

20 Principles of Good Practice

Governance

- (1) **Foundations maintain decision-making bodies which act in compliance with the foundation statutes and applicable law. Such bodies perceive their mission as custodians of the funder's will and the foundation's assets laid down in the deed of foundation and the statutes.**

Explanatory notes: This "Compliance Rule" constitutes the shared self-conception of all German foundations and it is the guiding principle of good and successful foundation practice. As a rule, a foundation's governing bodies comprise a decision-making body (e.g. Board of Trustees) and a supervisory body (e.g. Board of Trustees or Foundation Board).

The Volkswagen Foundation's Board of Trustees is the sole body within the organization which exercises a dual function: It is both decision-making as well as supervisory body. The Board of Trustees appoints a managing director (Secretary General). The Secretary General is responsible for the administrative affairs of the Foundation as well as for preparing and implementing resolutions passed by the Board.

The governing bodies take care to ensure that the earnings potential of the assets in their trust is sustainable and that administrative costs do not become excessive. They ensure that the necessary measures are in place to protect the foundation from the illegal acts of third parties and misuse on the part of any organization not acting in conformity with the constitution of the Federal Republic of Germany.

- (2) **The rights and duties of members of foundation bodies are laid down in internal regulations.**

Explanatory notes: Foundations may dispense with the need for internal regulations in cases where the rights and duties of members of foundation bodies are already laid down in the foundation bylaws. As a rule, though, the members of foundation bodies make up their own rules of procedure. The internal regulations contain rules pertaining to the convening of meetings of the various foundation bodies, the chairmanship of meetings, the deliberation and adoption of resolutions in oral proceedings, postal voting, keeping of the minutes and how the foundation is to be managed, including all necessary authorization powers and stand-in procedures. The rules of procedure often provide that honorary members of the foundation's bodies receive an allowance i.a. to cover expenditures incurred in the exercise of their duties.

The Volkswagen Foundation's Board of Trustees has developed its own internal regulations in accordance with Article 5 Clause 7 of the Foundation's bylaws. The

Board of Trustees' internal regulations, last amended 21 November 1997 can be accessed.

- (3) **The internal regulations prescribe the procedure for the adoption of resolutions by the foundation bodies, both in oral proceedings as well as in postal voting.**

Explanatory notes: Some foundations have rules of procedure governing the adoption of resolutions laid down in their bylaws.

Most foundations provide for notational voting on resolutions to augment attendance at meetings of their decision-making bodies, which as a rule take place three times a year (cf. Item 6). Notational voting using written circulations enables decisions which are necessary for the management of the foundation and pursuit of the foundation objectives to be reached whenever needed throughout the whole year. As a rule, a quorum is given when two-thirds of the members are present: likewise, a resolution is deemed to be adopted on the basis of two-thirds of the votes given being in favor of the motion proposed. In some cases decisions may be reached on the basis of straightforward majority voting.

Resolutions may be adopted by the Volkswagen Foundation's Board of Trustees by way of notational voting when at least 10 of the 14 members of the Board of Trustees – including the Chairperson or his/her deputy – participate in the voting.

- (4) **Members of foundation bodies are not permitted to vote on resolutions or be involved in deliberations if they may be considered to be materially prejudiced due to their business, financial or personal relations with an intended recipient of funds or group of recipients.**

Explanatory notes: Members of foundation bodies are to give notification of potential conflicts of interest and personal entwinement whenever they occur and prior to voting on resolutions. They are expected to arrange their activities in such a way that conflicts of interest are as far as possible ruled out. It is expedient to maintain a register of their membership of other bodies and participatory interests in enterprises in order that possible conflicts of interest may become readily apparent to their fellow members. How to deal with such conflicts of interest when they occur is subject to further internal provisions. In addition to members of foundation bodies, as a rule these provisions apply also to the administrative staff, as well as to members of juries and advisors to the foundation.

Members of the Board of Trustees of the Volkswagen Foundation refrain from submitting proposals in cases where adoption of the proposal may be beneficial to either the trustees themselves or their own research group. In the event that a research institution to which a trustee belongs submits an application for funding, the trustee concerned is excluded from the entire procedure. The trustee concerned is neither privy to documents concerning the proposal, nor to information. The trustee participates neither in deliberation of the application in question, nor in the subsequent voting.

- (5) **The appointment procedure for members of foundation bodies is standardized and subject to written rules. The trustor may make provision in the deed of foundation for their own permanent membership of foundation bodies: this may also apply to close relatives. For persons other than those so named, the foundation rules of business**

foresee membership of foundation bodies to be for a period of up to ten years, provided this is deemed reasonable and adequate with respect to the pursuit of the foundation's objectives.

