



# Enlarging the Space for European Philanthropy

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## Executive Summary

How big is the space for philanthropy in Europe today and what can be done to protect and enlarge the space? This DAFNE/EFC jointly commissioned report by Oonagh B. Breen undertakes a scanning of the horizon of philanthropy's operating space.

The report defines 'the philanthropic space', which it distinguishes from civil society space more generally, as the environment within which donors/funders and the philanthropic organisations they create, are facilitated in their use of their assets for the public benefit. It recognises that institutional philanthropy can take many different forms (both unincorporated and incorporated). Legal, fiscal and administrative obstacles may impact the "philanthropic space" and its potential to define, advocate for and achieve the public good.

The report discusses the Structural Space for Philanthropy within the EU and wider Europe. It examines what the EU Treaties/Fundamental Freedoms and European Fundamental Rights offer for philanthropy as well as the lessons learnt from previous European experiences of attempting to create supranational philanthropic structures to facilitate cross border activities.

Three broad areas relevant to the functioning of philanthropic space are analysed in detail, namely a) legal/regulatory measures; b) fiscal measures; and c) guidance/soft law and the report explains the place of each of these mechanisms within the EU and maps out their broad interaction with each other.

International and European regulatory measures that have impacted the philanthropic space, ranging from the Financial Action Task Force's implementation of Recommendation 8 ('R8') and the interrelation of the EU's anti-money laundering directive, to the EU's most recent attempts at supra-national risk assessment and emerging trends in some European countries towards the adoption of foreign agents' laws are reviewed.

Fiscal developments, with a special emphasis on cross-border philanthropy taxation, are analysed in light of the recent EFC and TGE *Boosting Cross Border Philanthropy Report 2017*.

**The study explores possible future policy avenues that may exist to facilitate philanthropy in Europe.**

Starting from the premise that "If you always do what you've always done, you will get what you've always gotten", a changed approach is recommended if we are serious about enabling the space for philanthropy.

Regarding the potential development of **non-profit oriented European regulatory measures** (e.g. new European legal forms), overcoming the unanimity requirement in the Council, which has been a constant stumbling block for European non-profit regulation, is recommended. One proposal could be to avail of the 'enhanced cooperation' mechanism for developing a supranational legal form regulation or to consider the potential for an EU Directive that would create a new legal form for institutional philanthropy at national level with a minimum common denominator in all EU countries. The Directive

could allow Member States the freedom to decide how to introduce such a legal form at national level, whether by way of an additional instrument or an instrument replacing currently existing legal forms.

Ongoing EU efforts to **counter-terrorism financing** and **money laundering** have continued to view the non-profit sector, including philanthropic money flows, as vulnerable to exploitation. Efforts are needed to ensure that measures intended to protect the sector are risk-based, proportionate and evidenced-based. In addition, policy makers must engage and consult with philanthropic institutions when assessing and addressing risks, both in the context of the FATF and at national and European levels.

More effort should be invested in developing **soft-law mechanisms** at national and European levels, specifically in the context of addressing potential terrorism financing and money laundering risks. There is a window of opportunity available to philanthropic organisations to engage with the Commission and national competent authorities in facilitating more informed conversations around the risks and how to address them. Philanthropy should also continue to engage via the Global NPO Coalition on FATF ('the Platform'), which has helped to bring about incremental reform of the guidance documents related to R8 and more recently reform of R8 itself. The culmination of this collaboration with the formal inclusion of the Platform and philanthropy on the Private Sector Consultative Forum (PSCF) has shored up the legally enabling environment for philanthropy, even as efforts continue through the Platform to ensure that philanthropic actors and the wider NPO sector play a full role in the site evaluation visits of countries undergoing their Mutual Evaluation assessments.

The continued existence of **fiscal and legal barriers to cross-border philanthropy** arising from incompatible and EU law conflicting laws and practices is identified as an ongoing challenge. National laws must be in line with the EU Treaties. Treaty infringement procedures provide a useful tool to address conflicts that arise, as borne out over the past 10 years in the challenged violations of the free movement of capital and the non-discrimination principles in the field of cross-border philanthropy taxation. It is interesting to note in this regard the EU Commission's launch of infringement proceedings against Hungary in July 2017 as the first EU country to introduce restrictions on foreign funding to NGOs, making the infringement procedure mechanism one of the most effective tool available to the EU in protecting the philanthropic space.

One of the main problems when it comes to enabling the fiscal space for cross-border philanthropy in Europe is the **lack of clarity and lack of publicly available information** around comparability processes operated by Member State tax authorities when faced with cross-border philanthropy cases. The report recommends the creation of a website resource and the pooling of national knowledge and knowhow, providing details on existing or emerging Member State tax authority procedures, coupled with the explanatory guidance or links to the relevant application forms. It is less convinced of the prospect for success of a proposal for determining comparability between local and foreign based public benefit organisations, broadened to look at core principles of public benefit, given the recent reluctance of Member States to support a European Foundation Statute with tax implications.

As the **current squeezing of civil society space** in some parts of Europe reverberates in the philanthropic space, the need for European protective measures and perhaps greater joined up thinking by stakeholder institutions to keep open the space for philanthropy is required. The role of the Fundamental Rights Agency, The Council of Europe, the European Court of Human Rights and OSCE also for philanthropy should be further reviewed.

The report also identifies the need to further explore and better understand the potential and, equally, the limitations of emerging forms of venture philanthropy and social investment to provide new tools for facilitating philanthropic growth and outreach in Europe.

# 1. Enlarging the Space for European Philanthropy: Introduction to the Conceptual Space

## Introduction

How big is the space for philanthropic giving in Europe today? What are the factors influencing current philanthropic capacity and what are the challenges that must be overcome if we are serious about simultaneously protecting and enlarging philanthropic space within the EU and Europe more broadly? To what extent is the space within which European philanthropic organisations operate growing or shrinking? These are just some of the issues to be explored in this jointly-commissioned European Foundation Centre (hereinafter 'EFC') and Donor and Foundation Networks in Europe (hereinafter 'DAFNE') study.

Tackling these important issues, however, first requires consideration of another question: what do we mean by "philanthropic space"? How, for instance, does 'philanthropic space' differ from 'civic space'? The concepts of 'civic space' and 'civil society' and 'civic engagement' are terms with a long historical pedigree that regained new currency, taking root in the public consciousness over the past half a century. The sociological and political understanding of "civil society" underwent a revival in the 1980s with the collapse of communism in Central and Eastern Europe and the emergence of post-communist and post socialist states.<sup>1</sup> Historically and politically, civil society has been perceived as the space outside of government and the family that may or may not include the market place.<sup>2</sup> Modern conceptions of civil society – driven by the growth in numbers of NGOs and INGOs, coalescing with citizen action on the ground seeking greater democracy, and coupled with the emergence of new social movements – revolve very much around the protection of the fundamental freedoms of assembly, association and expression.

## From Civic Space...

The domain in which civil society operates and responds to the other players – whether viewed as the state or the state and the market – is often referred to as the 'third sector' or 'civic space.' The presence of this dynamic zone – enjoying low barriers to entry, ensuring a plurality of ideas and voices that is yet subject both to the rule of law and to the natural competitive tendencies of the market – is meant to inject a healthy balance into the political constitution of democratic regimes. Civic space thus provides the environment within which civil society actors have the freedom and means to speak, access

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<sup>1</sup> Adam Michnik, "The new evolutionism" in *Letters from prison and other essays* (Berkeley: University of California Press, 1985); Vaclav Havel, "The power of the powerless" in John Keane, ed., *The power of the powerless: citizens against the state in central-eastern Europe* (London: Hutchinson, 1985), pp. 90–1.

<sup>2</sup> Compare, for instance, the views of Helmut Anheier, "Can culture, market and state relate?" *LSE Magazine*, (Summer, 2000), 16–18 (excluding the market from the definition of civil society) with those of John Keane, *Global Civil Society?* (Cambridge: Cambridge University Press, 2003), 77 (noting "The point is elementary, but important, for whether we like it or not, the division between market and civil society does not exist.")

information, associate, organise, and participate in public decision-making. The existence of civic space is seen as a prerequisite to the healthy functioning and development of any society.<sup>3</sup>

In regimes in which democracy is under threat, civil society and the civic space provide a valuable outlet for differing or dissenting views which, if denied, may lead to a greater destabilising of society. State rejection or repression of civil society has led to much talk of ‘the shrinking space for civil society’ both within national and international contexts. According to Douglas Rutzen, the president and CEO of the International Center for Not-for-Profit Law (ICNL), “since 2012, more than 120 laws constraining the freedoms of association or assembly have been proposed or enacted in 60 countries.”<sup>4</sup> International recognition both of the current and growing threats to civil society space and the need to protect it are widespread.<sup>5</sup> For its part, the European Commission has committed the EU to fostering a dynamic, independent environment in which civil society can grow in the context of its external relations policy.<sup>6</sup>

### ... to Philanthropic Space

If civic space is the broad horizon, to what then does the term ‘philanthropic space’ relate? The space for philanthropy relates to one aspect – albeit an important aspect – of this broader civil society space. The space for philanthropy focuses on the enabling environment for donors/funders (and the philanthropic organisations they may create) who wish to use their private wealth for the public benefit in a manner that does not suffer unduly from political interference or legal obstruction. While philanthropy can take many forms, from the magnanimous sole benefactor through to the family or corporate foundation, the type of philanthropy at the heart of this study is institutional philanthropy. Even within this realm of institutional philanthropy, many different forms (both unincorporated and incorporated) exist along with many different model types ranging from grant-making organisations to operating foundations and even hybrid organisations that mix grant-making with the running of their own funded programmes.

As defined by the EFC, public benefit foundations comprise those non-profit bodies that are “[i]ndependent, separately-constituted . . . bodies with their own established and reliable source of

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<sup>3</sup> Carmen Malena, *Improving the Measurement of Civic Space* (Transparency and Accountability Initiative, 2015), 7. See also, Swedish Government sponsored Civic Space Initiative, a multi-year program (2012-2016) that seeks to a) advance a legal environment that enables all people to exercise the freedoms of peaceful assembly, association, and expression; and b) create spaces for citizens, communities, and civil society organizations to meaningfully engage with government and other power holders on freedoms of assembly, association, and expression, <http://www.icnl.org/csi/index.html>.

