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NEWSLETTER SLOVAKIA

SETTING FOUNDATIONS

Issue:
June 2023

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Private foundations as the future of family wealth

Private foundations and trust funds are a well-known instrument abroad for the management of family assets. Parliament has already received a draft amendment to Act No 34/2002 Coll. on Foundations, which should introduce a new institution of private foundations.

The private foundation should be an independent administrative entity whose purpose will be mainly the administration of family assets, which will be particularly practical for the business class who want to prevent disputes and disagreements that could arise after the arrival of the next generation in the family company (e.g. by inheritance by operation of law). It is actually a relatively simple method of ensuring the transfer of assets from one generation to the next within the family or close persons designated by the founder of the private foundation. A private foundation becomes the owner of the contributed assets. The founder of the private foundation will no longer own the assets, but will have control over the operation of the private foundation. The assets of a private foundation may consist of movable property, real estate, but also business shares, stock and other forms of property. The assets owned by the foundation may be disposed of in accordance with the purpose of the private foundation, the statutes of the private foundation and in accordance with good morals. It is therefore up to the founder of the private foundation to decide how to set the relevant rules of the private foundation and thus which range of persons and under what conditions the private foundation will support.

From a legislative point of view, although private foundations will be regulated in the Foundations Act, which also regulates public benefit foundations, it is necessary to make a fundamental distinction between the two. Public benefit foundations are organisations that have been known in the Slovak Republic for years and generally collect financial contributions from the public for charitable purposes such as helping homeless children, helping abused women, single mothers, severely disabled citizens, etc. The main feature of public benefit foundations is that they aim at public benefit, they serve selected individuals who belong to some disadvantaged group of the population and basically anyone can contribute to such a foundation. Private foundations will serve only families or persons designated by the founder of the private

foundation, will not be open to public contributions, and are explicitly designed to provide for their own needs or the needs of other persons designated by the founder. Private foundations should also not be entitled to draw 2 per cent of taxes or to organise public collections.

The procedure for establishing a private foundation will be a relatively simple process, as it should be established by a foundation deed in the form of a notarial record and can be established by any natural person having legal capacity. The form of the notarial record will guarantee the uniformity and clarity of foundation deeds. A private foundation shall be established by registration in the relevant register of non-governmental non-profit organisations. In addition to the foundation deed, when establishing a private foundation, the notary public should directly on the spot carry out the identification of the beneficial owners and draw up a verification document, which should be without prejudice to the provisions of Act No. 315/2016 Coll. on the Register of Public Sector Partners, as amended (hereinafter referred to as the Act on RPSP). Any person to whom a benefit is provided by the private foundation, regardless of the size/amount of the benefit provided, will be considered as the beneficial owner. At the same time, private foundations will also be registered with the RPSP, but information on the foundation will not be publicly available. Pursuant to Act No 297/2008 Coll. on protection against money laundering as amended (hereinafter referred to as the AML Act), the trustee will be an obliged person and thus the bill also deals with the issue of AML obligations.

On the tax issue, the bill is set up so that contributions to a private foundation will not be subject to taxation. However, the income of the private foundation will be subject to income tax. The income from the private foundation's benefit in relation to the beneficiaries will be subject to withholding tax for the respective beneficiary.

Similar institutes to the proposed legal form of a private foundation exist in our neighbouring countries, namely in the Czech Republic and Austria. It should also be mentioned that trust funds are also used abroad to manage assets. In the case of trust funds, this is a set of assets without legal personality, i.e. a fundamentally different institute from a private foundation, which will be a legal person, i.e. it will

have legal personality. In our circumstances, unlike a trust fund, the institution of a private foundation appears to be more appropriate and easier to grasp legally.

The bill is due to be debated in Parliament during June 2023 and is already facing a wave of criticism. We will keep an eye on how the legislator deals with the proposal of this rather progressive novelty in the Slovak legislation.

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→ Business

Reporting information on corporate sustainability

We would like to bring you news on the increasingly discussed topic of corporate sustainability (ESG - Environmental, Social, Governance). As the abbreviation already implies, this topic should be seen in a broader context, however, not only in relation to negative global environmental developments. It is also about setting rules in the area of social relations of companies, both internal and external (e.g. social inclusion, diversity, adequacy of the working environment, child labour) and setting the culture of corporate governance (e.g. ethics in business, anti-corruption behaviour).



On 28 November 2022, the Council of the European Union adopted the Corporate Sustainability Reporting Directive (CSRD). This Directive replaces the current Non-Financial Reporting Directive (NFRD), which is transposed into the Slovak Accounting Act (Sec. 20 (9) - reporting requirements in the annual report). Currently, the original Directive only applies to public interest entities whose average recalculated number of employees for the accounting period exceeded 500 employees. Such companies are presently required to include in the annual report also non-financial information on the development, conduct, position and environmental, social and labour impact (ESG) of the entity's activities, information on respect for human rights and information on the fight against corruption and bribery.

The European Union's Directive on the Reporting of Corporate Sustainability Information imposes more extensive reporting requirements on information related to sustainability elements, which are further defined by a strategy based on:

- E for environment,

- S for social and human rights,
- G for governance.

The implementation of the requirements of the Directive will be applied progressively in the following steps:

1. in 2025 for 2024 - to companies currently covered by the Non-Financial Disclosure Directive (i.e. public interest entities with more than 500 employees),
2. in 2026 for the year 2025 - to large enterprises that meet 2 of the following 3 criteria: assets of more than EUR 20 million, turnover of more than EUR 40 million, average number of employees of more than 250,
3. in 2027 for the year 2026 - for listed small and medium-sized enterprises, excluding micro-enterprises, small and less complex credit institutions and captive insurance and reinsurance companies,
4. in 2029 for the year 2028 - to third country enterprises with substantial activities in the European Union market (which have achieved a turnover in the European Union market of more than EUR 150 million in the last 2 years on a consolidated basis) and which will have at least one subsidiary (large or listed) or branch (with a turnover in the last year of more than EUR 40 million) in the European Union.

An exemption will apply to subsidiaries included in the consolidated financial statements and consolidated annual report of the parent company (except for a listed subsidiary that meets the criteria of a large company). Nevertheless, the new legislation is likely to affect also companies, which are subject to exemption, e.g. on the basis of uniformly set rules for parent company compliance with ESG rules and for reporting information to the parent company for inclusion in the consolidated financial statements.

Companies will report in their sustainability reports information on their strategies and business models, value chain, governance and organisation, risks, as well as information on targets, action plans and performance.

As the Directive on the Reporting of Corporate Sustainability Information has not yet been transposed into Slovak legislation, no detailed reporting requirements for the required information are known at this point in time.

The required sustainability information will be subject to verification by an auditor or other

assurance provider (as decided by the individual EU Member States).

However, the new legislation will not just be about reporting. While reporting itself will likely require additional resources to collect and present the information, a much greater impact is expected in terms of modifying existing processes.

We will keep you informed of further developments in the future.

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