

By **Alexander A. Bove, Jr.**

## Building a **Solid** (Private) Foundation

Will a New Hampshire law start a new trend in estate planning?

It's now possible to establish here in the United States, a non-charitable private foundation (NCPF), an entity that was heretofore reserved for select jurisdictions outside the United States. At the moment, however, you may only establish such an entity in one state, New Hampshire, which, in mid-2017, adopted the country's first NCPF law.<sup>1</sup> Is this a small step for a state and a giant leap for U.S. estate planning? Or, is it merely an awkward attempt to go where no state has gone before?

When you think about it, here in the United States, we have only one basic vehicle for estate planning—the trust. Sure, we have limited liability companies, corporations, and the like, but they don't provide anywhere near the opportunities for the same long-term family and tax planning, creditor protection and estate distribution that we have with trusts. Numerous commentators (myself included) have repeatedly observed that the trust is the most flexible document in an estate plan. And, we know that trusts are used the world over—or are they? While the answer is generally yes at present, it's only recently from a historic standpoint that many civil law jurisdictions have recognized the trust,<sup>2</sup> which originated in a common law jurisdiction. So, what did they do before that? Most of them used NCPFs.

### NCPFs vs. Trusts

The NCPF isn't established to benefit the public, and thus, its terms are strictly private. It's almost as common in those civil law jurisdictions that use NCPFs

as trusts are in common law jurisdictions. NCPFs, like trusts, are typically established to hold family wealth for the benefit of a family. From there, however, the similarities fade. While a trust is a relationship between the trustee and the beneficiaries, with the trustee owing an affirmative fiduciary duty to the beneficiaries, the NCPF is a separate legal entity managed by directors, in which the directors owe a duty primarily to the NCPF itself and only secondarily, if at all, to the beneficiaries.<sup>3</sup> While a traditional common law trust would fail for lack of beneficiaries who have the inherent right to enforce the trust, an NCPF could be established with no beneficiaries, or it could be structured so that, depending on the jurisdiction, the beneficiaries have very limited or no rights. Further, many civil law jurisdictions don't recognize any fiduciary duty (other than good faith) between the directors of the NCPF and its beneficiaries.<sup>4</sup> For this reason, many practitioners believe that the NCPF offers more creditor protection than a trust.

### The Act

For U.S. estate-planning attorneys, except for those who are active in international estate planning, all of the foregoing may be academic, because up to now, no U.S. state would recognize the NCPF. As the article title suggests, however, we now have one state that's adopted NCPF law, so the questions arise: What's it all about, and how can we use it? The New Hampshire Foundation Act (the Act) permits the establishment of an NCPF which, as in the foreign jurisdictions, will be a separate legal entity, not dependent on the existence of any beneficiaries, so long as it has a purpose.<sup>5</sup> For some reason, however, the apparent intention of the New Hampshire legislature wasn't to create a statute that, if followed as is, allows the formation of an NCPF of the type used in the civil law jurisdictions. Instead,



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as explained below, the statute seems to result in the formation of an entity that, for all practical purposes, would operate as a trust, cloaked in a legal entity called an NCPF. For example, if we were to form an “off-the-shelf” New Hampshire NCPF following the statute as drafted, we would have an NCPF that the directors have a duty to manage “solely in the interests of the foundation’s purposes and the beneficiaries’ interests,” along with duties of impartiality, prudence, as well as duties to keep the beneficiaries reasonably informed and to maintain records.<sup>6</sup> Sound like a trust?

The strange thing about the Act is that it allows every one of the foregoing duties to be eliminated by providing in the bylaws that there will be no such duties on the part of the directors. This is because every one of the foregoing duties is preceded by, “unless the governing documents provide otherwise.”<sup>7</sup> The only duty that you can’t override is the duty of good faith.<sup>8</sup> For example, the directors may keep sloppy records, or even no records at all, so long as they do so in good faith. In addition to the statutory duties to the beneficiaries, the Act allows a beneficiary to challenge any action taken by the NCPF.<sup>9</sup> This could be comparable to a beneficiary’s right under a trust, and the Act doesn’t allow this right to be removed by the bylaws.

Interestingly, then, we can eliminate virtually all of the directors’ duties, and the beneficiaries would still have the right to challenge the directors’ acts. But, if we eliminate the duty of prudence, the duty of impartiality, the duty to keep records and the duty to keep beneficiaries informed, and yes, even the duty to manage the NCPF in the interests of the beneficiaries and the NCPF’s purpose, on what basis could the beneficiaries sustain a challenge since there are no duties (other than the duty of good faith, but as to what)? Perhaps such an arrangement is unlikely to occur, but why is the Act drafted in such an odd manner?

Similar to the default duties, are the default provisions for the “reserved” powers of the founder?<sup>10</sup> Once again, we see the default phrase “unless the governing documents provide otherwise,” and the section goes

on to provide that the founder will be held to have retained extensive powers over the trust, whoops, I mean NCPF, including the power to amend or restate the bylaws, dissolve the NCPF, remove and replace directors and direct distributions.<sup>11</sup> In effect, these powers together with the default duties mentioned above would make the NCPF almost the exact legal equivalent of a revocable trust, and if that’s what we

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want, why are we messing with an NCPF?