<sup>4</sup> Douglas Rutzen, “Civil society under assault” (2015) 26(4) *Journal of Democracy*, 28-39, 30.

<sup>5</sup> See Community of Democracies, Working Group on Enabling and Protecting Civil Society (<https://www.community-democracies.org/Working-for-Democracy/Initiatives/Governmental-Bodies/Working-Group-on-Enabling-and-Protecting-Civil-Soc>); UN Human Rights Council, Resolution on Civil Society Space, committing States to create and maintain a safe and enabling environment for civil society ([A/HRC/32/L.29 as orally revised](#)).

<sup>6</sup> European Commission, *Communication: The roots of democracy and sustainable development: Europe's engagement with Civil Society in external relations* COM(2012) 492 final (September 9, 2012).

income, usually but not exclusively from an endowment, and their own governing board. They distribute their financial resources for public benefit purposes, either by supporting associations, charities, educational institutions or individuals, or by operating their own programmes.”<sup>7</sup> Many of the core characteristics present in this definition are equally shared by the many philanthropic organisations not established as foundations and found more commonly in common law jurisdictions, a factor recognised and endorsed by DAFNE in 2014.<sup>8</sup> Having these characteristics as the defining proxy for European institutional philanthropy allows us to engage in a more holistic examination of the state of institutional philanthropy and the challenges facing it.

Within the philanthropic space, in this sense, we are concerned with any legal, fiscal, or administrative obstacles (whether viewed as political or more simply “technical” problems) that prevent a free-flow of funds from donor to donee and its effective use thereafter by the recipient or which unduly restrict the creation and operation of philanthropic organisations. The importance of this space to society and democracy more generally should not be underestimated. In the words of Payton and Moody:

[P]hilanthropy plays an essential role in defining, advocating and achieving the public good. Philanthropic actions are a key part of the ongoing public deliberation about what the public good is and how best to pursue it . . . . *Both* government and philanthropy provide public goods. Sometimes they do so in partnership – government money is a primary source of funding for non-profit organizations – and other times philanthropy steps in to provide public goods – goods that are vital to a democratic society -- when both the market and government fail to do so.<sup>9</sup>

How big then is the space for institutional philanthropy in Europe? How is this space currently changing and what can we do to enlarge it? According to DAFNE, there are approximately 147,000 public benefit foundations (adopting the EFC 2001 definition of ‘public benefit foundation’) in Europe with a combined annual expenditure of nearly €60billion.<sup>10</sup> Writing in 2010, Schuyt contended that ‘the potential of modern philanthropy should be used to benefit from the European philanthropic tradition. Philanthropy should be recognized as an economic and societal force with the potential to enhance the vitality of European civil society.’<sup>11</sup> Giving effect to this call to unlock the potential of modern philanthropy within Europe requires a micro-analysis of the European environment for philanthropic action.

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<sup>7</sup> European Foundation Centre, *Working with Foundations in Europe: Why and How*, (Brussels, 2001).

<sup>8</sup> Donor and Foundation Network in Europe, *Report on Public Foundations in Europe 2014*, at 4 (available at <http://dafne-online.eu/wp-content/uploads/2015/09/DAFNE-September-2014.pdf>).

<sup>9</sup> Robert Payton and Michael Moody, *Understanding Philanthropy: Its Mission and Meaning* (Bloomington: Indiana University Press, 2008), 156.

<sup>10</sup> Lawrence T. McGill, *Number of Registered Public Benefit Foundations in Europe Exceeds 147,000* (New York: Foundation Center, 2016) available at <http://dafne-online.eu/wp-content/uploads/2016/10/PBF-Report-2016-9-30-16.pdf>.

<sup>11</sup> Theo Schuyt, “Philanthropy in European welfare states: a challenging promise?” (2010) *International Review of Administrative Sciences* 76(4) 774–789, 786.



## Research Methodology

To this end, EFC and DAFNE jointly commissioned Oonagh B. Breen, Professor of Law at University College Dublin, Ireland to research and write a scoping report on the challenges and opportunities for institutional philanthropy in Europe in 2017 and to make proposals for future areas requiring further comprehensive research to assist these organisations in unlocking the potential for modern philanthropy in Europe in the twenty-first century. In completing this report, Professor Breen was assisted by Hanna Surmatz, EFC, and James Magowan, DAFNE, who provided additional research support and formed the secretariat for this project, facilitating the author's attendance at both the DAFNE Winter Meeting in Berlin in January 2017 and at the Annual General Assembly of the EFC in Warsaw in June 2017.

These meetings provided an opportunity to engage directly with DAFNE and EFC members and to explore first hand their philanthropic space experiences and insights while simultaneously allowing the author to introduce the research project in January and to provide, in close collaboration with James and Hanna, preliminary findings at the June meeting. In conjunction with this research project, DAFNE undertook a consultation survey of its members across Europe to provide empirical accounts of legal and fiscal challenges faced by DAFNE members in the European philanthropic operating environment. The responses to this survey informed this report. Similarly, the EFC Annual General Assembly provided a forum to undertake a number of round table sessions of EFC members focused on releasing philanthropic potential within Europe. These round tables allowed the author to road test and further refine and enrich the report's preliminary findings. A DAFNE/EFC steering group reviewed all of the research findings and provided valuable feedback which has further strengthened the final report.<sup>12</sup>

## Report Structure

Returning to the aforementioned required micro-analysis of the existing European environment for philanthropic action, Chapter 2 begins this process by identifying the Structural Space for Philanthropy within the EU. It examines the lessons learnt from previous European experiences of attempting to create new philanthropic structures to facilitate cross border activities and outlines the contours of the judicially created space for free movement of philanthropic funds within the Common Market. Barriers to institutional philanthropy are discussed in this chapter, an issue which is raised again in Chapter 4. Chapter 3 takes a macro approach to the measurement of the Enabling Space for philanthropy in Europe. It introduces three broad areas relevant to the functioning of philanthropic space, namely – a) legal/regulatory measures; b) fiscal measures; and c) guidance/soft law and explains the place of each of these mechanisms within the EU and maps out their broad interaction with each other.

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<sup>12</sup> The Steering Group comprised: on behalf of DAFNE, Isabel Peñalosa (Spanish Association of Foundations) and Anke Pättsch (German Association of Foundations); and on behalf of EFC, Anja Stanitzke (Volkswagen Stiftung, Germany) and Ludwig Forrest (King Badouin Foundation, Belgium).

Moving from macro to micro-analysis, chapters 4 to 6 respectively takes these areas in turn and explore in more detail their effects on institutional philanthropy in Europe. To this end, Chapter 4 focuses on the international regulatory measures that have impacted the philanthropic space, ranging from the Financial Action Task Force and the implementation of Recommendation 8 and the interrelation of the EU's anti-money laundering directives, to the EU's most recent attempts at supra-national risk assessment and emerging trends in some European countries towards the adoption of foreign agents' laws.

Chapter 5 examines the fiscal measures with a special emphasis on taxation and its impact on the philanthropic space. To this end, the findings from the EFC and TGE *Boosting Cross Border Philanthropy Report 2017* are reviewed.<sup>13</sup> Chapter 6 then assesses the role of soft law and guidance in creating space for philanthropy, reviewing in particular the EU Commission's previous less than successful attempts in this area. Drawing upon the Commission's current attitude towards European institutional philanthropy, the final chapter, Chapter 7, explores possible future policy avenues that may exist to facilitate or stymie philanthropy. It draws together the main themes identified in this report and offers some conclusions on this scoping exercise of the enabling space for philanthropy in Europe while also identifying new horizons for further research.

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<sup>13</sup> EFC and TGE, *Boosting Cross-Border Philanthropy in Europe: Towards a Tax Effective Environment* (Brussels, 2017) [hereinafter, '*Boosting Philanthropy Report*'].

## 2. Outlining the Structural Space for European Philanthropy: Lessons Learnt from Previous Forays

If we are to map the existing space for European philanthropy as a first step towards gauging possible options for enlarging it, we might best begin by exploring the legal infrastructural and structural space for institutional philanthropy in Europe. If one thinks of ‘legal infrastructure’ as the foundation or underlying basis of a system and ‘legal structure’ as the way in which parts are arranged together to form a complex whole, then our starting point in terms of European philanthropic legal infrastructure turns first to the European treaties. Regulation of philanthropy is primarily a matter for national legislators.<sup>14</sup> We look to the European treaties to provide the legal basis for the free movement of philanthropy throughout the common market and to underpin the protection and reasonable regulation of such activity when national legislation interferes with those fundamental freedoms accorded to philanthropic actors. A major difficulty in this regard is the absence of a valid Treaty basis to promulgate non-profit regulation at a European level. The Treaty of Rome, focused as it was on the European Economic Community of the time, provided little by way of affirmative support to non-profit entities and activities. Indeed, Art 58 EEC expressly excluded non-profits organisations from the benefit of the freedom of establishment right,<sup>15</sup> an exclusion which has endured in the Treaty text right up to the present day.<sup>16</sup>

This chapter explores the health of the European enabling legal environment for institutional philanthropy, considering first the Treaty basis for legislation (‘legal infrastructural issues’) before setting out recent unsuccessful forays to create new European legal structures for philanthropic action and explaining the reasons for these past failures. It looks at possible ways forward by reframing the purpose and form of future European legislation and the legal basis perhaps therefore required. Secondly, the chapter turns to the judicial protection.

