

New horizons

Todd D Mayo introduces the *New Hampshire Foundation Act*

New Hampshire is poised to become the first US state to allow the establishment of foundations. Earlier in 2017, the state introduced a bill (SB 225) that includes the *New Hampshire Foundation Act* (the Act). If enacted, the Act would enable families for whom a foundation is preferable to a trust as a wealth management device to avail themselves of a US-based structure.

The Act marries elements of the *New Hampshire Trust Code* and the state's company laws. It draws on the trust laws for the purpose of defining the rights and duties of the founders, beneficiaries, directors and protectors, and the processes for modifying or reforming a foundation's certificate of formation and by-laws. The Act draws on the company laws for the procedural rules governing the establishment, registration, domestication and dissolution of a foundation.

ESTABLISHMENT OF A FOUNDATION

Under the Act, an organiser establishes a foundation by filing a certificate of formation with the New Hampshire Secretary of State. The organiser may be a founder or any other person. The certificate of formation must include the foundation's name, the name of the foundation's initial registered agent and the address of the foundation's initial registered office. The certificate of formation may include other information, such as the foundation's purposes.

After a foundation's formation, the founder or initial directors must adopt by-laws. These by-laws must include the foundation's purposes, and generally would contain all other substantive provisions concerning the powers, duties, rights and interests of the founder, beneficiaries, directors and protectors. For example, dispositive provisions governing the

distribution of foundation property to the beneficiaries or in furtherance of the foundation's purposes would generally be included.

The certificate of formation or by-laws may contain a no-contest provision (i.e. a forfeiture provision) or a provision requiring the nonjudicial resolution of disputes among the founders, beneficiaries, directors and protectors. Both types of provision are expressly enforceable under the Act.

FOUNDERS

Under the Act, a founder is a person who contributes money or other property to a foundation. There is no minimum amount that must be contributed. If more than one person contributes property to a foundation, then each person generally is a founder to the extent of their contribution.

Under the foundation's certificate of formation or by-laws, the founder may reserve any rights, powers and interest in a foundation. For example, the founder may reserve the power to appoint and remove a director or protector, direct distributions, or dissolve the foundation. By default, a founder has the power to amend the foundation's certificate of formation, amend or revoke the by-laws, direct the directors to make distributions, and dissolve the foundation. The certificate of formation or the by-laws may modify or waive those powers.

PURPOSES AND BENEFICIARIES

A foundation must have one or more purposes. Each purpose must be lawful, not contrary to public policy and possible to achieve. The purposes may be charitable or non-charitable. A foundation's purpose may be the management of the foundation's property for the benefit of one or more beneficiaries. The certificate of formation or the by-laws may grant to a beneficiary any

➤ KEY POINTS

WHAT IS THE ISSUE?

New Hampshire has introduced legislation in bill form allowing the establishment and domestication of foundations. It would be the first US state to do so.

WHAT DOES IT MEAN FOR ME?

When advising families for whom foundations make sense, practitioners may soon be able to include a US-*situs* foundation in those families' wealth structures.

WHAT CAN I TAKE AWAY?

The *New Hampshire Foundation Act* would provide flexibility in designing a foundation and defining the powers, duties and rights of the founders, beneficiaries, directors and protectors. A New Hampshire foundation generally should qualify as a trust for US tax purposes.

rights, powers and interests. By default, a beneficiary does not have any property right in a foundation or its property.

DIRECTORS AND PROTECTORS

A foundation's board of directors is vested with the power to manage the foundation and its affairs. An individual or an entity may serve as a director. A foundation may have one or more classes of directors, whose qualifications, powers and duties would be defined in the foundation's certificate of formation or, more likely, its by-laws.

In addition to its board of directors, a foundation may have one or more protectors. The foundation's certificate of formation or by-laws would define a protector's powers and duties. A protector's powers generally include the power to commence a judicial proceeding to protect the foundation or enforce the foundation's certificate of formation and by-laws.

An individual or an entity may serve as a protector, and a foundation may have one or more classes of protectors.

The Act does not impose any citizenship or residency requirement on directors or protectors; thus, a director or protector is not required to be a US citizen or a New Hampshire resident.

PRIVATE TRUST COMPANY

A foundation may be organised as a private trust company. Under the New Hampshire *Family Trust Company Act*, a private trust company may provide trust, investment and related services to a single family. A foundation may be well suited to serve as a private trust company, because it does not have any shareholders, and thus can fully encapsulate its own governance structure.

REGISTRATION AND DOMESTICATION OF FOUNDATIONS

The Act permits the registration or domestication of a foundation established

under the laws of a jurisdiction other than New Hampshire. A non-New Hampshire foundation may register by filing a certificate of registration with the Secretary of State and should register before engaging in any significant transactions in the state, such as buying or leasing real property, and before commencing any judicial proceeding in the state.

A non-New Hampshire foundation may domesticate into New Hampshire by filing a certificate of domestication with the Secretary of State. By domesticating into New Hampshire, a foundation continues its legal existence, but will be treated as a New Hampshire foundation going forward. Domestication does not require any transfer of the foundation's assets, and does not affect the foundation's debts and other liabilities.

TAXATION

A foundation formed under the Act would likely be classified as a trust for US tax purposes, whereby a foundation's classification is determined on a case-by-case basis. Under the Treasury Regulations,¹ 'trust' generally means 'an arrangement created by... an *inter vivos* declaration whereby trustees take title to property for the purpose of protecting or conserving it for the beneficiaries under the ordinary rules applied in chancery or probate courts'.

The regulations further provide that: '[A]n arrangement will be treated as a trust under the *Internal Revenue Code* if it can be shown that the purpose of the arrangement is to vest in trustees responsibility for the protection and conservation of property for beneficiaries who cannot share in the discharge of this responsibility and, therefore, are not associates in a joint enterprise for the conduct of business for profit.'

Under the Act, the rights, powers and duties of a foundation's directors and beneficiaries mirror the rights, powers, and duties of a trust's trustees and beneficiaries. Like a trustee of a trust, a director has a non-waivable duty to manage the foundation and its property in good faith, in accordance with the terms of the governing documents and the Act, and has the duties of loyalty, impartiality and prudent management.

Importantly, the probate court has exclusive jurisdiction over a foundation's internal affairs, including any claim by a beneficiary against a director or protector for a breach of a duty. Thus, a foundation formed under the Act generally should qualify as a trust for US tax purposes.

For New Hampshire tax purposes, a foundation will be taxable in the same manner as a trust and thus ordinarily will be exempt from tax. A foundation, however, may be taxable if it is organised or operates as a commercial enterprise (e.g. having transferable interests that are functionally equivalent to company shares or directly engaging in commercial activities).

CONCLUSION

New Hampshire may soon become the first US state to allow the establishment and domestication of foundations. The Act, which seems likely to be enacted, would be effective from 1 October 2017. With the enactment, New Hampshire would enable families to include a foundation in a US-*situs* wealth structure.

¹ s301.7701-4(a)



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