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German Foundations - Essentials and Activities

Report to the Annual General Meeting
of the Union of Bulgarian Foundations

Sofia, 24 March 1993

I am very grateful for the opportunity to address the Union of Bulgarian Foundations. Since 1986 I have on several occasions met with representatives of one of your members, the St. Cyril and Methodius Foundation, and it was only two weeks ago that three of their staff members spent five days in Hannover studying the operations of the Volkswagen Foundation.

In Germany it is estimated that there are more than 7000 Foundations, by far the majority in western Germany. We have a national association of foundations and I am at present a member of its board. The oldest member foundation of the association was founded in 917, and it has been operating ever since. This supports my favourite remark that foundations are established for eternity. But what is it that makes a foundation function and last eternally?

My answer will be based on the German legal situation and on my own experience as Chief Executive Officer of the Volkswagen Foundation and member of the governing boards of some other Foundations. The legal institution of foundation in Germany is codified in the Civil Law Code of 1896 and in special foundation laws enacted by the German states in the post World War II period.

To establish a foundation requires a written act determining the purpose of the foundation, the endowment and the statutes including the name of the foundation and the composition of the governing board plus its duties and rights. To become legally existent as a legal person the act of foundation needs to be approved by a State authority as determined in the respective State foundation law. With the approval the founder loses his right to cancel or alter the act of foundation including the foundation's statutes; the new foundation can request payment of the endowment.

Approval of the act of foundation must be declined, if the essentials as mentioned above have not been fulfilled or if the purpose of the new foundation would be illegal or the endowment insufficient to fulfil the purpose.

As a legal person the new foundation is autonomous under the government of its governing board. It is subject to state supervision, which is restricted to a control of the legality of the foundation's administrative activities. In order to enable the respective State authority to exercise supervision all foundations are obliged by law to file an annual report, a statement of account and a declaration of property.

If the foundation's purpose and actual management is charitable, the foundation is granted tax exemption. This is controlled by the revenue authorities and regulated in the tax laws.

It will appear obvious that the mere legal provisions do not by themselves guarantee the lasting independence and stability of a foundation. What else has then to be observed?

The purpose of the foundation should be defined both clearly and in sufficiently general terms to make changes unnecessary. In the case of the Volkswagen Foundation the purpose was stated as "promotion of science and technology in research and university teaching".

The size of the endowment should correspond to the purpose of the foundation so that foreseeably the purpose can be fulfilled through the income drawn from the invested endowment. Legal provision should be made to add to the foundation's endowment from the annual income to a degree that will balance the loss of purchasing value caused by inflation. It is also advantageous to allow foundations to change their investments cautiously in order to optimize - not necessarily maximize - the foundation's income.

The composition of the governing board and the rules for it deserve utmost attention. This is especially the case, when foundations are established by public institutions or large enterprises including banks. I shall describe the rules effective in the Volkswagen Foundation, because I feel that they are good and useful: The Foundation was established in 1961 by the Federal Republic of Germany and the State of Lower Saxony as part of the policy to privatize publicly owned corporations. The Foundation's endowment was made up of the proceeds of the sale of shares of the Volkswagen Corporation to the public plus all titles to the gains on Volkswagen shares retained by the founders.

The right to appoint members of the governing board rests with the two founders. Each founder appoints one half of the members, the size of the Board is fourteen. The term of office is five years and may be prolonged for a second term only once. Thanks to a special arrangement at the start of the foundation, the terms of office overlap. The Board itself has no share in the appointment of new members. There are no ex officio members on the Board. No Board member may be withdrawn during the term of office. Board members cannot be requested to act in a certain way by the appointing founder. The limitation of the number of reappointments to one brings about an automatic change and thus helps avoid an undue dominance by long-standing Board members. It has also saved the Foundation of the commonly known problem of Board members becoming too old.

The quorum for meetings has been set at eight members, while decisions require a two thirds majority of the members present, decisions on amendments of the statutes a majority of two thirds of the members of the Board. Absentees may authorize another member to vote on their behalf. Non-member substitutes are not admitted.

With the Volkswagen Foundation there is an intricate system of division of functions, which safeguards the Foundation's independence and protects it from any abuse of power. This system has worked well for the 31 years of the Foundation's existence and may serve as a pattern for other sizeable foundations. It is the Board that selects and employs the chief

executive officer, the Secretary General, decides on the budget, approves of the annual accounts and decides on the grant policy and all grant proposals exceeding a certain value level. The Secretary General is responsible for the functioning of the Foundation including asset management and processing of grant proposals. He prepares the Board meetings, which means that any proposal for decision going to the Board needs his approval; all items on the Board's agenda are prepared in writing. The Secretary General selects and employs the Foundation's staff. While he reports to the Board, the staff report to him. Through a set of internal rules executive and supervisory functions have been separated. External expertise is being used through a system of peer review for all grant proposals and through a consultative committee for investment policy and investment results. This committee is composed of three high ranking external experts plus one member of the Board. The external members are appointed by the Board for a three years' term of office with the possibility of one reappointment. The entire financial operation of the Foundation is audited by a chartered auditor. The Board upon the suggestion of the Secretary General recently decided to change the auditor every ten years to assure a high level of critique.

