

## EFC Legal and Fiscal Country Profiles: Introduction and Comparative Highlights

This publication aims to provide the reader with an overview of the diverse legal and fiscal environments of foundations across the 27 EU Member States, plus Albania, Switzerland, Turkey and Ukraine. Standard sections across all profiles enable an easy comparison of specific legal and tax issues across the countries.

The profiles have widened in scope since the previous EFC country profiles publication in 2002, and their structure has been redesigned by the EFC membership. The profiles now address issues concerning the legal environment of foundations, such as the purposes that foundations are allowed to pursue, the requirements for setting them up, and governance and transparency requirements. The tax treatment of foundations is also discussed, with details on the income tax treatment of the foundation, including income from economic activities and asset management. In addition they provide information on tax incentives for individual and corporate donors, including on the issue of cross-border donations, and a section on recent legal trends and developments affecting foundations, such as the impact of the anti-terrorist debate.

### ***Comparative highlights of Europe's national legal and fiscal environments***

No common European legal definition of the term “foundation” exists. Nevertheless, there is across Europe at least a generally understood and accepted concept of what public benefit foundations are: Independent, separately-constituted non-profit bodies with their own established and reliable source of income, usually but not exclusively from an endowment, and their own governing board. They distribute their financial resources for educational, cultural, religious, social or other public benefit purposes, either by supporting associations, charities, educational institutions or individuals, or by operating their own programmes (this functional definition was developed by the EFC)<sup>1</sup>. Below is a brief analysis comparing key areas of the 30 2011 EFC Legal and Fiscal Country Profiles, which are available to download from the EFC website.

### ***Requirements for setting up a foundation***

Most of the countries surveyed that have civil law systems recognise the foundation as a legal form. In other countries, such as the UK, Ireland and Cyprus, the focus is on the public benefit character and the activities of the foundation, which can take different legal forms such as incorporated or unincorporated associations, trusts, companies limited by guarantee, etc. The law on charities in these countries has been developed on a common law basis.

All countries require that the foundation's assets be dedicated to a specified purpose. In approximately half of the countries, the foundation laws require that the foundation pursue public benefit purposes only. Some foundation laws allow foundations to pursue any lawful purpose, including private purposes. Private purposes include, for example, the advancement of one family, relatives of the founder, trust funds for the funders' children's education, etc.

Most EU countries require foundations to register with an authority or the court. In several countries, state approval is needed for a foundation to be established. However, only in very few countries do the authorities have discretionary powers not to approve a foundation (Cyprus, France, Greece, Luxembourg, and Switzerland).

In most countries, no initial starting capital for foundations is required by law, but the authorities require that the foundation possess a sufficient amount of capital to fulfil its purposes. Starting capital is required by law, for example, in: Austria (for private foundations), Czech Republic, Denmark, Finland, Malta, Romania, Slovakia, Spain, and Turkey and the amount ranges from approximately

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<sup>1</sup> “Working with Foundations in Europe: Why and How”, EFC, Brussels 2001

€240 for public benefit foundations in Malta to the €70,000 required for private foundations in Austria. In practice (not required by law), a starting capital of up to €1 million may be required by the authorities (France). Other countries, such as Estonia, the Netherlands, Poland, Sweden, UK (charitable companies) and Slovenia do not require a minimum capital.

### **Governance**

Legal requirements regarding the governance of foundations vary between countries. In most countries, the mandatory governance organ is a governing board, but foundations are free to set up other organs if they deem it necessary. 9 countries (Albania, Czech Republic, Estonia, Italy, Poland, Portugal, Slovakia, Turkey, and Ukraine) require a supervisory board to be set up in addition to the governing board. Some countries also make requirements concerning the appointment of auditors or setting up of auditing boards. France gives foundations the option of having a supervisory board and executive board or a management board. In several countries, the board can be composed of one board member only. However, there seems to be a trend towards requiring at least three board members.

In most countries the board can be composed of individuals as well as legal entities. However in some countries only natural persons are allowed to become board members (Austria for public benefit foundations, Czech Republic, Denmark, Finland, Hungary, Latvia). The founder is generally allowed to be a member of the board. In Hungary, the founder and his relatives have to be the minority, and in Sweden, the founder must not be the sole board member.

