Estate planning on the edges of time: *The Czech Perspective*

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Abstract

Over the past few years, fundamental changes have been adopted in Czech private law, modifying both its conceptual framework and its content. The innovations also include the introduction of some new legal instruments for estate planning. However, the optimistic expectations concerning the applicability of such instruments clash not only with the imperfections of the legal regulation, but also with the distrust towards instruments for the administration of property that are currently being jeopardized by global pressures aimed at achieving maximum transparency of such structures. Consequently, shortly after its introduction, the concept of estate planning has had to fight for its legitimacy and thus, essentially, for its very survival.

Introduction

After the emergence of the Czechoslovak totalitarian socialist regime in 1948, almost all private property of any value was nationalized, including the property of existing foundations that was confiscated. In 1953, the extensive expropriation was accompanied by a currency reform, resulting in the devaluation of financial savings. As a result, all family property that had previously been handed over from generation to generation became essentially reduced to personal items and the humble furnishings of small apartments. Combined with a ban on entrepreneurial activities, those actions resulted in the creation of a relatively poor society that was only minimally socially diverse. The egalitarian nature of the society was exceptional also in comparison with other countries of the former Central and Eastern Europe.

The efforts by the then socialist state, aimed at the elimination of private property, were also reflected in the legal reforms of the 1950s and 1960s. As a result, many traditional institutes of private property law were cancelled or extensively limited, including those that may have well been used in the area of *estate planning* (*inter vivos*/*mortis causa*), like eg inheritance contract, bequests, or foundations.

At the time of the fall of the socialist regime at the end of 1989, there were essentially no standard tools available in the Czech society for the purpose of intergenerational management of property. At the same time, there were hardly any people actually in need of such instruments.

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Although Czech private law has been subject to several waves of amendments over the past 25 years, with the changes reflecting the new social situation, the area of instruments regulating estate planning was

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beyond any interest for a long time. The situation started to change only in the past few years, after sufficient capital had been created after more than 20 years of free market economy in the Czech Republic. This refers mostly to the property of those who started their business as middle-aged entrepreneurs in the 1990s and have now reached retirement age. The new Czech Civil Code No 89/2012 Coll., effective from 1 January 2014, meets this demand by the introduction of the possibility to establish foundations now also for private purposes, and has also brought a new form for the administration of property—the trust fund.

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However, the optimistic expectations concerning the applicability of these legal instruments clash with not only the imperfections of the legal regulation but also with the distrust towards instruments for the administration of property, that are currently being jeopardized by the global pressure for maximum transparency of such structures.

The aim of this article is to point out some crucial issues that, while currently being dealt with in Czech law, appear to be much more than just 'local'. Thus, they are significant from the point of view of international comparison.

Registries and registries . . .

The present era is characterized by the 'public authorities' love of registries', which are intended as adequate responses to, among others, fears of terrorism, corruption, and tax offences. There is an evident effort to ensure that all legal structures for property administration are registered in central registries that are accessible to—at least—public bodies. This requirement also applies to trusts.

The suggestion that relevant authorities should have quick access to current and exact data on express trusts has been periodically voiced since 2003 by the Financial Action Task Force on Money Laundering (FATF) in their recommendations to fight money laundering.[2] Thus, in many European countries public registries of licenced professional trust administrators (eg Malta, Cyprus) or even trusts (San Marino, Hungary) are maintained. In France, trust administrators are obliged to register the fiducie,[3] not later than one month after the formation of a trust agreement (with the tax authority).[4] In addition, in 2010, France established *Registre national des fiducies*.[5]

In the Czech Republic, the amendment of the trust fund legislation was passed at the end of 2016.[6] According to the amendment, the trust fund *inter vivos* (one arising during the life of the settlor) no longer comes into existence on the basis of an agreement, but upon the entry into the registry of trust funds.

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1. For more details, see K Ronovská, 'Svěřenský Fond (Trust fund): A Daring New Legal Transplant in Czech Republic' in S Farran and others (eds), *The Diffusion of Law* (Ashgate 2015) 203ff.
2. FATF 40 Recommendations of 2003, bod 34, FATF 40 Recommendation (2012), sub 25.
3. F Barrière, 'The French fiducie, or the Chaotic Awakening of a Sleeping Beauty' in L Smith (ed), *Re-imagining the Trust: Trusts in Civil Law* (CUP 2012) 222ff.
4. If they fail to do so, a trust agreement is considered invalid, see Article 2019 of the French Civil Code.
5. Décret no 2010-219 du 2 mars 2010.
6. Amendment of Czech Civil Code (Act no 460/2016 Coll), effective from 1 January 2018

From a functional point of view, Czech trust funds come into existence in a similar manner as foundations and foundation funds. This essentially erases the difference between the trust structure and a legal person and, as a result, restricts the functional applicability of trust structures as a mere alternative to foundation-like forms of legal persons. To a considerable degree, this negates the reason why these instruments were introduced in the Czech (continental) legal system. After all, there are only few arguments left for why the same function should not be performed by traditional legal persons. That stimulates attempts aimed at pushing them out of the legal system again since they are seen as 'alien' and essentially redundant elements.

