation. In this sense, in many aspects it will be possible to create an entity tailored to the family's needs. This adaptation will, however, require a great deal of precision and imagination when designing the foundation's statutes.

On the other hand, elements of the family foundation's design that do not necessarily serve succession purposes well,

such as the broad powers of beneficiaries in some foundation operations, should not be overlooked. Succession using a family foundation will also be largely pre-determined at the stage of its creation, which limits the possibility of change under the influence of future factors.

It is also worth considering using a family foundation as a solution not so much to replace existing succession mechanisms in family businesses, but rather to complement them.

It is worth highlighting that, with regard to issues related to legitim that often pose an obstacle to free succession, the Act introduces significant changes that will be of great practical importance, although they do not solve the legitim problem entirely. The amendments do, however, make it possible to defer payment of the legitim and to divide it into instalments or, in certain cases, to reduce it.

From a tax perspective, regulations provide for the income of foundations to be tax exempt and for more preferential tax rates for payments from foundations to beneficiaries than for transfers from other types of entities. A more in-depth analysis of these regulations, however, reveals certain restrictions and risks that need to be taken into account. The tax exemption for foundations is not unconditional and the wording of some of the rules is evaluative, which may lead to the risk of a dispute with the tax authorities. In contrast, from the perspective of payments to beneficiaries, while the tax rate itself is preferential, the rules for calculating the tax lead to a situation where not only the foundation's income but also the distribution of capital contributed to the foundation is effectively taxed. There are also doubts about the rules for taxation of such payments when the founder contributes assets to the foundation successively.

The Domański Zakrzewski Palinka law firm was one of several law firms that submitted comments on the draft law, which led to the current, more favourable wording of the Act. The Act is currently awaiting entry into force. However, we invite you to contact us now so that together we can make an initial assessment of the suitability of the new provisions of the Family Foundations Act for the implementation of succession goals in your family business.

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