### Infrastructural Challenges of Regulating for European Philanthropy

It was only with the treaty revisions on foot of the Treaty of Nice in 2001 that formal institutional recognition of civil society occurred for the first time. Art 57 EC saw a change to the composition of the European Economic and Social Committee (EESC) with the charge that the EESC was to comprise “representatives of the various economic and social components of organised civil society.” The space for civil society was further endorsed in the Lisbon Treaty in 2007 when Article 11 TEU provided that “the institutions shall maintain an open, transparent and regular dialogue with representative associations and civil society.” While such treaty changes facilitated greater discussion of participatory

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<sup>14</sup> Across Europe there is a rich culture and tradition of institutional philanthropy in both common law and civil law Member States. The regulatory challenge in the absence of European harmonised laws on philanthropy, which are neither currently sought nor necessarily feasible, is to ensure that in drafting individual regulatory frameworks for institutional philanthropy, national legislators recognise and respect the fundamental freedoms enjoyed by non-profits which are enshrined in the Treaty on the Functioning of the European Union.

<sup>15</sup> Treaty of Rome, Article 58.

<sup>16</sup> Art 54 TFEU.

democracy and civil dialogue, it is arguable that the ill-defined nature of these broad consultation rights did little to change the European infrastructure for the promotion of philanthropy.<sup>17</sup> The problems experienced by public benefit foundations persisted particularly in terms of the common legal and fiscal barriers faced by these entities when engaged in cross-border philanthropy. As the Feasibility Study on a European Foundation Statute Final Report explained,

There are legal barriers to cross-border activities of foundations of the Member States both in civil law and in tax law. As in company law, most of the barriers can be overcome, but this leads to compliance costs which will often be higher than they would be in company law, given that the legal and personal environments vary . . . The calculable cost of barriers against cross-border activities of European foundations ranges from an estimated € 90,000,000 to € 101,700,000 per year. Additionally, there are incalculable costs (costs of foundation seat transfer, costs of reduplication, psychological costs, costs of failure, etc.) which are certainly higher.<sup>18</sup>

One of the major infrastructural challenges faced by policymakers seeking to introduce enabling European legislation for philanthropy is the lack of an apparent specific legal Treaty basis on which to ground such proposals. The default treaty article in such instances is Article 352 TFEU (formerly Art 308 EC). Article 352 might be described as the 'last chance saloon' legal basis when it comes to making EU regulations or directives. It allows the EU to adopt legal measures if action by the Union should prove necessary, within the framework of the policies defined in the Treaties, to attain one of the objectives set out in the Treaties, and the Treaties have not provided the necessary powers.<sup>19</sup> Stepping into this legal vacuum, Article 352 provides the otherwise absent legal basis but this comes at a price of unanimous agreement being required within the Council on the basis of a Commission proposal that has also received the consent of the European Parliament. Promulgation by way of Article 352 is, therefore, demanding. To be adopted, any legislative proposal relying on this article as its legal basis must prove that it has a) the support of the Commission; b) the backing by a majority of the members of the European Parliament; c) an explicit approval of some national parliaments; d) no formal opposition by the other national parliaments and e) the absence of a veto in the European Council.<sup>20</sup>

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<sup>17</sup> Lia CRM Versteegh, "Civil Society under the Treaty of Lisbon: Relationship between National Public Benefit, Organizations and European Union Policy?" (2011) 2(2) *Nonprofit Policy Forum* 4; Acar Kutay, "Limits of Participatory Democracy in European Governance" (2015) 21(6) *European Law Journal*, 803–818; Oonagh B. Breen, "EU Regulation of Charitable Organizations: The Politics of Legally Enabling Civil Society," (2008) 10(3) *International Journal of Not for Profit Law*, 50-79.

<sup>18</sup> Feasibility Study on a European Foundation Statute Final Report (University of Heidelberg, Centre for Social Investment, Max Planck Institute for Comparative and International Private Law, 2009), 1.

<sup>19</sup> Article 352(1) TFEU.

<sup>20</sup> Dominik Hanf, *Adopting a Supranational European Foundation Statute: Which Legal Bases are available to the EU since the entry into force of the Lisbon Treaty?*, Study carried out for the European Foundation Centre (2011), 21.

## Unsuccessful Structural Forays: From European Associations to European Foundations

If one starts from the premise of this less than ideal infrastructure, it is perhaps not so surprising that building new structures reliant on this same infrastructure can be quite challenging. The past thirty years have seen numerous unsuccessful attempts to create new European legal vehicles to facilitate cross-border philanthropy. Amongst those failures have been proposals for the European Association, the European Foundation, and the European Mutual Society (twice). In each of these instances, the process of their adoption has either been officially suspended or interrupted. The common factor shared by all these initiatives, which also led in each case to their downfall, has been the reliance on Art 352 TFEU (or Art 308 EC) as the legal basis for their promulgation.<sup>21</sup>

In 2006, the Commission withdrew its proposals for Regulations on the Statute for a European Association (ESA)<sup>22</sup> and the statute for a European Mutual Society,<sup>23</sup> introduced in 1991, on the overarching grounds that they “were not found to be consistent with the Lisbon and Better Regulation criteria, unlikely to make further progress in the legislative process or found to be no longer topical for objective reasons.”<sup>24</sup> An inability to make legislative progress rather than a lack of stakeholder belief in the merit of the proposals appears to have been the basis for the withdrawal; a view that draws further support from subsequent renewed stakeholder and institutional calls for the subsequent re-introduction of proposals for both regulations.<sup>25</sup>

While efforts to reintroduce proposals for the European Mutual Society and Association were continuing in 2012, momentum was gathering for a new attempt to advance proposals for a European Foundation Statute (EFS). Again, the legal basis for the EFS was grounded in Art 352 TFEU, requiring that the European Parliament be consulted on the proposal and that the European Council unanimously vote in favour of its adoption. The Commission Proposal for the EFS<sup>26</sup> was published in February 2012 and received the required support from the EESC,<sup>27</sup> the Committee of the Regions<sup>28</sup> and the European Parliament.<sup>29</sup> Inability, however, over the following four years to reach unanimous agreement on the

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<sup>21</sup> Article 352(1) TFEU, formerly Art 308 EC. On the importance of the correct legal basis, see Case C-436/03 *European Parliament v Council of the European Union* [2006] ECR I-03733.

<sup>22</sup> COM (1991) 273, OJ C 99, 21.4.1992, 1.

<sup>23</sup> COM (1991) 273, OJ C 99, 21.4.1992, 40.

<sup>24</sup> OJ C 64, 17.3.2006, 3.

<sup>25</sup> See Declaration of the European Parliament of 10 March 2011 on establishing European statutes for mutual societies, associations and foundations (P7\_TA (2011)0101); European Economic and Social Council, *Towards a Statute of the European Association Public Hearing Report*, (28 April 2011, European Economic and Social Committee, Brussels); Luigi Berlinguer, *Own Initiative Report with recommendations to the Commission on the Statute for the European Mutual Society* (European Parliament, A7-0018/2013).

<sup>26</sup> European Commission, *Proposal for a Council Regulation on the Statute for a European Foundation (FE)*, COM(2012) 35 final (Brussels, 8.2.2012).

<sup>27</sup> <http://eur-lex.europa.eu/legal-content/EN/AUTO/?uri=OJ:C:2012:351:TOC>.

<sup>28</sup> <http://eur-lex.europa.eu/legal-content/EN/AUTO/?uri=OJ:C:2013:017:TOC>.

<sup>29</sup> P7\_TA(2013)0293 *Statute for a European Foundation* European Parliament resolution of 2 July 2013 on the proposal for a Council regulation on the Statute for a European Foundation (FE) (COM(2012)0035–2012/0022(APP)).

proposal at Council, despite paring back the privileges to be awarded to the new legal vehicle,<sup>30</sup> resulted in the Commission ultimately withdrawing the proposal in 2015.<sup>31</sup>

### ***Lessons Learnt: The Challenges of Art 352 as the Legal Basis***

What lessons can thus be learnt from the legislative experiences gleaned in the unsuccessful passage attempts to date of the European Association, European Foundation and the European Mutual Society statutes? The first important lesson to note is that while promulgation of regulations based on Art 352 may be difficult, it is not impossible. Council Regulation 1435/03 on the Statute for a European Cooperative Society (SCE)<sup>32</sup> was promulgated on 18 August 2003 with its legal basis grounded on Art 352 TFEU. The European Parliament had challenged the legal basis before the Court of Justice, arguing that the correct legal basis should have been Art 95 EC (today, Art 114 TFEU)<sup>33</sup> rather than then Article 308 EC (today, Art 352 TFEU), as the former would have given the parliament a right of co-decision rather than simply a right of consultation. The Court of Justice, in *European Parliament v Council of the European Union*, following the opinion of Advocate General Stix-Hackl, held that Art 352 was the correct legal basis.<sup>34</sup> Nevertheless, the necessary unanimity was found within the European Council to enable the regulation to be passed. Nevertheless, the necessary unanimity was found within the European Council to enable the regulation to be passed.

Both the Commission and other stakeholders have sought to draw on the successful experience of the SCE's passage in more recent legislative proposal forays. As part of an attempt to introduce a new proposal for a Statute for European Mutual Societies in 2013, the Legal Affairs Committee of the European Parliament commissioned a European Added Value Assessment (EAVA) of the proposed Statute.<sup>35</sup> The EAVA identified evident problems that needed to be tackled by learning from the track record of previous unsuccessful instruments if the Statute for European Mutual Societies (SEMS) was not to suffer a similar fate. It noted:

Among other considerations, creating a legal form which does not exist in some Member States might pose some difficulties, so new company forms should be carefully checked against existing national law so that, on the one hand, the new form is as flexible as national companies, and, on the other, it does not interfere with national

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<sup>30</sup> For further background reading on the fall of the European Foundation Statute see Oonagh B. Breen, "The European Foundation Statute Proposal: Striking the Balance between Supervising and Supporting European Philanthropy?" (2014) 5(1) *Nonprofit Policy Forum*, 5-43; Oonagh B. Breen, "European Non-profit Oversight: The Case for Regulating from the Outside In" (2016) 91(3) *Chicago-Kent Law Review*, 991-1020.

<sup>31</sup> <http://eur-lex.europa.eu/legal-content/EN/AUTO/?uri=OJ:C:2015:080:TOC>.

<sup>32</sup> Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society (SCE) OJ L 207/1 (18 August 2003).

<sup>33</sup> Art 114 TFEU allows the EU to adopt measures 'which has as their object the establishment and functioning of the internal market.' Such measures need to enable or to further facilitate the exercise of economic free movement rights established by the Treaties.

