Introduction

The late twentieth century witnessed the transformation of the global economy beyond the fixed geographic boundaries of the nation-state system to one dominated by financial centers, global markets, and transnational firms. In the two decades to 2011, cross-border philanthropy from OECD Development Assistance Committee (DAC) donor countries to the developing world grew from
approximately USD 5 billion to USD 32 billion (OECD, n.d.),[1] with some estimates for 2011 as high as USD 59 billion (Center for Global Prosperity, 2013). This is only part of cross-border philanthropy, which also includes remittances from migrant communities, social-media-enabled global fundraising, and medical research collaborations.

This era of “philanthropic globalisation” (Anheier, Glasius, & Kaldor, 2001) has been ushered in through the convergence of a number of factors, including deeply integrated global markets (Cutbill, Paines, & Hallam, Eds., 2012), free-trade zones, significant advances in communications technology, borderless social media, and an increasingly mobile workforce, particularly work tourism of young professionals. A tipping point was the creation of the Bill and Melinda Gates Foundation with its funding in over 100 countries. So significant is its contribution that in 2011 the OECD included global health grants made by the Gates Foundation in its aid data, enabling comparisons with governments (Smith, 2011). The Gates Foundation is now the largest funder in the global health arena outside the US and UK governments (Smith, 2011), spending more annually on global health than the World Health Organisation (McGoey, 2014).

The classic case (Pemsel) which established the definition of charity also dealt with cross border purposes and activities. The judges in Pemsel’s case found nothing amiss with a trust to advance “the missionary establishments among heathen nations” (Commissioners, 1891) in the context of a UK-wide taxing statute. Lack of direct or indirect public benefit to the local jurisdiction or the inability of the Attorney-General to supervise such charities in a foreign jurisdiction has also been repeatedly brushed aside in many cases since 1891. While commonwealth charity jurisprudence still maintains this stance, newly devised restrictions to avoid terrorism funding or money laundering through charities as well as taxation protections do not reflect this new-found passion for global philanthropy. European civil law countries have become progressive in their treatment of cross-border philanthropy compared to common law jurisdictions.

We examine two jurisdictions, Australia and the UK, and their fiscal policies regarding cross-border philanthropy. Australia has adopted a restrictive policy towards cross-border charity, whereas the UK, as part of the European Union, has had to adopt a more liberal policy.

**Australia**

In Australia, the common law of charity follows the direction set in Pemsel’s case, generally facilitating cross-border activities. However, charitable status only gives access to taxation exemption, not donation deductibility. The legislative environment of donation deductibility for cross-border activity is marked by strictly defined and guarded thresholds. Paradoxically, the Australian tax authorities have an enforcement strategy that at best appears to rely on self-regulation and the law-abiding nature of Australian citizens.

In 1991, a Parliamentary report found evidence of charitable trusts using tax havens to reduce declared income through tax deductions, and legislation to address the gap was finally passed in 1997. Income tax exemption for charitable organisations was made conditional on incurring expenditure or pursuing objectives principally in Australia. An organisation’s gifts and government grants were not counted in relation to such expenditure. Donation deductibility is regulated separately in Australia and the requirements for Deductible Gift Recipients (DGRs) were interpreted by the ATO more strictly than those for income tax exemption. For an organization to maintain status as a DGR, it must be established, controlled, maintained and operated in Australia; have its benevolent purposes in Australia;
and provide relief to people located in Australia. There are some exemptions for just over 1,200 organisations, with approval given to specifically named organisations and classes of organisations by the government departments responsible for overseas aid and the environment.

The regulatory strategy is simply to prohibit income-tax-exempt cross-border activity for all but the most incidental of transactions. A high threshold for gaining exemption from this prohibition has meant that it could take up to two or three years of negotiation in some categories. Once the status is granted, minimal overt regulation is applied to those organisations. Australian charities and nonprofit organisations are not required to file an annual tax return or any other information with regulators,[2] and there appears to be minimal auditing in the area by the Australian Tax Office. No easy means exist to even identify organisations at risk of noncompliance, for example, through a database. This also means that virtually no data are available on the size or extent of cross-border charity or philanthropy, making informed policy making difficult.

In 2008, the Tax Commissioner’s view of what was meant by “being located” or “physically in” Australia was overturned by the High Court in the Word Investments case (2008). The applicant (Word Investments), which operated a series of businesses as a fundraising arm, distributing donations to an Australian charity conducting missionary work overseas, met the “in Australia” requirements for income tax exemption. A majority of the Court determined that Word Investments had a physical presence in Australia, incurred its expenditure and pursued its objectives principally in the country; the decisions to pay were made domestically, the payments were made in Australia to Australian organisations and Word’s objectives included providing financial assistance to those organisations.