Explanatory notes: As a rule the foundation bylaws contain all necessary references to the appointments procedure. Nevertheless, the foundation rules of operation or the internal regulations pertaining to the various foundation bodies may also contain references to appointment procedures. These may include stipulation of the number of persons making up the body, responsibility for the appointments procedure, period of office, possibilities for extending periods of office and the procedure for electing the chairperson or president. Some foundations have in addition attached conditions calling for retirement of members of foundation bodies upon reaching a certain age. In most cases this applies upon reaching the age of 70. It is also considered expedient to provide for a staggered renewal of memberships.

Private trustors often make provision for permanent membership for a relative or relatives. Such provisions may not always be advisable, for as a rule foundations are created to last forever, and at the time of their creation it is impossible to determine whether the family representative will in future always be sufficiently competent, in agreement with the foundation objectives, or true to the family tradition. Likewise, representation on the part of a lawyer, solicitor or other trustee should be subject to a thorough examination of their professional competence in foundation affairs, their expertise with regard to pursuit of the foundation objectives, as well as their genuine involvement with the foundation objectives.

The appointment procedure for members of the Board of Trustees of the Volkswagen Foundation is regulated in Article 5 of the Foundation's bylaws. Article 5 Clause 3 limits a trustee's period of office to five years. Subsequent reappointment is possible for one further term only.

(6) **Members of foundation bodies meet at least twice a year.**

Explanatory notes: This guiding principle is to be regarded as a minimum requirement. The large German foundations convene meetings of their decision-making bodies with a frequency of between once a week (management) and twice a year.

As a rule most bodies convene three times each year.

The Board of Trustees of the Volkswagen Foundation convenes three times a year. As a rule, meetings of the Board of Trustees are in March, June and November.

(7) **In the event that a member's ill health results in a long-term impairment of their ability to carry out their duties, or that collisions of interest accumulate, or that serious deficits become apparent in the way they execute their duties, talks are held with a view to premature termination of their membership.**

Explanatory notes: The focus here is on ensuring the capacity to act of the foundation body in question as well as ensuring the existence of a quorum in voting processes. This is of particular relevance in the case of decision-making bodies whose members act for the foundation in a voluntary capacity and whose meetings are convened with long periods in between. Talks with a view to premature termination of membership should be instigated when, for example, a member is

absent from meetings on three recurrent occasions. Ideally, it is the member himself/herself who should raise the question of premature termination of their membership under such circumstances.

- (8) **Emoluments paid to members of foundation bodies and members of the management are disclosed in summary in the notes appended to the balance sheet.**

Explanatory notes: The term 'emoluments' includes the gross remunerations as well as all benefits in kind.

Foundation practice with regard to regulating the emoluments accruing to the members of foundation bodies as well as to members of the foundation management who are not involved in any one particular body is twofold. The persons concerned are either full-time employees or acting in an honorary capacity. In the first case they receive a salary; in the second case they receive an allowance. Notwithstanding, the guiding principle of disclosure of emoluments applies equally to the representation allowances paid to persons acting in an honorary capacity as well as to full-time employees. In the event that the persons acting for the foundation are both full-time employees as well as persons acting in an honorary capacity their emoluments are reported separately.

This does not apply to other members of foundation bodies who are solely acting for the foundation in an advisory capacity, such as referees, assessors, consultants, experts etc.

The relationship between the total emoluments accruing to the management and to all other members of foundation bodies must be reasonably proportionate to their duties, to the assets position of the foundation and to the financial results, as well as to the amount of their own individual liability.

The members of the Board of Trustees of the Volkswagen Foundation receive an allowance for their honorary work. Members of the Foundation's management are full-time employees and are paid a salary. All such amounts are contained in summary in the annual report 2007.

Achievement of foundation objectives

- (9) **Foundation resources are used solely in pursuit of the objectives laid down in the foundation bylaws.**

Explanatory notes: This guiding principle not only applies to the generally accepted self-conception of foundations in Germany, but to all foundations represented in the European Foundation Center. The term 'foundation resources' is taken to include not only a foundation's financial resources, but also their human resources and technical capacities, which are also basically and essentially to be deployed in pursuit of the foundation objectives.

- (10) **The foundation aims and main fields of activity are transparent for the public at large.**

Explanatory notes: Funding foundations engage in public relations to inform the public at large about the main focus of their activities and the orientation of their funding programs. The allocation practice of funding foundations is regulated by generally applicable guidelines or funding criteria. These can be accessed on the foundation homepage.