<sup>34</sup> Case 436/03, above, n.21.

<sup>35</sup> European Added Value Assessment (EAVA), *A Statute for European mutual societies: An assessment accompanying the European Parliament's Legislative own-Initiative Report (Rapporteur Luigi Berlinguer MEP)*, PE 494.461 EAVA 1/2013.

arrangements. Similarly, certain areas of law, such as taxation, competition, employee involvement in the decision-making process or intellectual property rights, might conflict with the statute.<sup>36</sup>

Following the European Parliament's adoption of the Berlinguer Report<sup>37</sup> in March 2013, the Commission conducted a public consultation which revealed that not all Governments and stakeholders supported the idea for a specific legal statute to promote the activities of mutual societies across borders.<sup>38</sup> Learning itself from past experiences with the European Private Company Statute and the European Foundation Statute, the Commission concluded in light of this feedback, that there was 'no realistic possibility for the unanimous adoption needed and therefore the Commission does not intend at this stage to initiate such a proposal.'<sup>39</sup>

### ***Alternatives to Art 352: Rethinking the Legal Basis and Mode of Adoption***

Seemingly undaunted by this unwelcoming political environment, the European Parliament's Committee on Legal Affairs recently commissioned a study on *A European Statute for Social and Solidarity-Based Enterprise* to investigate the legislative background at the state level against which any potential EU initiative in social enterprise law should be evaluated. The study published in 2017 provides an overview of the current state of social enterprise (SE) legislation in the EU and compares existing laws in EU Member States before assessing whether a common, European core regulation of SEs exists and exploring the possibility for potential EU legislation on this subject.<sup>40</sup>

In its assessment of whether a feasible legal basis for any such future statute can be found, the study acknowledged "the negative atmosphere that has characterized the debate over the introduction of additional EU legal entities in the last few years", commenting further that this climate "infuses pessimism about the introduction of an EU statute on SEs."<sup>41</sup> The study considered briefly the possibility of an alternative legal basis to Art 352 TFEU, which is currently being explored in relation to the proposed *Societas Unius Personae* (SUP) in company law, in the form of Art 50(2)(f)<sup>42</sup> as perhaps offering a way forward that had not proved possible in the previous instance in which Council unanimity was required under Art 352.<sup>43</sup> Not all institutions are convinced that Art 50 provides the correct legal

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<sup>36</sup> EAVA, n. 35, at 7.

<sup>37</sup> Luigi Berlinguer, Report with recommendations to the Commission on the Statute for a European mutual society 2012/2039(INI), (European Parliament Committee on Legal Affairs, January 28, 2013).

<sup>38</sup> European Parliament resolution of 14 March 2013 with recommendations to the Commission on the Statute for a European mutual society (2012/2039(INL)).

<sup>39</sup> Commission answer to written parliamentary question E-001717-15 on the European Mutual Society (April 15, 2015) available at <http://www.europarl.europa.eu/sides/getAllAnswers.do?reference=E-2015-001717&language=EN>.

<sup>40</sup> Directorate General for Internal Policies, *A European Statute for Social and Solidarity-Based Enterprise: Study for the Juri Committee* (PE 583 123, January 2017).

<sup>41</sup> *Ibid* at 36.

<sup>42</sup> Art 50(2)(f) TFEU allows the European Parliament and Council to act by means of directive to effect 'the progressive abolition of restrictions on freedom of establishment . . . as regards the conditions for setting up agencies, branches or subsidiaries in the territory of a Member State. . . '.

<sup>43</sup> *Ibid*.

basis.<sup>44</sup> Conceding that important differences existed between the SUP and SE, the study nevertheless argued that the SUP proposal remained of interest because it offered a new perspective on how to achieve harmonization of organizational law that could be applied to the SE.<sup>45</sup>

### *Possibilities for using Article 20 TFEU Enhanced Cooperation*

Aside from seeking a different legal basis for European regulations to facilitate philanthropy, another possible option is to leave the legal basis as Art 352 but to use the ‘enhanced cooperation’ mechanism set out in Art 20 TFEU to adopt the regulation instead.<sup>46</sup> The advantage of the enhanced cooperation mechanism is that it overcomes the need for unanimity in Council that is required by Art 352. Measures adopted under the enhanced cooperation framework apply only in the territory of the participating Member States – so one trades off universal application (and the need for unanimity in Council) for more limited territorial reach (with the option of other Member States joining after the fact) based on unanimity amongst only those participating Member States. To be feasible, there must be at least 9 Member States that support the regulation in question.<sup>47</sup> To authorise the use of enhanced cooperation, it must be politically supported by the Commission, approved by a majority vote in the European Parliament and a qualified majority vote in Council. An additional procedural requirement of Art 20.2 is that the Council’s adoption of the authorisation decision must be one of last resort when the Council ‘has established that the objectives cannot be attained within a reasonable period by the Union as a whole.’

Enhanced cooperation has been authorised on two previous occasions - in respect of Council regulations relating to divorce and legal separation<sup>48</sup> and unitary patent protection.<sup>49</sup> A challenge by Spain and Italy to the Council’s use of enhanced cooperation in the case of the unitary patent protection regulation provided the Court of Justice with its first opportunity to interpret the mechanism. It stated:

The expression ‘as a last resort’ highlights the fact that only those situations in which it is impossible to adopt such legislation in the foreseeable future may give rise to the

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<sup>44</sup> See European Economic and Social Committee, Opinion of the EESC on the ‘Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies’ COM(2014) 212 final, 2014/0120 (COD) (2014/C 458/04), at [1.2] stating “The choice of legal basis (Article 50 TFEU) is unconvincing, and appears to be primarily aimed at circumventing the requirement for unanimity in the Council and ensuring that this initiative does not fail as the European private company (SPE) has. The intention may be for SUPs to be formally enshrined in national law as an alternative company form, their essential characteristics are nonetheless clearly defined in supranational law. The legal basis should therefore be Article 352 TFEU.”

<sup>45</sup> Ibid.

<sup>46</sup> This was first suggested by Dominik Hanf, *Adopting a Supranational European Foundation Statute: Which legal bases are available to the EU since the Entry into Force of the Lisbon Treaty?* (European Foundation Centre, 2011). For full discussion, which is beyond the scope of this current paper, on the possible application of Art 20 TEU and its prospective pitfalls see 21-36.

<sup>47</sup> Art 20.2 TEU.

<sup>48</sup> Council Decision 2010/405, OJ 2010 L 189/12, July 12, 2010, implemented by Regulation 1259/2010, OJ L 343/10, 20 December 2010.

<sup>49</sup> Council Decision 2011/167, OJ L 76/53, March 10, 2011, implemented by Regulation 1257/2012, OJ L 361, December 31 2012. In Joined Cases C- C-274/11 and C-295/11 *Spain and Italy v Council*, the Court of Justice dismissed actions brought by Spain and Italy against the Council’s decision authorising enhanced cooperation in the area of the single European patent.



adoption of a decision authorising enhanced cooperation. . . The Council, in taking that final decision [authorising enhanced cooperation], is best placed to determine whether the Member States have demonstrated any willingness to compromise and are in a position to put forward proposals capable of leading to the adoption of legislation for the Union as a whole in the foreseeable future. The Court, in exercising its review of whether the condition that a decision authorising enhanced cooperation must be adopted only as a last resort has been satisfied, should therefore ascertain whether the Council has carefully and impartially examined those aspects that are relevant to this point and whether adequate reasons have been given for the conclusion reached by the Council.<sup>50</sup>

Given the poor record of legislative adoption around philanthropic facilitation, it might be safely said that this latter condition would be met to allow authorisation of the Art 20 procedure. The actual implementation of the subsequent substantive regulation – which would still be enacted on the basis of Art 352 TFEU – would, in the words of Hanf, “necessitate a Council decision resting upon the support of the participating Member States’ representatives only.”<sup>51</sup>

It would be fair to say that the EU treaties have made it difficult to date to develop bespoke legal vehicles to advance philanthropy per se on a pan-European basis. Civil Law and Common Law differences matter when it comes to drafting enabling regulation for philanthropy. Although there is EU level consensus and recognition of the substantial contribution made by institutionalised philanthropy to European goals and the important role played by public benefit foundations in enhancing and facilitating a more active involvement of citizens and civil society in the European project,<sup>52</sup> harnessing that macro consensus and turning it into unanimous agreement on new legal tools to support philanthropy is difficult. The different philanthropic traditions that co-exist across the 28 EU Member States mean that there is no single accepted definition of philanthropy, or legal or reporting structure. Moreover, differences in history and culture, economic and political conditions, and taxation rules between not only common law and civil law member states but also between states of the same legal tradition make the promulgation of non-profit regulation extremely complex and challenging in the absence of a more enabling legal basis than Art 352 currently provides.<sup>53</sup> In this vein, we turn our attention briefly to review the efforts of the European Court of Justice to ensure that in the absence of tailored legislative tools, philanthropic activity is not excluded from the protection of the fundamental freedoms guaranteed by the EU Treaties.

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<sup>50</sup> Joined Cases C- C-274/11 and C–295/11 *Spain and Italy v Council* [52]- [54].

<sup>51</sup> Hanf, n. 46 above, at 37.

<sup>52</sup> European Commission, Proposal for a Council Regulation on the Statute for a European Foundation, COM(2012) 35 final, at [1.1].

<sup>53</sup> See Oonagh B. Breen, “The European Foundation Statute Proposal: Striking the Balance between Supervising and Supporting European Philanthropy?” (2014) 5(1) *Nonprofit Policy Forum*, 5-43.

## European Court of Justice and Rule of Law Mechanisms Aimed at Legally Enabling European Philanthropy at the National Level

More than a decade after the European Court of Justice's seminal judgment in *Stauffer*,<sup>54</sup> recognising the application of the free movement of capital to philanthropic funds, the ECJ has continued its important task of interpreting the fundamental freedoms guaranteed under the European treaties along with ensuring that the principle of non-discrimination on the grounds of nationality applies fully to individuals and public benefit foundations engaged in the support of institutional philanthropy throughout the EU.