To address the implications of this High Court decision and to guard against the risk of cross-border financing of terrorism, the government at the time consulted on draft amendments in 2011, and again in 2012 following revisions. Both exposure drafts attracted serious criticism from the international development sector, mainly on technical grounds, but also pointing out the narrow view of the benefits to Australia of encouraging cross-border charitable activity. The first draft would have unwittingly caught applied to touring cultural exhibitions, educational activities and global medical research collaborations. In 2012, the Tax Laws Amendment (Special Conditions for Not-for-profit Concessions) Bill 2012 was introduced into Parliament but lapsed when Parliament was dissolved in August 2013 for an election. After the 2013 federal election the incoming government reviewed all tax proposals and decided to proceed with this particular initiative, publishing a third exposure draft (Sinodinos, 2014), which was opened for public consultation in March 2014 (Tax and Superannuation Laws, 2014). That Bill has yet to be introduced into Parliament.

While the sector has been successful in rolling back unintended technical consequences of the reform, it has made little headway on the proposition that outgoing philanthropy should be encouraged because of its public benefit to Australia. The political wisdom is against this notion at present. At the same time a bipartisan political commitment to increase Australia’s international aid ended in 2012 and the government of the time announced significant funding cuts from the Australian aid program. In 2014, the new federal government went further in limiting overseas development assistance, announcing in its first budget that foreign aid would be capped, to realise an estimated saving of A$7.6 billion over five years. The political climate was very much that tax concession benefits were to stay in Australia and little recognition was given that there were any public benefits for Australia in facilitating cross-border charity or philanthropy.
United Kingdom

As in Australia, the common law of charity in the UK follows the direction set in *Pemsel’s case*, generally facilitating cross-border activities. However, the legislative environment in the UK regarding cross-border charity is more permissive than it is in Australia, largely due to judicial decisions in the European Union (EU). UK tax legislation containing charitable tax reliefs traditionally relied on the common law definition of charity now contained in the Charities Act 2011; however, as a result of developments in European law leading to the expansion of charitable tax reliefs beyond the UK’s geographic borders, the public revenue agency’s response has been to introduce a new definition of charity for fiscal purposes providing increased oversight of charities engaging in international charitable activities.

UK charities are able to operate overseas provided the trustees take reasonable steps to ensure that funds expended overseas are applied for the organisation’s charitable purposes. Any funds found not to have been applied for charitable purposes may be deemed by the UK tax authority, HM Revenue and Customs (HMRC), to be a non-charitable expenditure, resulting in liability for tax on the amount of the non-charitable expenditure (HM Revenue and Customs, n.d.). The principal UK charity regulator, the Charity Commission for England and Wales, provides detailed guidance on how to identify and manage risks for charities working overseas (Charity Commission, 2013). All registered charities with income greater than £10,000 are required to submit an annual return to the Charity Commission, which must include information on the amount spent in each country overseas (Charity Commission, 2014), thereby also providing valuable data on cross-border charitable activities.

Historically, donations by UK taxpayers directed overseas did not receive the same favourable tax treatment applied to domestic donations. Those donors seeking tax relief had two options: give to a “friends of” charity serving as a UK affiliate for a foreign charity, or donate through a giving intermediary, such as Charities Aid Foundation (Cutbill, Paines, & Hallam, 2012). However, the European Court of Justice determined in *Hein Persche v Finanzamt Lüdenscheid* (2009) that a member state cannot impose territorial fiscal restrictions on charitable tax reliefs,[3] so the majority of member states, including the UK, amended their tax laws to reflect this principle of non-discrimination (von Hippel, 2014). The UK’s Finance Act 2010 now extends Gift Aid (Scharf & Smith, 2014)[4] and other charitable tax relief[5] to donors who make gifts to a charity in an EU member state, Iceland or Norway. Concerned about the potential for fraud and other abuses with this geographic expansion, HMRC introduced a stricter definition of charity, which applies to all charities (UK or foreign) seeking charitable tax relief. The Act now defines a charity as a body of persons or trust that:

- is established for charitable purposes only (as defined in the Charities Act 2011),[6]
- meets the jurisdiction condition (i.e. is subject to the control of a relevant UK or EU court or the equivalent under the law of another territory),
- meets the registration condition (by complying with any requirement to be registered as a charity in the UK or with any equivalent requirement under the law of another territory),
- meets the management condition (requiring that its managers are “fit and proper persons”; Finance Act, 2010).

Interestingly, the jurisdiction condition is not restricted to European countries. Instead, the wording leaves scope for charitable organisations beyond Europe to become eligible in the future if their country is included in the regulations (Bowler Smith, 2012), prompting one commentator to ask why more
countries, particularly other common law countries, have not yet been included (Meakin, 2013).