Operative foundations have declared aims and develop their projects on the basis of these aims. They inform the public at large about their aims via suitable public

relations activities. Internal rules regulate both the form of contract as well as allocation practice, so as to ensure the equal treatment of potential project partners.

The Volkswagen Foundation provides the public at large with comprehensive information especially by means of the Foundation's website. This contains details of the Foundation's current funding initiatives. Information sheets for applicants together with checklists provide details of how to apply for funding within individual programs. The website also contains details of the Foundation's funding principles and guidelines. In addition, anyone can ask for the Annual Report of the Volkswagen Foundation to be sent to them.

(11) Monitoring and evaluation to ensure the best possible achievement of foundation objectives.

Explanatory notes: Monitoring is generally taken to mean that the foundation accompanies projects whose implementation is in the hands of a third party. Project accompaniment may include: a visit to the project team on site, connected with a presentation of intermediate results; telephonic consultation or the perusal of progress reports. The aim of monitoring is to support and optimize the course of the project concerned.

On the other hand, evaluation as a rule entails a considerably more comprehensive scope, whereby the focus is on the overall impact of individual instruments of foundation activity. Thus, an evaluation procedure looks into the aims pursued by the instrument in question and the level to which these have been achieved. An objective evaluation calls for the involvement of an external panel of experts. The aim of such an evaluation is to determine any weak points in implementation of the particular instrument of foundation policy and, if necessary, to take appropriate steps towards a change in orientation (midterm evaluation), or from the experience gained from a project to draw conclusions and consequences to attain a more optimal result from the instrument in future (ex-post evaluation).

The monitoring of projects funded by the Volkswagen Foundation has always been a principle task of the employed as programme managers by the Foundation in the various fields of funding.

Besides the evaluation of individual projects, especially in connection with an extension of funding, the evaluation of entire funding initiatives was introduced in 2006. The evaluation of funding initiatives is carried out by external panels of experts. They are supported by a special member of staff working in cooperation with the Foundation experts in the various fields of funding.

(12) Periodical reporting on the foundation activities is established.

Explanatory notes: Normally, a foundation publishes an annual report containing information on the foundation activities, the projects funded or its operative engagement over the past year. The annual report also contains details of the foundation's administrative structure, the composition of the foundation bodies, and notes on important financial aspects and the foundation's assets. As a rule the annual report is published in print form and ideally it can be accessed on the foundation's website as well.

Although it does not constitute a legal requirement, the annual report, which is designated for the broader public at large, as a rule also fulfils the local [*landesgesetzlich*] legal requirements with regard to the foundation and tax authorities: This is because the annual report serves mainly to provide the public at large with information on the activities of the foundation, which could also be achieved via

the distribution of updates in the form of brochures or similar public relations media.

Large foundations publish annual reports as a matter of course. In other cases, periodical reporting every two or three years is considered to be adequate.

The Volkswagen Foundation provides information on its aims and areas of activity by means of issuing an annual report and the brochure entitled "*Impulse für die Wissenschaft*", which also appears once a year. In addition to this, a number of special publications appear dealing with the Foundation's activities as and when necessary. The homepage on the Foundation's website includes a possibility to subscribe to the Foundation's electronic newsletter.

Financial management and accounting

(13) **The allocation of funds and administrative expenditure ensues on the basis of budgetary planning.**

Explanatory notes: The budgetary plan for each following year is adopted by the supervisory body (as a rule in fall). The budget plan contains the expected income and expenditure.

The Volkswagen Foundation's budgetary plan for each coming year is adopted by the Board of Trustees at their fall meeting.

(14) **All financial transactions are subject to dual control as well as reporting procedures. Financial controlling is implemented to ensure that the financial objectives are achieved; this applies in particular to the investment of foundation assets.**

Explanatory notes: The term 'financial transaction' is used in a broad sense. Besides the routine transfer of payments it is taken to include all asset-relevant contracts; for instance purchase contracts, contracts for work or services, and employment contracts. Only trifling amounts are not subject to the process of dual control. Here the corresponding amounts are proportionate to the assets held by the foundation. Individual authorizations determine which persons are empowered to act with regard to any asset-relevant transaction of business. Procedures involving dual signatures ensure due diligence and the avoidance of malpractice and misuse.

Financial controlling supports the successful pursuit of financial aims. Financial controlling periodically provides the foundation bodies with information on the actual liquidity situation, deviations from financial planning, and the current state of capital commitment.