In her Opinion in *Stauffer*, Advocate General Stix-Hackl considered the application of the free movement of capital to charitable foundations. Its application, she noted, depended on the extent to which a charitable foundation belongs to the group of persons covered by the free movement of capital. Distinguishing free movement of capital from the freedom of establishment (and the restrictions inherent in Art 54(2) TFEU which focused on the profit-making nature of the individual reliant on the right), the Advocate General found that the free movement of capital is consistent with the nature of this fundamental freedom, which is object-related and not personal. She concluded that the proceedings fell "within the scope *ratione personae* of the free movement of capital irrespective of whether or not the foundation is profit-making within the meaning of [Article 54 TFEU (ex Article 48(2) EC)]."<sup>55</sup>

Building upon this understanding of the law, the Court of Justice in its judgment in *Stauffer* held further that "where a foundation recognised as having charitable status in one Member State also satisfies the requirements imposed for that purpose by the law of another Member State and where its object is to promote the very same interests of the general public, which it is a matter for the national authorities of that other State, including its courts, to determine, the authorities of that Member State cannot deny that foundation the right to equal treatment solely on the ground that it is not established in its territory."<sup>56</sup>

The context for the court's jurisprudence on the treatment of cross-border philanthropy has arisen in a series of cases examining the tax treatment of donors to public benefit entities. The effect of these cases – which include *Hein-Persche*,<sup>57</sup> *Missionswerk*,<sup>58</sup> *Laboratoires Fournier*<sup>59</sup> and *European Commission v Austria*<sup>60</sup> – was summarised in the 2014 EFC/TGE commissioned report on taxation of cross-border philanthropy in Europe: philanthropic activities are protected by the fundamental freedoms enshrined in the Treaty on the Functioning of the EU. The restriction of these freedoms is therefore only

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<sup>54</sup> C-386/04 *Centro di Musicologia Walter Stauffer/Finanzamt München für Körperschaften* [2006] ECR I-8203.

<sup>55</sup> Case C-386/04, Opinion of Advocate General Stix-Hackl, delivered on 15 December 2005, at [61]. Article 48 TEC equates with Article 54 TFEU today.

<sup>56</sup> C-386/04 *Centro di Musicologia Walter Stauffer/Finanzamt München für Körperschaften* [2006] E.C.R. 1-8203, at [40].

<sup>57</sup> C-318/07 *Hein Persche/Finanzamt Lüdenscheid* [2009] ECR I-359.

<sup>58</sup> C-25/10 *Missionswerk Werner Heukelbach eV/Belgien* [2011] 2 C.M.L.R. 35.

<sup>59</sup> C-39/04 *Laboratoires Fournier SA/Direction des vérifications nationales et internationales* [2005] ECR I-2057.

<sup>60</sup> C-10/10 *Commission/Austria* [2011] 3 C.M.L.R. 26.

justifiable and proportionate if the foreign [public benefit organisation] is not comparable to a domestic one; a blanket discrimination is not permissible.<sup>61</sup>

The procedural effect of these rulings has been two-fold. From a European institutional perspective, the European Commission has taken (and continues to take) infringement procedures against Member States in cases in which the national tax legislation has discriminated against donors and public benefit organisations.<sup>62</sup> Starting with a formal request to a Member State to change its legislation to end discrimination against foreign EU-based philanthropic organisations, the Commission can elevate the matter to an infringement procedure before the Court of Justice if a Member State fails to cooperate. The geographic spread of the Commission's requests for legislative change to infringing member states demonstrates the widespread nature of the problem being tackled by the Commission.<sup>63</sup>

From a national perspective, Member States are under an obligation to engage in a comparability test to ensure that treatment of foreign EU-based philanthropic organisations is not discriminatory when compared with the treatment of domestic organisations. In practice, Member States have each adopted their own approaches to comparability, as they are permitted to do under *Hein-Persche*, which provided that within the framework of the comparability test the competent national authorities could require the foreign philanthropic organisation, and/or as relevant its donors, to provide any documentation the authorities deemed useful for the carrying out of the comparability test.<sup>64</sup> The practical implications of these diverse approaches and possible ways to alleviate the administrative burden on claimant philanthropic organisations while simultaneously respecting national sovereignty on matters of taxation will be explored further in Chapter 5.

Thus, from a functional perspective, it might be said that the ongoing work of the European Commission through its infringement proceedings and the judicial decisions of the European Court of Justice have begun to build a scaffolding of rights upon which philanthropic organisations can rely. The difficulty with this incremental approach is that the resulting structure depends greatly upon the will of the interpreting Member State to assist such organisations. Whereas one Member State may operate a system within which philanthropic organisations may exercise their rights, including engagement in cross border philanthropy, resulting in no discrimination between national and non-national EU based organisations by facilitating comparability claims, another Member State may employ an opaque, oblique or an

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<sup>61</sup> Thomas von Hippel, *Taxation of Cross-Border Philanthropy in Europe after Persche and Stauffer: From landlock to free movement?* (EFC/TGE, 2014), at 13. The report, at 13, summarised the relevant rules as stating that, "It is not permitted that foreign EU-based PBOs and their donors are excluded from eligibility for tax privileges if, seat aside, they fulfil all requirements of the national public-benefit tax law. It is not permitted that a (domestic or foreign EU based) PBO is required to undertake its philanthropic activities in the Member State which grants the tax privilege, unless there are compelling objective reasons for this. . . . It is necessary in cross-border cases that Member States carry out a comparability test to determine whether or not a foreign EU-based PBO meets the requirements of national tax law. Such tests are to be carried out by the national authorities and courts of the Member State concerned."

<sup>62</sup> Von Hippel, n. 61 above, at 21 noting that in 2014 28 cases taken by the Commission were successfully closed due to changes made to national legislation.

<sup>63</sup> Germany, Poland, UK, Netherlands, Greece, Italy, Spain, Belgium, Austria, Ireland.

<sup>64</sup> *Hein-Persche*, n. 57 above, [53]-[58].

expressly onerous set of criteria for determining comparability, the effect of which is to restrict the fundamental freedoms of the non-domestic philanthropic organisations. The burden of proving discrimination in such cases ultimately resides with the claimant organisation since it must prove that it is comparable to the domestic organisation under whatever test is prescribed by the host member state or prove that the host member state is engaging in blanket discrimination against foreign EU-based organisations.

In the context of the debate on the shrinking space for civil society, in some countries it is not only NGOs, but also their donors and other philanthropic actors that have faced more difficult conditions. These obstacles take many forms, ranging from restrictive foreign funding legislation, changes in tax laws, additional administrative burdens (substantially increasing the cost of making a grant and the time required to process it) as well as difficulties in cross-border financial flows, caused by ongoing incidences of bank de-risking, even within the EU. The practical effects of these obstacles are that smaller grants become so cost prohibitive that they will no longer be made, edging out smaller foundations from international grant-making. Even for those larger foundations that can comply, philanthropic momentum can be lost.<sup>65</sup>

In the 2016 Civic Space in Europe Survey,<sup>66</sup> the key question explored was whether civil society organisations felt that their rights are being eroded. The survey sought to draw out some initial perceptions of civil society leaders in Europe as part of a wider global process to understand and analyse the changes that are taking place in many countries. With a response rate of 300 partial replies and 180 complete responses with every EU member state represented, a notable trend was the substantive differences in response between Eastern and Western Europe, demonstrating the more challenging environment that currently exists in the former for both civic and philanthropic space to flourish.

	<b>Western Europe</b>	<b>Eastern Europe</b>
<b>Confidence in freedom of association rights</b>	90%	60%
<b>Confidence in freedom of expression</b>	70%	55%
<b>Confidence in State's duty to protect civil society</b>	60%	30%
<b>State financial support for civil society<sup>67</sup></b>	43%	27%

<sup>65</sup> On this note, see Mary A. Gailbreath, "Closing space for civil society creates new challenges for international grantmakers" in *The Shrinking Space for Civil Society: philanthropic perspectives from across the globe* (EFC, 2016), 45.

<sup>66</sup> Civil Society Europe and Civicus, *Civic Space in Europe Survey* (2016).

<sup>67</sup> The Survey further breaks down the data relating to assessment of the current situation of financial support for civil society in each country. In Western Europe, the average was 43% and in North Western Europe it was even lower, at only 37%. In Central & Eastern Europe 27%, while in Southern and Eastern Europe only 22%.

The reduction in funding across the board for civil society initiatives was a cause of concern to many respondents across Europe – counting as the greatest concern for one third of respondents - with indications that this reduction had “led to a real drop in support to maintaining the enabling environment.”<sup>68</sup> Building on this, the Survey noted:

Surveillance and counter-terrorism measures also feature relatively high in the responses, suggesting that these practices have an increasing impact on CSOs and are often combined with funding restrictions against organisations that find themselves under scrutiny. Contract conditionality was also rated as a relatively high concern. Restrictions within contracts can limit the capacity of associations to bring the voice of citizens into decision-making as well as providing their expertise based on access to key citizens.<sup>69</sup>

The Survey, noting the responsibility and role of the EU in this space, called upon the EU along with national governments to support (including through adequate resources) the independent functioning and sustainability of civil society organisations. Notwithstanding the varying degrees of difficulty experienced by civil society organisations relating to their state of establishment, an overwhelming majority of respondents considered that cross-border European collaboration was important for the effective operation of CSOs.<sup>70</sup> A further interesting finding in the survey was the strong support among all respondents (but particularly Eastern Europeans) for the EU to do more to guarantee and promote civic space in their countries.<sup>71</sup> Thus, it can be seen from the survey that free-flow of philanthropic funds is a concern to many philanthropic organisations whether this takes the form of new State obstacles to the movement of an organisation’s own funds or a more general reduction in state funding to civil society, making the need ever greater for more philanthropic involvement and an enabling legal environment to facilitate such input.<sup>72</sup>

## What Space Exists to Protect Civil Society Within the Emerging Framework on the Rule of Law

If the structural space for institutional philanthropy is but an aspect of the larger structural space for civil society, briefly identifying the current policy approach of the European Commission to protecting civil society within the emerging framework on the rule of law may provide some indication of the EU’s policy agenda more broadly.