The traditional civil law foundation is one established by an individual with some wealth that she wishes to place in a vehicle that will accomplish her wishes for herself and her family’s benefit, but with minimal interference from descendants or other relatives after her death and minimal interference from creditors. She wants it to continue that way for generations. Although most jurisdictions allow beneficiaries limited rights to information and standing to address a breach of duty (to the NCPF, not to themselves)—the beneficiaries generally have no rights to interfere with the management of the NCPF or the discretion of the directors.<sup>12</sup> To accomplish this with a New Hampshire NCPF, the bylaws would have to be drafted to negate



almost every duty of the directors and most powers of the founder. Further, it should be noted that it isn't clear whether the duty in a given case could be split. That is, instead of deleting the duty to act "solely in the interests of the foundation's purpose and the beneficiaries' interest,"<sup>13</sup> could we say, "solely in the interests of the foundation's purposes?" If so, perhaps that would allow us to get much closer to a real NCPF.

And speaking of purposes, the Act provides that the NCPF must have a purpose,<sup>14</sup> though it needn't have any beneficiaries. One of the essential requirements for an entity or a trust that's established for a purpose rather than for a beneficiary is that there must


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be some provision for the oversight or enforcement of the purpose if the directors or trustees aren't complying with their obligation to carry out the purpose. Thus, every jurisdiction that recognizes the purpose trust or purpose NCPF mandates that the governing document contain provisions for the appointment of an enforcer.<sup>15</sup> The Act contains no mention at all of the requirement of an enforcer in such a case, meaning that unless the drafter thought to provide for one, if there was wrongdoing or a breach of duty in managing a New Hampshire purpose NCPF, it would be left to chance that someone may come forward to file a petition in court requesting the appointment of an enforcer to address the problem.<sup>16</sup>

Some commentators have suggested that having NCPF law here in the United States may attract foreign individuals who are familiar with the NCPF, or even a migration of an existing foreign NCPF. In fact, the Act does contain a provision allowing the registration of a foreign NCPF.<sup>17</sup> Such registration allows the for-

eign NCPF to engage in any "registerable activity" in the state. This would include most usual investment activities but excludes the carrying on of a business. One problem is that once registered under the Act, the foreign NCPF has "the same duties, restrictions, penalties, and liabilities...imposed on a foundation of like character."<sup>18</sup> It's unclear what's meant by an NCPF of "like character," but if it means a New Hampshire NCPF of like character (which is likely the case, as otherwise the state would have to examine and interpret the law of the applicable foreign jurisdiction), then that could present a serious problem for the foreign NCPF, as it's highly unlikely that the duties and restrictions imposed by the Act would be the same as those of the foreign jurisdiction, and no doubt the foreign directors wouldn't want to adopt new duties and restrictions that may not be in compliance with their law or that may expose them to new liabilities. If, however, it turned out that you can overcome such hurdles, it's feasible to picture a situation in which a foreign NCPF that had U.S. beneficiaries wished to establish a U.S. presence, and it might consider registering here and establishing an investment account for the convenience of the U.S. beneficiaries. The complicated international tax considerations, however, are another matter, as are the U.S. tax considerations, which will be dealt with in a future article. There's another thing about the foreign NCPF rules that could discourage registration. With a domestic New Hampshire NCPF (and foreign NCPFs) the names of the directors may be kept private, but for a foreign NCPF registered in New Hampshire, the certificate of registration must disclose the names and addresses of the foreign NCPF's directors.<sup>19</sup>

The last comment I wish to make, and which I feel is one of the most important, is this: New Hampshire, like virtually all of our states, is a common law state, and when a matter dealing with a civil law NCPF (established in New Hampshire) arises before a New Hampshire judge who presumably would have no familiarity with civil law, will she view it and judge it based on trust law, especially because the statute is clearly fashioned with trust law in mind? Or, will it be viewed as a "real" civil law PF, like a corporation with no beneficiaries? With absolutely no precedent (other than foreign law, if they would be willing to consider it) or even treatises to guide

the judiciary, we may have a long wait before the several kinks in this new law are ironed out. 

## Endnotes

1. New Hampshire Foundation Act (the Act), RSA 564-E.
2. Liechtenstein is the first civil law jurisdiction to formally adopt a trust statute (1926), the Persons and Companies Act of 1926, Articles. 894-932.
3. For a more thorough comparison of trusts and private foundations, see Alexander A. Bove, Jr., "Should Your Client have a Non-charitable Foundation?" *Trusts & Estates* (November 2009).
4. See, e.g., Cook Islands Foundations Act 2012, Section 24 (3). The duties of the members of the council of a foundation are owed to the council (foundation) itself and not to its beneficiaries.
5. RSA 564-E:6-601(a).
6. *Ibid.*; RSA 564-E:11-1103 et seq.
7. *Ibid.*
8. RSA 564-E:2-201(m).
9. *Ibid.*; RSA 564-E:16-1601 (d)(3).
10. *Ibid.*; RSA 564-E:7-702.
11. RSA 564-E:7-702(b).
12. The beneficiaries of the private foundation can't rely on the rights, powers and entitlements that can be enforced in equity by the beneficiaries of a trust. Paolo Panico, *Private Foundations, Law & Practice*, Section 4.128. Oxford University Press (2014).
13. RSA 564-E:11-1102 (a).
14. *Supra*, note 5.
15. See, e.g., Section 13(1)(e) Trusts (Special Provisions) Act 1989 Bermuda; Al W. King III, "Trusts Without Beneficiaries," *Trusts & Estates* (February 2015).
16. Although the Act allows for the appointment of a protector, there's no requirement that the foundation have one. RSA 564-E:12-1201 (a).
17. RSA 564-E:21.
18. RSA 564-E:21-2105 (b)(2).
19. RSA 564-E:21-2102 (b)(2).