Each month the Finance and Accounting Department of the Volkswagen Foundation submit a financial report to the Foundation management. This includes updated key data with regard to the balance sheet, income statement/budgetary plan, development of the securities portfolio and securities transactions, funding statistics, disposable amounts for funding resulting from the (estimated) annual income, as well as funding plans. Likewise on a monthly basis, the Asset Management Department submits a report on the actual development of asset values in the areas of shareholdings, interest rate instruments, real estate and alternative investments.

- (15) **Internal audits ensure that funds are properly appropriated. There is only one exception: donations backed by appropriate donation receipts.**

Explanatory notes: The correct appropriation of funds by persons in charge of implementing projects, who are usually not in a direct employment relationship with the foundation, is ensured by internal audits. A report on the expenditure of funds can be submitted prior to an audit. This is to be completed by the recipient of the funds in question. It comprises a list containing expenditures on personnel and non-personnel items in connection with the project over the funding period. The foundation reserves the right to demand the presentation of receipts from the recipient of funds and to make random checks on site. Foundation funds proven to be expended outside the context of their allocation must be returned. The internal audit of appropriation of funds does not apply to donations for which the recipient (e.g. a public utility institution) has provided an appropriate receipt. Any allocation in the form of a donation must be proportionate with the size of the foundation and should not be in excess of 20,000 euros.

The proper appropriation of funding allocated by the Volkswagen Foundation is controlled by special audit. These audits are carried out on the basis of accounts submitted by the recipients of funding. A special form is provided to evidence such accounts. The Foundation reserves the right to demand presentation of receipts and to conduct inspections on site.

- (16) **The foundation and financial authorities are provided with an annual report on the fulfillment of the foundation objectives as well as an annual financial statement of accounts.**

Explanatory notes: Nearly all pertinent local [*Landesstiftungsgesetze*] legislation contains a stipulation that at the end of each financial year the foundation authority is to be provided with an annual financial statement of accounts together with an overview of foundation assets and a report on the fulfillment of foundation objectives. A regulatory gap exists solely in very few of the new German states. The legal period of grace varies depending on the state between four (Berlin) and nine months (North Rhine-Westphalia). As a rule the period is six months. There is no obligation on the supervisory body to report in cases where due to the legal framework (e.g. a Ltd. foundation) no foundation authority is responsible. The tax authorities also require an annual statement of accounts as well as a report on the fulfillment of foundation objectives in order to confirm the status as a tax-exempt institution. It is up to the discretion of the authority whether or not to require annual submission of the special tax declaration applying to tax-exempt institutions entitled "*Erklärung zur Körperschaftssteuer und Gewerbesteuer von Körperschaften, die gemeinnützige, mildtätige oder kirchliche Zwecke verfolgen*" (cf. AEO Nr. 7 zur § 59 AO).

Pursuant to § 11 Abs. 3 of the foundation law of Lower Saxony, the Board of Trustees of the Volkswagen Foundation is to submit to the foundation authority annual statements of account accompanied by an overview of the Foundation's assets and a report on how the Foundation goals have been achieved. The Volkswagen Foundation complies with this legal obligation by means of submitting the complete auditor's report to the appropriate ministry of internal affairs acting in their capacity as the foundation authority. A summarized version of the annual statement of accounts is included in the generally available annual report as well as on the internet.

Every three years the Foundation submits to the tax authorities the declaration applying to tax-exempt institutions entitled “*Erklärung zur Körperschaftssteuer und Gewerbesteuer von Körperschaften, die gemeinnützige, mildtätige oder kirchliche Zwecke verfolgen*”. A certified auditor’s report is submitted to the tax authorities on an annual basis.

- (17) **Rendering of accounts is done on the basis of generally accepted accounting principles. Accounts are audited and certified by an accounting firm.**

Explanatory notes: A few German states have included a legal obligation in their foundation laws for accounts to be rendered on the basis of generally accepted accounting principles. Other state legislations refer to foundation good governance in this respect. But for the most part, for foundations the rendering of accounts and foundation management remains unregulated. Therefore, most foundations orientate to the provisions of §§ 238 – 263 HGB [German Commercial Code]. This conforms with the minimum requirements for the rendering of accounts as contained in the declaration IDW RS HFA 5 of the *Institut der Wirtschaftsprüfer zur Rechnungslegung von Stiftungen* [Institute of foundation auditing firms] dd. 25th February 2000.