Despite this geographic expansion, the increased regulatory powers of HMRC created some alarm in the UK charitable sector. It was concerned that if a manager failed the fit and proper test, HMRC could refuse to provide the charity with tax relief (Morris, 2014). While the test was designed to prevent abuse of an organisation’s charitable tax status by its trustees and senior managers, “fit and proper” was not defined in the legislation. HMRC subsequently issued detailed guidance (HM Revenue and Customs, 15 October, 2014), which resulted in better oversight of charities (Morris, 2014). The Finance Act 2010 also provided HMRC with a greater role in the governance of charities. Historically HMRC was satisfied that organisations registered with the Charity Commission qualified for charitable tax relief, however charities are now also required to register with HMRC, which duplicates the Charity Commission process and takes approximately 10 weeks (Cutbill, Paines, & Hallam, 2012).

While these legislative developments have increased the administrative burden for charities, they have also widened the territorial scope of UK charitable tax reliefs. In 2013, the UK government also increased its overseas aid by almost 30 per cent, which enabled it to reach the UN target of 0.7 per cent of aid as a percentage of gross national income, for the first time (OECD, 2014). These policy developments appear to recognise a broader conception of public benefit, facilitating cross-border charitable activities.

Conclusion

An examination of Australia and the UK presents two different policy responses to the tax treatment of cross-border charity and philanthropy. Australia has adopted a particularly restrictive policy, confining the benefits of its charitable tax reliefs largely to taxpayers who reside within its territorial borders. By contrast, the UK, responding to developments in European law, has adopted a more progressive stance, albeit with regulatory controls, adopting a more expanded view of public benefit in the tax law, consistent with the approach taken in the common law charity jurisprudence.

There are some lessons to be learned from the response of the fisc in these two commonwealth jurisdictions. The Australian approach of placing territorial limits on charitable tax reliefs through the adoption of a strict regulatory strategy for cross-border charitable activities and donations, without an appropriate enforcement strategy, has resulted in a complicated and costly system for organisations engaging in international charitable activities. These organisations are faced with regulations that are on the one hand extremely restrictive, and on the other are able to be circumvented. This situation has created great uncertainty for Australian organisations and donors operating in a global charitable and philanthropic environment, and paradoxically has the potential to heighten the very risks (such as cross-border terrorism financing) that the government is trying to guard against.

Recent legislative developments in the UK have engendered productive debate between the government and the charitable sector around tax reliefs for cross-border charity and philanthropy. The UK approach of extending charitable tax reliefs to organisations operating in, and donations directed to, countries outside its geographic borders that meet specific conditions while increasing regulatory controls, has not led to significant leakage of tax revenue or a spike in tax abuse. At the same time, the UK experience highlights the importance of engaging with the charitable sector from the outset when making such regulatory changes, to avoid unnecessary alarm and uncertainty.

As part of the EU, the UK has become part of a larger regional movement recognising the charitable
and philanthropic globalisation taking place in Europe, reflecting the larger global reality of a world where charitable activities and donations routinely cross borders. For other countries seeking to participate effectively in this charitable and philanthropic globalisation, the UK shows that fiscal policies with appropriate regulatory and enforcement frameworks may be the best way forward.

NOTES

[1] This figure is from the line item “net grants by NGOs” in all DAC countries to both “Part I” and “Part II” countries. These consist of all low- and middle-income countries based on gross national income (GNI) per capita as published by the World Bank. See also OECD’s DAC List of ODA Recipients: Factsheet January 2012.

[2] Minor exemptions apply to some family foundations and community foundations which are required to file annual audited statements to the ATO. The Australia Charities and Not-for-profits Commission was established in 2013 to remedy this information gap, by requiring audited annual accounts and an information return to be filed for online publication, but the current government is seeking its abolition.

[3] This case built upon an earlier ECJ decision involving the taxation of foreign charities, Centro de Musicologia Walter Stauffer v. Finanzamt München für Körperschaften (C-386/04) [2006] ECR I-8203.

[4] Gift Aid is the main scheme for individuals to get income tax relief on their charitable donations. The Gift Aid Scheme offers a match on donations made by all taxpayers through the scheme, combined with an additional rebate for higher rate taxpayers.

[5] Tax relief is also available through payroll giving and for charitable gifts of shares and land. Charitable gifts are also exempt from inheritance tax.

[6] To be established for charitable purposes, the purposes of the organisation need to fit under at least one of the statutory purposes listed in the Charities Act 2011 and those purposes must be for the public benefit. See Charities Act 2011 s. 1.

References


Charities Act 2011 (UK) c.25, s.1.


Finance Act 2010 (UK) c. 13, s. 30, sch. 6.


*Word Investments*(2008) 236 CLR 204 [73].