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<sup>68</sup> *Civic Space in Europe Survey*, n. 66, at 9.

<sup>69</sup> *Ibid*, at 11.

<sup>70</sup> 89.5% rated cross border collaboration as important for effective CSO operation with 34.1% agreeing strongly.

<sup>71</sup> *Civic Space in Europe Survey*, n.66 above, 16-17 (noting 66.4% (69.9 % in Eastern Europe) in favour of greater EU involvement, “Comments point to a lack of clarity, and visibility of EU action in guaranteeing and promoting civic space, in particular as regards addressing breaches of the rule of law, democracy and fundamental rights in Member States.”)

<sup>72</sup> See further, *Challenging the Closing Space for Civil Society: A Practical Starting Point for Funders* (ARIADNE, EFC and International Human Rights Funder Group, 2016).

In contrast to the EU's external policies which have been acknowledged as providing a 'good declaratory framework' around civil society space with strong articulations of the EU's reasoning about the value of civil society and why it is important to protect it,<sup>73</sup> when it comes to the EU's internal policies on protecting civic space, the EU's framework is far less well developed. The policy framework and policy tools that exist in the context of external relations are lacking, leaving the EU "very ill-equipped" to tackle restrictions on civil society space within the Union. Those tools that do exist are five-fold and comprise:

- a) Article 7 of the Treaty on European Union (TEU);
- b) The Commission Framework to strengthen the rule of law;
- c) The Council's Rule of Law Dialogue; and
- d) Recent calls for a new binding EU mechanism to monitor the state of democracy, rule of law and fundamental rights in the member states.
- e) Commission Infringement Procedures for breach of Treaty obligations

**a) Article 7 of the Treaty on European Union (TEU)**

Article 7 is often referred to as the 'nuclear option' as it grants the EU Member States and EU institutions, acting together, the legal means to withdraw membership rights from a Member State whenever a Member State acts in contravention of the values of Article 2 TEU such as freedom, democracy and rule of law. The procedure may be applied regardless of whether the action occurs within the field of EU law or merely in an area of national competence. The mechanism for invoking Article 7, however, is complex and unlike the judicially-governed infringement procedures of Article 258 TFEU, Article 7 TEU procedures have never been tested in practice, making it an unlikely vehicle for protecting civic space or indeed institutional philanthropic space within the EU.

**b) The Commission Framework to strengthen the rule of law**

In March 2014, the Commission adopted a new framework for addressing systemic threats to the rule of law in any of the EU's 28 Member States.<sup>74</sup> Focusing on systemic threats to the rule of law, this new framework is complementary to the existing infringement procedures - when EU law has been breached – and to the Article 7 procedure, outlined above. In essence, the Rule of Law framework establishes an early warning tool allowing the Commission to enter into a dialogue with the Member State concerned to prevent the escalation of systemic threats to the rule of law. If no solution is found within the new EU rule of law framework, Article 7 remains the last resort to resolve a crisis and ensure compliance with European Union values. Comprising a three-stage process beginning with a Commission assessment ('a rule of law opinion'), followed by a Commission recommendation, and then a final stage of Commission monitoring of implementation leading to any 'follow up recommendation'. The Commission has exercised its powers under the framework to open dialogue with Poland and to

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<sup>73</sup> See, e.g., Directorate-General For External Policies Policy Department, *Shrinking space for civil society: the EU response* (European Parliament, April 2017, PE578.039).

<sup>74</sup> See Communication "A new EU Framework to Strengthen the Rule of Law", COM(2014) 158 final. See also [http://europa.eu/rapid/press-release\\_IP-14-237\\_en.htm](http://europa.eu/rapid/press-release_IP-14-237_en.htm).

issue rule of law recommendations in 2016 and 2017 in relation to events concerning its Constitutional Court.<sup>75</sup>

**c) *The Council's Rule of Law Dialogue***

The conclusions of the Council and the Member States of December 2014 on ensuring respect for the rule of law established an annual rule of law dialogue and foresee possible thematic debates in the Council (General Affairs) to promote and safeguard rule of law in the framework of the Treaties as one of the key values on which the Union is based.<sup>76</sup> Dialogues to date have considered issues ranging from internet security to migration integration and fundamental rights.

**d) *Recent calls for a new binding EU mechanism to monitor the state of democracy, rule of law and fundamental rights in the member states***

In October 2016, the European Parliament adopted a resolution containing recommendations to the Commission on the establishment of an EU mechanism on democracy, the rule of law and fundamental rights ('DRF').<sup>77</sup> The Parliament called for an EU Pact for DRF that would: (i) be evidence based; (ii) be objective and not subject to outside influence, in particular political influence, non-discriminatory and assessing on an equal footing; (iii) respect the principle of subsidiarity, necessity and proportionality; (iv) address both Member States and institutions of the Union; and (v) be based on a graduated approach, including both a preventative and corrective arm. The Parliament sought that the Pact for DRF include all relevant actors (including civil society representatives) and consist of:

- an annual report on democracy, the rule of law and fundamental rights ('European DRF Report') with country-specific recommendations incorporating the reporting done by the European Union Agency for Fundamental Rights (FRA), the Council of Europe, and other relevant authorities in the field;
- an annual inter-parliamentary debate based on the European DRF Report,
- arrangements for remedying possible risks and breaches, as provided for by the Treaties, including the activation of the preventative or corrective arms of Article 7 TEU,
- a DRF Policy Cycle within the Union institutions.

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<sup>75</sup> See Commission Opinion on the Rule of Law in Poland (June 1, 2016) at [http://europa.eu/rapid/press-release\\_MEMO-16-2017\\_en.htm](http://europa.eu/rapid/press-release_MEMO-16-2017_en.htm); Commission Recommendation (EU) 2016/1374 regarding the Rule of Law in Poland (July 27, 2016) at [http://europa.eu/rapid/press-release\\_MEMO-16-2644\\_en.htm](http://europa.eu/rapid/press-release_MEMO-16-2644_en.htm) and Commission complementary recommendation (December 21, 2016) at [http://ec.europa.eu/newsroom/document.cfm?doc\\_id=40988](http://ec.europa.eu/newsroom/document.cfm?doc_id=40988). See also, Commission Recommendation of 26.7.2017 regarding the rule of law in Poland, C(2017) 5320 final at [http://ec.europa.eu/newsroom/document.cfm?doc\\_id=46116](http://ec.europa.eu/newsroom/document.cfm?doc_id=46116).

<sup>76</sup> See First Council Rule of Law Dialogue - General Affairs Council, Ensuring the respect for the rule of law - Dialogue and exchange of views on internet security, 17 November 2015, doc. 13744/15. Second Council Rule of Law Dialogue on Migration (May 2016) <http://data.consilium.europa.eu/doc/document/ST-8774-2016-INIT/en/pdf>.

<sup>77</sup> European Parliament, Recommendations to the Commission on an EU mechanism on democracy, the rule of law and fundamental rights (P8\_TA-PROV (2016) 0409) <http://www.europarl.europa.eu/sides/getDoc.do?type=TA&language=EN&reference=P8-TA-2016-0409>.

The Commission's response, while fully supportive of the objective underlying the resolution, expressed serious doubts about the need and the feasibility of an annual Report and a policy cycle on democracy, the rule of law and fundamental rights prepared by a committee of "experts" and about the need for, feasibility and added value of an inter-institutional agreement on this matter.<sup>78</sup>

#### **e) Commission Infringement Procedures**

It remains open to the Commission to initiate an infringement procedure under Article 258 TFEU against any Member State that fails to fulfil an obligation under the Treaties (including the contravention of the fundamental freedoms guaranteed to EU citizens). The Commission has used this enforcement power in the past in the wake of the *Stauffer* and *Hein Persche* rulings to compel other Member States to reform tax laws and practices that conflicted with the principle of non-discrimination. In practical terms, the use of infringement proceedings and European Court's jurisprudence which ensues has been one of the more effective ways of the five discussed here to protect philanthropic space in the EU.

### Satellite Structures and Related Protection Mechanisms

Aside from EU institutions, a number of European satellite structures play an important role in protecting human rights and fundamental freedoms in Europe and thus are relevant to our mapping of the legal infrastructure that exists to protect both European civic and philanthropic space. The role of the Council of Europe (through the European Court of Human Rights, the Venice Commission and the Conference of INGOs) and that of the Organisation for Security and Cooperation in Europe (through its Office for Democratic Institutions and Human Rights) are briefly explained below.

#### **The Council of Europe**

Founded in 1949, the Council of Europe is an international organisation of which the stated aim is to uphold human rights, democracy, rule of law in Europe and promote European culture. The Council of Europe is responsible for the 1986 Convention on the Recognition of the Legal Personality of International NGOs,<sup>79</sup> under which the contracting states agree to recognize, "as a right", legal personality and capacity as acquired in the state where a non-profit organization with aims of international utility has its statutory offices. The Council of Europe's experience in terms of ratification rate, coverage, value and enforcement of such an international convention could be a matter for further research when it comes to finding European structures to enable institutional philanthropy.

Three institutions merit mention in the context of the infrastructural framework for the protection of European philanthropic space in this regard, namely the European Court of Human Rights, the Venice Commission and the Conference of INGO's Expert Council on NGO Law.

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<sup>78</sup> European Commission, Follow-up to the European Parliament resolution on with recommendations to the Commission on the establishment of an EU mechanism on democracy, the rule of law and fundamental rights, adopted by the Commission on 17 January 2017, at <http://www.europarl.europa.eu/oeil/spdoc.do?i=27630&j=0&l=en>.

<sup>79</sup> See <http://www.coe.int/en/web/conventions/full-list/-/conventions/rms/090000168007a67c>.



## *The European Court of Human Rights*

The best-known body of the Council of Europe is the European Court of Human Rights, which enforces the European Convention on Human Rights.<sup>80</sup> Ample jurisprudence of the European Court of Human Rights indicates that, apart from individual citizens, NGOs enjoy rights protected under the ECHR,<sup>81</sup> and like individual applicants, NGOs may also bring their cases directly before the Court.