The financial accounts of a foundation are audited and certified by a private auditing firm which is selected and commissioned by the foundation’s supervisory body. It is deemed expedient to consider changing the auditing firm every five to eight years.

The Volkswagen Foundation renders accounts in accordance with the generally accepted accounting principles for enterprises pursuant to the German Commercial Code (§§ 238 to 263 HGB). The provisions contained in the German Commercial Code with regard to large joint stock companies are not considered relevant. The annual statement of accounts is supplemented by notes on the financial statements [*Ergänzende Angaben zur Jahresrechnung*], which do take into account the provisions applying to large joint stock companies. In addition a capital maintenance account is drawn up. The Foundation’s bookkeeping, the annual statement of accounts, the supplementary notes on the statement of accounts and the capital maintenance account are checked and certified by a firm of auditors which is chosen and commissioned by the Foundation’s Board of Trustees. The choice of auditing firm is changed approximately every ten years.

- (18) **Representatives of the supervisory body adopt the auditor’s report together with the responsible member(s) of the management.**

Explanatory notes: The auditor’s report is submitted to the foundation in the written form. As a rule this is combined with a meeting between the auditors, representatives of the supervisory body and the management [*Abschlussgespräch*], at which the foundation representatives are informed of the audit results. At least one member of the supervisory body who is present must be an acknowledged expert in financial and accounting matters. In the event that no such member is available an external expertise must be sought. In addition, the foundation is at liberty to appoint an audit committee pursuant to EU audit guidelines.

The body responsible for adopting the auditor’s report checks the adequacy of the audit services, the neutrality of the auditors, and submits proposals for the choice of auditing firm.

The Volkswagen Foundation accepts the auditor's report within the framework of a special meeting with the auditors. In attendance on the part of the Foundation are the Chairperson of the Board of Trustees, the member of the Board of Trustees appointed to the expert panel of advisors on the Foundation's assets and representatives of the management and the administration.

- (19) **The investment of liquid foundation assets is in accordance with the principle of risk differentiation. In the event that investment funds are managed by the foundation itself it is usual to appoint an asset management committee or similar body.**

Explanatory notes: The principle of risk differentiation can clearly apply only to the liquid foundation assets. The trustor is at liberty to determine irrevocably the composition of the foundation assets dedicated to foundation investment. For instance, it may be determined that the foundation hold the shares of a named issuer, or participation interests in a particular enterprise. In all other cases diversifying the risk exposure of the investment portfolio mitigates the danger of loss and contributes towards sustainable earnings. As foundations are under obligation to maintain the real value of their assets they tend to invest in assets which hold the promise of an increase in value. The retention quota pursuant to § 58 Nr. 7 AO can thus be reduced in favor of the foundation's funding activities. The investment portfolio may encompass classic forms of investment in property or shares as well as alternative innovative investments in private equities or hedge funds. A portfolio committee or similar body accompanies the correct choice of investment of the foundation assets. Such advisory bodies may be dispensed with in the event that the trustor or other members of foundation bodies possess the necessary expertise.

The Volkswagen Foundation's portfolio comprises investments made according to the principle of risk diversification. Foundation assets comprise shareholdings, real estate and alternative investments. A panel of experts advises the Secretary General on the Foundation's investment policy and submits recommendations. The expert panel of advisors on the Foundation's assets is convened twice a year.

- (20) **Monetary transactions are transparent.**

Explanatory notes: This principle underscores the accepted practice of German foundations and via creating transparency in monetary transactions takes account of the EU Commission's efforts to prevent misuse of the tertiary sector by terrorist organizations. Foundations take care to ensure that their liquid funds do not flow via dubious channels and as far as possible they avoid the transfer of cash money.

Upon the receipt of funds the onus passes to the recipient, who has to evidence that expenditure is solely in accordance with the provisions laid down by the funding foundation and maintain appropriate accounts. Recipients are screened with regard to their suitability; their selection is always carried out to the best of the foundation's knowledge.

The Volkswagen Foundation transfers funds exclusively to university and non-university research institutions in Germany and abroad. The allocation of funding is subject to a prior examination of the merits of a proposed project. In certain cases the Foundation may require to inspect the bylaws and request information

on the legal form, composition of bodies and committees, as well as budget details.

By accepting proffered funds the recipient agrees to the principles on which they are allocated and in certain cases specially agreed conditions. The submitted receipts and evidence of use are carefully inspected. Funds expended outside the framework of their intended allocation are recalled immediately. Upon discovery of irregularities in the course of a project the Foundation blocks any further funding until the matter is resolved.