The fourth anti-money laundering directive[7] directly requires the European Union (EU) Member States to establish central registries for the beneficial owners of all legal entities and trusts, as long as they generate tax consequences. From the point of view of foundation structures, the concept of the 'beneficial owner' raises many questions. A 'beneficial' owner is considered to be anybody who ultimately controls an asset and can benefit from it.[8] These two aspects are, however, principally separated in the case of foundations and trusts. Their beneficiaries are typically not in control of the administration of the foundation or trust.

The new legal regulation in the Czech Republic has taken the implication of these considerations to quite an absurd end: As a pre-condition for the creation of the right of the beneficiary of a trust fund to claim performance, it requires its prior entry into a registry of trust funds.

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The more public, the better?

The most burning issue facing the structures of estate planning (not only in the Czech Republic) is likely to be the attempt to make it public the data about beneficiaries and the conditions under which the structures operate.

Foundation and trust structures established for private purposes (unlike those established for public benefit purposes) are primarily tools for property administration and only have a very limited impact upon the 'public'. While the arrangement typically reflects the family situation of the settlor and the settlor's relatives, the benefit itself however constitutes the main source of the beneficiaries' income assets. Making this information public thus represents a major interference with the privacy of all persons involved, which stands in a particularly stark contrast when compared to essentially non-public probate proceedings.

The impact of the '(lack of) trustworthiness' may also be documented with the example of the Czech private foundation fund. Although it had seemed that this 'lighter' (special) type of foundation would become a more useful and comprehensible institute in the Czech legal environment than the unusual conception of the trust fund, potential founders still prefer trust funds, precisely because of the inadequate protection of privacy when setting up a private foundation fund. The main reason is the excessive transparency (publically accessible collection of deeds in the foundation registry), thanks to which anybody can access the statutes and other related documents revealing a large set of data about the operation of foundations and foundation funds.

7. Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.

8. E van der Does de Willebois and others, *The Puppet Masters: How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do about It* (Stolen Asset Recovery Initiative 2011) 18.

As a result, during the first three years of effect of the new Civil Code, no (or just very few) foundation funds were established for estate planning purposes. Settlors are not interested in having the conditions for the operation of such schemes made publically available, including the conditions for the payment of benefits and the range of beneficiaries. In some cases, they are afraid to let others 'see' into the complexity of family situations, in other cases they may fear the personal safety of beneficiaries or their children, who could easily become targets of criminal acts inspired by (sometimes incorrect) assumptions about their property situation.

The reasons given for the attempts to make the information about estate planning structures public include the interest to prevent corruption, terrorism, and tax offences. However, foundations and trusts are used for such goals very rarely.[9] It may be doubted that their publication will lead to a major breakthrough in fighting these phenomena.

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Quite on the contrary: such attempts *de facto* lead to the impossibility of an effective utilization of legitimate arrangements for the administration of property and its passage from one generation to another. Moreover, they create the impression that the mere existence of such structures constitutes—regardless of anything else—a social risk. That, inevitably, undermines their legitimacy.

A positive development in this respect can be seen in France. In October 2016, the French Constitutional Court[10] upheld the protection of privacy and cancelled a legal regulation enabling unlimited access to data kept in the *Registre national des fiducies*. The Constitutional Court held that the register imposes a disproportionate infringement of the right to privacy compared to the constitutional aim of the fight against tax fraud and evasion.

Czech lawmakers had also been toying (for some time) with the idea of making the registry of trust funds publically accessible to the full extent. However, at a later stage in the legislative process, it was eventually decided that the access to the data should be given only to a limited number of public authorities, financial institutions, and persons demonstrating special legal interest. However, it remains unknown why a similar approach was not adopted also with respect to private foundations.

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What next?

The debate about the optimal extent of record-keeping and the suitability of public access to data about the structure of property administration will continue in the Czech Republic. It will be necessary to deal with a number of issues: the role of the trust-like instrument of the trust fund, the extent of suitable arbitration between the individual forms of foundation structures, the optimal access to the protection of sensitive information, etc.

9. cf eg J D'Souza, *Terrorist Financing, Money Laundering, and Tax Evasion. Examining the Performance of Financial Intelligence Units* (CRC Press 2012) s 27ff.; T Bennett, *Money Laundering Compliance* (Bloomsbury 2014) 126.

10. Décision no 2016-591 QPC du 21 October 2016.

It is necessary to search for a sober and rational approach to various initiatives that eventually result in the de-legitimization of the instruments of *estate planning*. If such instruments cease to be trustworthy, people will turn away from them, reorienting themselves towards alternative foreign structures, if available, or revert to various contractual constructions that will be difficult to identify easily and, consequently, difficult to regulate. Ultimately, this will be to the detriment of everybody—the state will have a lower degree of control and the people will enjoy a reduced degree of legal certainty.

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