## *The Venice Commission*

The European Commission for Democracy through Law - known as the Venice Commission - is the Council of Europe's advisory body on constitutional matters.<sup>82</sup> Established in 1990, the role of the Venice Commission is to provide legal advice to its member states and to help states wishing to bring their legal and institutional structures into line with European standards and international experience in the fields of democracy, human rights and the rule of law. It also helps to ensure the dissemination and consolidation of a common constitutional heritage, playing a unique role in conflict management, and provides “emergency constitutional aid” to states in transition. The Commission has 61 member states: the 47 Council of Europe member states, plus 14 other countries.

The Venice Commission has issued several important opinions and studies around country specific developments that impact on philanthropic space in the context of freedoms of assembly, association and freedom to receive funding.<sup>83</sup> The Commission does not seek to impose the solutions set out in its opinions. Rather, it adopts a non-directive approach based on dialogue and shares member states' experience and practices. For this reason, a working group visits the country concerned to meet the various stakeholders and to assess the situation as objectively as possible. In this regard, representatives of the Venice Commission visited Poland in May 2107 to participate in the meeting of the OSCE-ODIHR Panel on freedom of peaceful assembly and to discuss assembly "monitoring"

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<sup>80</sup> See <http://www.echr.coe.int/>.

<sup>81</sup> In this regard, the ECHR is distinguishable from the International Covenant on Civil and Political Rights, as the ICCPR does not contain enforceable rights for NGOs. See further, Erik Denters and Wino J.M. van Veen, “Voluntary Organizations in Europe: The European Convention on Human Rights” (1998) 1(2) *International Journal for Not-for-Profit Law*. Note, however, UN Human Rights Council Resolutions on Civil Society Space (Resolution 7/31 of 26 September 2014 and 24/21 of 27 September 2013, on civil society space and A/HRC/32/L.29 of 27 June 2016) calling upon States to “ensure that domestic provisions on funding to civil society actors are in compliance with their international human rights obligations and commitments and are not misused to hinder the work or endanger the safety of civil society actors, and underlines the importance of the ability to solicit, receive and utilize resources for their work.”

<sup>82</sup> See <http://www.venice.coe.int/>. The Commission's individual membership comprises university professors of public and international law, supreme and constitutional court judges, members of national parliaments and civil servants.

<sup>83</sup> CDL-REF(2017)025 on Hungary - Draft Law on the Transparency of Organisations Receiving Foreign Funds and Reasoning; CDL(2014)059, Draft Joint Guidelines on Freedom of Association by the Venice Commission and the OSCE/ODIHR CDL-PI(2014)004 Compilation of Venice Commission Opinions concerning Freedom of Association (revised July 2014); and CDL-AD(2014)025 Opinion on Federal Law n. 121-fz on non-commercial organisations (“law on foreign agents”), on Federal Laws n. 18-fz and n. 147-fz and on Federal Law n. 190-fz on making amendments to the criminal code (“law on treason”) of the Russian Federation.

(including the issue of the safety of journalists covering assemblies) and the role of municipalities in facilitating assemblies.<sup>84</sup>

Requested by the Parliamentary Assembly of the Council of Europe to deliver an opinion on Hungary's then draft Law on the transparency of organisations receiving support from abroad in April 2017, the Venice Commission issued a Preliminary Opinion and a subsequent clarifying opinion in June 2017, which are further discussed in Chapter 4.<sup>85</sup>

### ***The Expert Council on NGO Law***

Finally with regard to the Council of Europe, the Expert Council on NGO Law, established by the Conference of INGOs of the Council of Europe in 2008, carries out thematic and country studies on specific aspects of NGO legislation and its implementation that seem to pose problems of conformity with international standards, notably the European Convention on Human Rights and Recommendation (2007)14 on the legal status of NGOs in Europe.<sup>86</sup> Its work covers the 47 member countries of the Council of Europe and Belarus and its aim is to create an enabling environment for NGOs through examining national NGO legislation and its implementation.<sup>87</sup> Recent studies of the Expert Council include its 2015 report on Non-Governmental Organisations: Review of Developments in Standards, Mechanisms and Case Law 2013-2015<sup>88</sup> and its holding that same year of a roundtable on protecting civic space with the participation of Council of Europe representatives.<sup>89</sup> Recent legal opinions of the Expert Council include those relating to Hungary's draft Law on the transparency of organisations receiving support from abroad.<sup>90</sup>

### ***The Organisation for Security and Cooperation in Europe (OSCE)***

With 57 member states in Europe, Asia and North American, the OSCE is the world's largest regional security organisation which seeks to prevent conflict, foster economic development and promote full respect for human rights and fundamental freedoms. Charged with this last mission, the OSCE Office for Democratic Institutions and Human Rights (ODIHR), based in Warsaw, provides support, assistance

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<sup>84</sup> <http://www.venice.coe.int/webforms/events/?id=2404>.

<sup>85</sup> Venice Commission, Preliminary Opinion on the Draft Hungarian Law on the Transparency of Organisations receiving support from abroad, (June 2, Opinion 889/2017) available at [http://www.venice.coe.int/webforms/documents/?pdf=CDL-PI\(2017\)002-e](http://www.venice.coe.int/webforms/documents/?pdf=CDL-PI(2017)002-e); Venice Commission, Opinion on the Draft Hungarian Law on the Transparency of Organisations receiving support from abroad, (June 19, Opinion 889/2017) available at [http://www.venice.coe.int/webforms/documents/?pdf=CDL-AD\(2017\)015-e](http://www.venice.coe.int/webforms/documents/?pdf=CDL-AD(2017)015-e).

<sup>86</sup> <http://www.coe.int/en/web/ingo/expert-council>.

<sup>87</sup> See Oonagh B. Breen, "Through the Looking Glass: European Perspectives on Non-Profit Vulnerability, Legitimacy and Regulation" (2011) 36(3) *Brooklyn Journal of International Law*, 948-991, 989.

<sup>88</sup> OING CONF/EXP, Non-Governmental Organisations: Review of Developments in Standards, Mechanisms and Case Law 2013-2015 (November 2, 2015) at <http://rm.coe.int/CoERMPublicCommonSearchServices/DisplayDCTMContent?documentId=0900001680492965>.

<sup>89</sup> Meeting of The Expert Council on NGO Law of The Conference of International Non-Governmental Organisations of The Council of Europe, Strasbourg, 28 -29 September 2015.

<sup>90</sup> Expert Council on NGO Law Opinion on The Hungarian Draft Act on the Transparency of Organisations Supported from Abroad, April 2017, available at <https://rm.coe.int/CoERMPublicCommonSearchServices/DisplayDCTMContent?documentId=090000168070bfb>

and expertise to participating States and civil society to promote democracy, rule of law, human rights and tolerance and non-discrimination. In response to a request by Poland to the ODIHR to review its draft Act on The National Freedom Institute - Centre for the Development of Civil Society, the ODIHR issued its legal opinion in August 2017<sup>91</sup> in which it expressed its concern that the draft Act's proposed new civil society development scheme should not lead to a situation where, in practice, the responsibility of distributing the great majority of public funds or resources to civil society organizations would be assigned to just one executive entity, an opinion shared by the Council of Europe's Conference of INGOs.<sup>92</sup>

### Further Avenues for Exploration – Alternative Philanthropic Models of the Future?

In scoping the future of philanthropy in Europe, one cannot ignore the need to further explore and better understand the potential and, equally, the limitations of emerging forms of venture philanthropy and social investment to provide new tools for facilitating philanthropic growth and outreach in Europe. While mapping the current state of use and future potential of these innovative and experimental methods to create a wider operating space for philanthropy in Europe and considering how national or European policy measures might further support these aims are beyond the scope of this report, it is important to horizon scan where future research might usefully be carried out.

In 2017, the European Commission created an Expert Group on Venture Philanthropy and Social Investments to analyse the different forms that foundations, venture philanthropist and social investors' involvement could take in order to contribute to Horizon 2020 and Europe 2020 policy priorities, in particular those fostering a smart, sustainable and inclusive growth through research and innovation activities.<sup>93</sup> Social investment (also known as 'social impact investment') is an investment that intentionally targets specific social objectives along with a financial return and measures the achievement of both. Venture philanthropy is a type of impact investment that takes concepts and techniques from venture capital finance and business management and applies them to achieving philanthropic goals.<sup>94</sup> Venture philanthropists (foundations being only one of the actors in this context) use a wide range of financing mechanisms (ranging from, but not limited to, grants, debt, equity hybrid financing, direct loans, and loan guarantees) tailored to the specific needs of the supported organisation in addition to supplying organisational support.

While for the majority of European foundations asset administration, on the one hand, and grantmaking/operational activities, on the other, are two separately contained areas of activity, more

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<sup>91</sup> See legal opinion (n° NGO-POL/303/2017 [AIC]) of OSCE/ODIHR on the draft Act on the National Freedom Institute - Centre for the Development of Civil Society <http://www.osce.org/odihr/336546?download=true>.

<sup>92</sup> Following the publication of the OSCE/ODIHR legal opinion on the draft Polish Act, the Conference of INGOs reiterated its concern in a letter to the Polish authorities <https://www.coe.int/en/web/ingo/-/communique-by-the-president-of-the-conference-of-ingos-and-of-the-president-of-the-expert-council-on-ngo-law>.

<sup>93</sup> <http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetail&groupID=3495>.

<sup>94</sup> More information on venture philanthropy can be accessed from the European Venture Philanthropy Association at <https://evpa.eu.com/about-us/what-is-venture-philanthropy>.

and more foundations have begun to consider how asset administration might, at least to some extent, be linked to philanthropic mission and/or be supporting start-ups/social enterprises in the form of social impact investments. Low interest rates have also led to attempts to create more impact with mission linked or social investments.<sup>95</sup> Originating in the United States, the concept of programme related investment facilitates foundations in legally setting aside the stricture of maximum return on investments in order to invest in projects with important social goals.<sup>96</sup>

Given that some national laws require a preservation of the value of the endowment<sup>97</sup> – and mission related investment or investment in social enterprises do not always generate the required returns (or are considered too risky investments) – and some national laws do not permit the giving of loans by charities,<sup>98</sup> barriers to this type of investment exist in some countries.<sup>99</sup> The EFC is currently conducting a thorough review of how its members invest their assets while several of DAFNE’s members have also carried out research on the practice and policy of asset impact investment.<sup>100</sup> Further comprehensive research is warranted in this area.