Most countries give freedom to the founder to define in the statutes how board members are appointed. The founder usually appoints the initial members of the governing board. The power to appoint new board members may rest with the founder, with another natural or legal person, with the supervisory board of the foundation, or with the members of the board of directors (co-option system). Only a few countries have mandatory rules: In Denmark, the majority of the board members of commercial foundations must be persons not appointed by the founder or his/her family and in Austria, the initial members of the board of directors of a public foundation are appointed by the supervisory authority.

Most countries also give freedom to the founder to determine in the statutes in what circumstances a board member may be dismissed. In certain cases (e.g. mismanagement/breach of the statutes) the state supervisory authority has the right to remove a member of the board as part of state supervision.

Generally, it falls to the governing board to manage the foundation and represent the foundation towards third parties. Regarding the remuneration of board members, most countries allow a reasonable level of financial compensation. In Denmark, the state supervisory authority may check whether the remuneration is appropriate, and can reduce any remuneration deemed excessive.

Some countries generally prohibit remuneration of board members (e.g. France, Spain, and the UK). The majority of countries surveyed provide for rules against a conflict of interest of board members. Some national laws provide special rules about self-dealing transactions (e.g. Czech Republic, Estonia, Germany, and Sweden).

### **Reporting and accountability**

All 31 countries surveyed indicated that public benefit foundations are required to submit financial information (variously in the form of annual budget/balance sheet, audited/unaudited annual accounts, and financial report) to a relevant authority, be this the fiscal authorities or the supervisory body for foundations, or both.

In 21 countries, annual reports/accounts need to be made publically available. In Albania, Austria, Cyprus, Germany, Ireland, Italy, Latvia, Slovenia, and Turkey, it is not required that annual reports and/or accounts be made publically available. For Private foundations in Austria, Cyprus, foundations

in Czech Republic, commercial foundations in Denmark, Estonia, Finland, public utility foundations in France, Greece, Lithuania, Slovakia, Switzerland with some exceptions, and Sweden an external audit of foundations' accounts is required. In many other countries, an audit is required only for larger foundations.

Foundations are in general supervised by a designated state authority, although the powers of the supervisory authorities vary widely. In England and Wales, the supervisory authority is the Charity Commission, an independent corporate body, which replaced in February 2007 the five individual Charity Commissioners for England and Wales.

### ***Economic activities***

In this publication, economic activity is understood as "trade or business activity involving the sale of goods and services". It has to be noted that the term "economic activity" is not always clearly defined in the different countries. "Related" economic activity is in itself related to and supports the pursuance of the public benefit purpose of the foundation. Foundations can engage in economic activities in most of the countries surveyed, although the majority of countries impose some limitations on the nature of activities permitted. The tax exemption of income from economic activities is restricted to income below a certain threshold in many countries. This is the case the Czech Republic, Germany, Hungary, Lithuania and Romania.

The most common limitation imposed on economic activities is the requirement for related activities, i.e. the activities must facilitate the foundation's purposes and/or should remain ancillary to the foundation's activities. This is the case in: Albania, Belgium, Cyprus, Czech Republic, Finland, France, Germany, Ireland, Italy, Portugal, Spain, UK, Switzerland, and Ukraine. Slovakia and the Czech Republic only allow some very specific economic activities listed in the law. In Denmark, two foundation acts exist side by side providing different legal regimes for commercial and non-commercial foundations. Commercial foundations, regulated by the Act on Commercial Foundations, can pursue economic activities as a part of their purpose or as their sole purpose. In such cases the statutes must contain a regulation on the distribution of profits.

The rules concerning major shareholding also vary widely across the countries. Most national laws allow major shareholding, but active involvement in operational management / exercise of voting rights would lead to taxation as economic activity.

### ***Tax treatment of the foundation<sup>2</sup>***

All countries surveyed provide for some form of special tax treatment for public benefit purpose foundations. However, there is no common approach to defining the public benefit criteria that can lead to tax relief. What can qualify as public benefit in one country might not be considered as such in another.

In addition, procedures for obtaining tax privileges vary considerably, e.g. application to the tax authority, decision by the Ministry of Finance, etc. The majority of countries allow foundations to engage in activities abroad without compromising their tax status, but foundations, for example in Austria and Portugal, may lose their tax-exempt status if they engage in activities mainly outside of their home country. German legislation requires that the activities of a tax exempt foundation have a positive impact for Germany.

Coming back to the tax treatment of public benefit foundations, we can underline that donations to public benefit purpose foundations are in general exempt from corporate income tax. In Denmark, however, public benefit foundations do pay income tax on grants and donations, although this is with the exception of grants/donations given for the purpose of building up the foundation's endowment.