On the grant giving side it is important to know that with the Volkswagen Foundation a single grant may not exceed five years. This means that the Foundation cannot engage in long-term financial responsibilities. The Foundation requests of a grantee brief annual reports on the progress of work, it pays out grant money in instalments meeting as a rule a three months' demand. At the latest after the completion of a project the Foundation collects a detailed financial statement plus a report. The Foundation expects of every grantee to publish his results in a monograph or in a reviewed journal. The reaction of the scientific community to such a publication is observed by the Foundation as the most effective way of evaluating projects. If a former grantee files another proposal, the results of the former project will be made available to the peers in the review process of the new proposal.

Foundations, at least large foundations, should act transparently. This means that they should publish annually or bi-annually their policy and their activities plus their financial status. This is helpful, if a foundation reacts to requests, because it widens attention for the foundation on the part of individuals or institutions, at whose support the foundations is aiming. Published reports also help foster a foundation-mindedness in society and they reduce distrust in foundations' activities. In a certain sense this is "the reverse side of the medal" of tax-exemption. The Volkswagen Foundation has published annual reports since its first year of activity. To serve its international interests it proceeded to publish condensed versions in English.

I am fully aware of the fact that the Volkswagen Foundation by its mere size does not easily lend itself to comparisons with other foundations. Yet the essentials, which I meant, are essentials for any foundation enjoying autonomy and act-

ing responsibly. A foundation needs a system of checks and balances, which means attributable responsibilities. It needs rationality and professionalism, and it needs impartiality. And these qualities are no functions of size. So much about essentials. I shall now turn towards the activities of German foundations.

At the end of 1991 for the first time in the history of German foundations a handbook of foundations was published by our national association. For this handbook roughly 6000 foundations had been sent questionnaires and almost 5000 were included in the handbook. Roughly one half of this number of foundations were established after 1950. Amazingly enough 185 were founded before the year 1500. It is interesting to look at the purpose for which the foundations were established. Many foundations serve various purposes. A table in the handbook discloses that the majority of foundations are dedicated to social welfare, namely 33,8%. The second largest group of 21% is listed under education, professional training, adult education. 11,1% focus on research and academic education, 9,5% on the arts and culture in general.

With regard to the size of the endowments I believe one might guess that the total sum of endowments is near 20 billion German Marks. The endowments of the 10 biggest foundations constitute around 10 billion Marks. There are no reliable figures beyond these very rough guesses, because rather little research has been conducted so far of the foundation scene. That is the reason why we also lack reliable information on how many foundations are operational and how many grant-giving.

I suppose that the majority of foundations operate locally or in rather small regions. It is usually only the very big foundations that work on a national or even an international scale.

I shall abstain from describing in detail what the Volkswagen Foundation does, because it is so big that it is most likely no practical example for Bulgarian foundations. I suppose that many of the foundations, which are members of your union, find it difficult to accumulate an endowment and for very practical reasons work on a limited geographical basis. But that then is also true of the majority of the German foundations. To establish a foundation requires some wealth. There is however one exceptional chance even in countries like Bulgaria that is the phase of privatization. I understand that Bulgaria is following a policy of privatization. If the political parties could be persuaded to follow the pattern of the Volkswagen Foundation, they would then vote in favour of endowing foundations with the proceeds of privatization. The existence of many foundations serving purposes on behalf of public well-being makes a society far more flexible than those relying entirely on the State for activities. In Germany like in many other countries you would find many institutions, which owe their existence to foundations. This is true of many hospitals, homes for the aged, schools, museums, theatres, sports grounds. It is not so much the

total amount of annual expenditure that is the most amazing aspect of foundations; it is rather their strength of vision of future needs, the diversity of their purposes, their ability to respond quickly to needs and demands, which constitute the value of foundations. I take it that you have by now learned to talk of a civil society. Foundations are a constituent element of a civil society, because they mean citizen participation and decentralized, individualized responsibilities.

I suppose that many of you are full of expectation with regard to an international cooperation of foundations. Let me pour some water into this wine - to use a German proverb. Even in wealthy countries there are relatively few foundations, which are authorized through their statutes and the national legal provisions for foundations to operate internationally. The Volkswagen Foundation is one such example. We do engage considerably in international grants, but for very practical reasons we prefer not to enter joint funding. We rather finance a project entirely ourselves or stay out of it. The main practical reason is that it is difficult enough to assess the quality of a project before making a grant and that this is even^{more} complicated if a foundation also has to adjust to the policies and the granting conditions of other foundations. This does not mean that international grant making is not based on cooperation. To give you an example: Yesterday I had the pleasure of opening an exhibition of books and library equipment in the library of the Bulgarian Academy of Sciences, which were procured with the help of the Volkswagen Foundation. To select the books to be procured the Volkswagen Foundation invited proposals from Bulgaria and did not itself select a single book. For another example: We have a programme to support cooperative research projects between East European and German research institutes. Here we leave it to the partners of cooperation to determine the objective of their research and to define their financial demands. We do however consult external peers to appraise the proposals, before we accept them or turn them down.

There is another aspect of international cooperation and that is the provision of information on how a foundation functions. That is, what we just did with the St. Cyril and Methodius Foundation. I am quite sure that many western foundations would be equally willing to let new foundations in Eastern Europe look into their cards. In the Volkswagen Foundation we have received and continue to receive many delegations and visitors from other countries and even other German foundations and explain to them our operations. Much of this can be seen by merely reading our annual reports and printed material^{which}, we put out and distribute very generously upon request.

I should like to stop here and leave the rest of the time to questions and comments. I should like to emphasize how happy I am that the political changes of 1989/1990 have made

it possible for representatives of western foundations to participate in an annual general meeting of a Union of Bulgarian Foundations. This is, I feel, an enormous step forward and I wish you many more steps in this direction.