Authors:
Hansjörg Wehrle, LL.M., Member of Executive Board, Allgemeines Treuunternehmen (ATU)
Dr. Ulrich Stertkamp, Head of Tax, Allgemeines Treuunternehmen (ATU)

Why establish a family foundation in Liechtenstein?

This article outlines the advantages of a Liechtenstein family foundation as a tailored asset protection solution for wealthy families and entrepreneurs.

1. A private-law solution offering high flexibility

Since 1926, and thus for 100 years, Liechtenstein has had a very liberal and attractive corporate law system following the introduction of the Law on Persons and Companies (PGR), at the heart of which lies the Liechtenstein foundation.

A (family) foundation in Liechtenstein is established purely under private law, without the need for lengthy discussions and approvals with a government foundation supervisory authority, allowing for a very quick and unbureaucratic setup.

In principle, it is also possible to make subsequent amendments to the articles of association and other foundation documents without legal hurdles, as long as the founder is still alive. Even after the founder's passing, the board of trustees may amend the foundation documents if the situation so requires.

Liechtenstein foundation law is also very flexible regarding the definition of a family foundation's purpose, as long as the foundation serves, directly or indirectly, the welfare and support of the family; in addition, other purposes, such as charitable ones, may also be pursued (in a so-called « mixed foundation », as opposed to a purely private-benefit foundation).

A Liechtenstein foundation may not engage in commercial activities, but it is permitted to hold any form of assets, ranging from securities portfolios, bank accounts, real estate, and equity interests in other companies to works of art, classic cars, and precious metals (gold, etc.). There are generally no requirements regarding the preservation of specific foundation assets, unless the founder has expressly stipulated otherwise.

2. Succession Planning

Furthermore, the structure of the beneficiary provisions in the so-called supplementary statute, which specifies who is to receive distributions from the foundation in the future and under what conditions, is highly flexible. Thus, a family foundation in Liechtenstein is also a highly suitable vehicle for succession planning for wealthy families.

Depending on the complexity of the family situation, it can, under certain circumstances, be very time-consuming and protracted to obtain a certificate of inheritance from the competent probate court in a standard probate proceeding, which is absolutely necessary to gain access to the inherited assets. If at least a portion of the family's assets was transferred to a family foundation prior to the death of the founders, the beneficiaries (who are also heirs) are not required to apply for a certificate of inheritance for that portion of the assets.

3. Protection of Privacy

In Liechtenstein, following the establishment of the foundation under private law, only the articles of incorporation are filed with the Commercial Register; other foundation documents, such as the supplementary bylaws, are not filed. The supplementary bylaws contain the provisions governing the specific beneficiary arrangements, that is, the names of the foundation's specific beneficiaries and the exact conditions under which claims against the foundation may be asserted, ensuring that these provisions remain anonymous and are not accessible to the public. The beneficiary provisions are recorded in the Register of Beneficial Owners (VwbP), but this register is not publicly accessible.

4. Asset Protection Through Separation of Asset Spheres

A foundation in Liechtenstein is an independent legal entity that has no shareholders or partners, only beneficiaries. It is legally self-owned, and this legal independence provides a high degree of asset protection. Two years after the transfer of assets from the founder to the foundation, family members are no longer permitted under Liechtenstein law to assert any claims to a statutory share of the estate, provided that an effective transfer of assets has taken place. Consequently, the assertion and enforcement of legal claims against the founder are only possible within a short time window. Third-party creditors of a founder can generally assert any claims against the founder only for one year, but for no longer than five years.

5. Political and Financial Stability

A little over a hundred years ago (in 1923), the customs treaty between Liechtenstein and Switzerland was signed, through which Liechtenstein was incorporated into the Swiss customs territory. Looking back, Liechtenstein has undergone fundamental changes during this period. While it was still a comparatively poor agrarian state in 1923, the small principality is now one of the world's most prosperous economies. It is also one of the few countries in the world with no public debt and holds an AAA+ credit rating.

Politically, it is very stable thanks to its unique legal structure as a constitutional principality, in which political decision-making power is shared between a democratically elected Landtag and the Princely House.