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<sup>2</sup> For further comparative analysis of tax laws in Central and Eastern Europe, please refer to "Survey of Tax Laws affecting Non-Governmental Organisations in Central and Eastern Europe", second edition, International Center for Not-for-Profit Law, 2003

The same is applicable for income deriving from asset management in most countries. Foundations that pursue public benefit purposes are, in the majority of the countries, also exempt from gift and inheritance tax. In Slovakia, Sweden, and Ukraine, there is no gift/inheritance tax.

An important point is, of course, the tax treatment of economic activity. Three categories can be found: Some Member States tax all business income in full whether from related activity or unrelated activity. Most countries tax income from unrelated activity but exempt income from related activity. Some Member States (e.g. Germany, Hungary, Spain and the UK) go even further as they also exempt unrelated economic activity. However, all those countries mentioned above only exempt small-scale unrelated economic activity. Some have introduced a ceiling into the law text – this is the case in Germany, Hungary and Spain.

16 countries report that a **foreign based foundation** can get the same tax benefits as a national foundation. To take some examples: In Bulgaria and the Czech Republic EU/European Economic Area based organisations are entitled to the same tax benefits as national foundations. In Switzerland non-profit organisations with their registered offices abroad are entitled to tax privileges under the same conditions as national foundations. In Denmark any foundation can apply to the Danish national tax authorities to be approved as having a public benefit purpose for certain tax purposes (deductibility of donations made to foundations and other public benefit organisations). Every year a list is published with the names of all foundations approved as public benefit. Similarly, in the UK foreign foundations wishing to receive tax exemptions must be registered with the tax authority (HMRC) and thus recognised as being comparable to a UK charity. Some countries, such as France, Greece and Germany, grant comparable tax benefits to foreign foundations only when certain additional criteria are fulfilled.

### ***Tax treatment of donors<sup>3</sup>***

Individual and corporate donors are eligible to claim tax relief for charitable donations in most jurisdictions. Only Slovakia has no tax incentives in place for individual or corporate giving, while Albania, Finland and Sweden only provide some tax incentives for corporate donors. In some countries, tax exemptions for donations by corporate or individual donors can be claimed only in certain limited circumstances. Some countries, such as Lithuania, Poland, Slovakia, Italy, Portugal and Spain have percentage schemes where an individual donor can choose to allocate a certain percentage of their payable taxes to a designated public benefit organisation.

In many countries, **donations to non-resident foundations** do now qualify for tax relief to the donor, to some degree. However, the extent of the incentives and the requirements to claim them vary between countries. Several countries only grant tax incentives for donations to foreign public benefit organisations if the organisations are locally registered (for example, Austria, Denmark, and the Netherlands).

Within the European Union, the European Commission has been active in initiating infringement procedures against Member States whose tax treatment of donations to public benefit organisations varies according to whether or not the recipient organisation / donor is domestic or foreign based. The Commission has deemed such provisions to be discriminatory and in breach of the Treaty on the Functioning of the European Union. In recent years, several Member States have amended their legislation in response to such procedures (for example, Poland, Belgium, Netherlands, and the UK). In some cases (such as Belgium and the Netherlands) amended provisions on this issue continue to impose what the Commission considers to be unnecessary restrictions and further requests for changes to the legislation have been issued. In Sweden and Slovakia, no tax incentives are available for cross-border donations, reflecting the absence of such incentives for local giving.

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<sup>3</sup> Detailed information about cross-border giving can be found on the King Baudouin Foundation's Giving in Europe website: [www.givingineurope.org](http://www.givingineurope.org)

Outside of the EU, donations by residents of Albania, Switzerland, Turkey and Ukraine to non-resident public benefit organisations are not tax deductible for the donor. In Switzerland, the law provides that the receiving organisation must have its registered office in Switzerland in order for Swiss resident donors to receive tax benefits for making a gift. In Turkey, non-resident public benefit organisations are not accepted as meeting public benefit criteria, while in Ukraine donations to both non-resident organisations and the representative offices of foreign public benefit or private foundations in Ukraine that have the legal status of tax non-residents do not qualify for tax incentives.

The above general overview highlights only some of the overall trends in foundation laws across the countries surveyed. Please read the profiles themselves to learn more about the different legal and fiscal environments for foundations across Europe.