Furthermore, Liechtenstein has been a member of the EEA since 1992, thereby ensuring access to the EU market, which is particularly important for Liechtenstein's strong industrial sector. Additionally, Liechtenstein's membership in the EEA allows for legal structures that would not be possible in a third country such as Switzerland.

6. Tax Advantages

Liechtenstein is also attractive as a foundation location from a tax perspective. A normally taxed foundation is subject to an income tax rate of only 12.5 %, and there are no additional business taxes or similar levies as in other countries, e.g., Germany.

Due to a very generous exemption rule, dividends received and gains from the sale of equity interests in corporations are 100 % tax-exempt at the foundation level, and distributions to beneficiaries are not subject to withholding tax.

Assuming that the foundation's income from capital assets is fully retained and not distributed to beneficiaries, this income is therefore not subject to income tax at the level of the founder or the beneficiaries. (In contrast to the situation where the securities are held directly by a private individual and the resulting income from capital assets is generally subject to taxation.) Calculated over a longer period, this tax shield effect of a Liechtenstein foundation offers a significant economic advantage.

This is based on the assumption that the (discretionary) foundation in Liechtenstein is considered non-transparent for tax purposes (see the last paragraph for more on this). A foundation with its registered office and place of administration in Liechtenstein is also not subject to any substitute inheritance tax, as is the case in Germany, for example, or to an anniversary tax, as in the UK.

7. Attractive Investment Fund Hub

Last but not least, Liechtenstein has also become a very attractive fund location in Europe, thanks to an EU-compliant regulatory framework that also applies to alternative investment funds (AIFs).

The focus here is on so-called « private label funds, » which are individually structured and managed to meet the needs of specific clients (e.g., trustees, family offices, banks, asset managers) and in which the investor enjoys full investor protection. The client has a say in the investment policy and is also free to choose the fund's name, as well as, for example, serve on the fund's board of directors. The tasks are subsequently carried out by licensed and regulated service providers.

These private-label funds can be easily combined with family foundations as needed.

8. Tax Challenges: The Case of a Founder from Germany

In conclusion, while the advantages of a family foundation in Liechtenstein listed above are significant, it should not be overlooked that certain hurdles must be considered from a German tax perspective.

The most significant hurdle, as stipulated by the German Foreign Tax Act, is that the foreign foundation must not be legally «controlled» by beneficiaries or founders residing in Germany (the law refers to legal « power of disposal »). Otherwise, the foreign foundation would be treated as fiscally transparent, and the foundation's assets would be directly attributed for tax purposes to the beneficiaries residing in Germany.

Typically, however, foundations in Liechtenstein are managed by external board members, not by family members, and under the PGR, it is also mandatory that at least one member of the board of trustees be a resident or have a place of business in Liechtenstein and be authorized to act in this capacity. Thus, foundations in

Liechtenstein established for German families can easily be structured as non-transparent for German tax purposes.

It should be noted here that the provisions of the Foreign Tax Act may be amended in the near future, as a draft bill from the Federal Ministry of Finance is currently under consideration. According to this draft, there will continue to be no doubt regarding the tax recognition of a foreign foundation in the future, provided it does not constitute an « artificial arrangement. » What this specifically entails cannot be deduced from this draft bill, but we currently assume that a "normal" family foundation established for asset protection purposes should not fall under this category. The benchmark in this regard should be a comparison with a normal family foundation in Germany.

If the German founder wishes to appoint a so-called « protector » (advisory board) to exercise supervisory and control functions in order to maintain a certain degree of indirect control over the activities of the foundation's board of directors, our experience indicates that this is tax-neutral for German tax purposes, as long as this additional body has no authority to issue instructions to the foundation's board of trustees.

In addition, German gift tax law imposes certain obstacles on the transfer of assets to a family foundation in Liechtenstein; however, these can be overcome with appropriate advice from an experienced German tax attorney or tax advisor, for example, by transferring tax-privileged business assets or by utilizing a right of usufruct, which reduces the value of the transfer.

However, due to the complexity of German tax law, these issues must be clarified with an experienced tax advisor in Germany before establishing the foundation or transferring assets to it.

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ulrich.stertkamp@atu.li
hansjoerg.wehrle@atu.li
www.atu.li