To this end, as part of the joint EFC/DAFNE session on ‘Releasing philanthropic potential – Constraints and opportunities in the operating environment’ at the EFC 2017 Annual General Assembly, EFC and DAFNE convened a roundtable to discuss the potential of venture philanthropy/social investment as a tool to enlarge the space for philanthropy. Some of the main findings of this roundtable inform the calls in this chapter to prompt future research to explore the feasibility of this new tool. Apart from the asset

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<sup>95</sup> See, for instance, the website of the German Foundations Association, <https://www.stiftungen.org/stiftungen/basiswissen-stiftungen/stiftungsvermoege/kapital-wirkung.html>, noting the potential for ‘intelligent investment’ as a way to overcome low interest rates.

<sup>96</sup> First statutorily defined in the US in 1969; see US Tax Reform Act 1969, s.4944, under which private foundations are allowed to make ‘program-related investments’ if: a) the primary purpose of the investment is to advance the foundation’s charitable objectives; b) neither the production of income nor appreciation of property is the primary purpose; and c) the funds cannot be used directly or indirectly to lobby or for political purposes. PRIs can result in a market rate of return or above as long as they comply with the Internal Revenue Service rules.

<sup>97</sup> National laws require foundations to maintain their capital in the following jurisdictions - Croatia, Czech Republic, Germany, Slovakia and Spain and also in Lithuania (in respect of endowment only). See further, EFC, *Comparative Highlights of Foundation Laws: The Operating Environment for Foundations in Europe* (Brussels, 2015) at 17-19. In Germany, most Länder laws currently include rules that the value of the endowment is to be kept and there are currently proposals made to include this also in the Civil Code, see Angelo Winkler “Die BGB-Stiftungsrechtsreform – eine Zwischenbilanz” in ZStV 5/2017, at 168.

<sup>98</sup> In Italy, for instance, recoverable grants, low-interest loans, and equities, as well as forward purchase of shareholding or other kind of contributions to third parties, are activities assigned to banks and financial intermediaries by the “Bank Law” (Decree no. 385/1993); an explicit prohibition is stipulated for foundations of banking origin by Article 3, para. 2 of Decree no.153/99. See further, *EFC Legal and Fiscal Country Profile, 2014: Italy*, at 10 (available at <http://www.efc.be/wp-content/uploads/2015/05/Italy-2014.pdf>). Similarly, foundations in the Czech Republic are not legally allowed to allocate grant funds towards furthering their public benefit purpose/programmes which can also generate income. See *EFC Legal and Fiscal Country Profile, 2014: Czech Republic*, at 16 (available at <http://www.efc.be/wp-content/uploads/2015/05/Czech-Republic-2014.pdf>).

<sup>99</sup> Several countries have, however, introduced measures supporting social investments. See, e.g., new UK tax relief measures in the Finance (No. 2) Bill 2017, clause 27, Schedule 8 that offer individual investors a tax reduction of 30% of the value of qualifying investments in social enterprises.

<sup>100</sup> See, e.g., the German Association of Foundations’ case studies on mission related investment at: <https://www.stiftungen.org/stiftungen/stiftungsmanagement/stiftungsvermoege/kapital-wirkung.html>

administration side, it was noted that philanthropic organisations are also making grants, loans and other financial support as well as organisational support (through developing skills or improving processes) to social or green businesses. Some national laws, however, do not allow for the “programmatic” side to generate returns or may only permit expenditure of charitable assets on charitable purposes which will not always coincide with the broader work undertaken by social enterprise recipients.<sup>101</sup> Hence barriers to some of these engagements (e.g. if loans are given on the grant-making side) were reported in some countries.<sup>102</sup>

A series of EU regulations aim to support social entrepreneurship,<sup>103</sup> and an Expert Group on Social Entrepreneurship established by the Commission to examine the progress of measures improving access to finance for social enterprises, enhancing their visibility and optimising their legal environment reported delivered its findings in 2016.<sup>104</sup> In May 2017, the EU agreed to do more to stimulate venture capital investment in, inter alia, social enterprises, by agreeing reforms to expand investment possibilities for funds, broaden the range of eligible managers and simplify administration which in turn will help investor capital reach the bodies, such as social enterprises that need it.<sup>105</sup> Thus, research scope exists to scrutinise the opportunities and challenges for philanthropic engagement in both venture philanthropy and social impact investments at national and European level.

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<sup>101</sup> Spanish foundations, e.g., can only allocate funds towards the aim of the foundation or complementary to it and any profits generated have to be reinvested in the pursuit of the purposes of the organisation (*EFC Legal and Fiscal Country Profile, 2014: Spain*, at 8).

<sup>102</sup> It is worth noting that in its early years of Program Related Investment, the Ford Foundation – an early adopter of the concept – did not integrate its PRI activity (conceived as an investment activity) with the foundation’s grants program.

<sup>103</sup> See, e.g., the Regulation 346/2013 on European Social Entrepreneurship Funds (EUSEF), which came into force in July 2013 and covers alternative investment schemes that focus on social enterprises, i.e., companies that are set up with the explicit aim of having a positive social impact and addressing social objectives, rather than only maximising profit.

<sup>104</sup> Commission Expert Group on Social Entrepreneurship (GECES), *Social enterprises and the social economy going forward: A call for action* (October 2016), available at <https://ec.europa.eu/docsroom/documents/24501/attachments/1/translations/en/renditions/native>.

<sup>105</sup> See Commission Press Release, Capital Markets Union: EU agrees to more support for venture capital and social enterprises (Brussels, 30 May 2017), IP/17/1477 available at [http://europa.eu/rapid/press-release\\_IP-17-1477\\_en.htm?locale=en](http://europa.eu/rapid/press-release_IP-17-1477_en.htm?locale=en).

### 3. Making Sense of the Enabling Space for Philanthropy in Europe

Given the legal infrastructural and structure context described in Chapter 2, it is important to think broadly as to the possible tools available to those who wish to protect or enlarge upon the existing space for philanthropy in Europe. Three different tools, all relevant to cross-border philanthropy, will be considered in the following chapters. When we think of the enabling space for philanthropy, three types of regulation deserve specific attention, namely the role of legal regulation in the area of anti-money laundering and terrorist financing, which occurs at both EU and national levels, the separate role of fiscal regulation in the form of tax laws, as the right to pass these laws is reserved to the Member States and finally, the place of codes of conduct, administrative guidelines, best practice guidelines and other types of soft law that shape the space within which philanthropy functions. Each of these areas has its own distinct characteristics and thus deserves individual attention over the coming chapters. Nevertheless, all three areas are interlinked and inform each other in practice – hence the need to take a holistic approach to regulation in seeking to better understand the existing space for philanthropy within Europe and the potential to enlarge it.

Turning first to the regulations that emerge to counter money laundering and terrorist financing concerns. The regulations in question here spring from political commitments at international level rather than binding EU Treaty obligations. They have, however, taken effect at national, regional and EU level in the more traditionally binding regulatory sense, informing national regulatory and administrative practices as well as being the subject matter of EU Directives on Anti-Money Laundering. The growth of FATF regulation in this area with the recent emergence of the EU's Supra-National Risk Assessment merits special consideration in this context, given its potential to impact on cross-border philanthropic capital flows. Closer to home, the recent flurry of restrictive Eastern European regulation aimed at foundations and associations (particularly in Hungary) on the pretext of countering terrorism financing raises new questions about the shrinking space for philanthropy in Europe.<sup>106</sup> Chapter 4 considers these issues and presents the challenges facing and opportunities open to philanthropic organisations to be part of the legislative and policy process.

Turning next to the role of fiscal regulation, Chapter 5 focuses on the fiscal and taxation issues facing philanthropic organisations active across borders. Much has been written about the fiscal restrictions experienced by philanthropic organisations. Much progress, however, has also been made in light of the European Court of Justice's developing jurisprudence in this area and the Commission's active use of enforcement notices to bring Member States into line with the non-discrimination principles set out

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<sup>106</sup> See, e.g., Poland's draft Act on the National Freedom Institute-Centre for the Development of Civil Society 2017 and Hungary's Act on the Transparency of Organisations Supported from Abroad 2017. Such developments however are not limited to Eastern Europe. In 2014, Spain passed a law requiring all donations greater than €100 to be reported upon request – see Spanish Royal Decree (B.O.E., 304/2014, Art 42), passing the Regulation of Act 10/2010 on Anti-Money Laundering and Counter-Terrorist Financing, which completes the implementation into Spanish law of Directive 2005/60/EC, while in 2017 Reuters reported that more than 300 charities were hit by a global crackdown on illegal funds - <http://uk.reuters.com/article/uk-banks-charities/three-hundred-uk-charities-hit-by-global-crackdown-on-illegal-funds-idUKKBN1AC0F3>.

under EU law. Nevertheless, problems still remain, as identified by previous and more recent reports commissioned by EFC and Transnational Giving Europe (TGE). This chapter provides a brief overview of the current fiscal landscape and examines the extent to which potential still remains to make this a more enabling space for philanthropic organisations.

Finally, outside of Directives and Regulations and national laws, exists the whole realm of soft law and administrative guidance, much of which shapes the day-to-day experience of many philanthropic organisations throughout Europe. Soft law refers to rules that are neither strictly binding in nature nor completely lacking in legal significance. In the context of international law, soft law refers to guidelines, policy declarations or codes of conduct which set standards of conduct. Although they are not directly enforceable, they can produce some legal effects. It is therefore important to distinguish soft law's lack of legally binding effect from its potential impact in practice. Precisely because it exercises an informal 'soft' influence, soft law may affect policy development, creating the space to float ideas and persuade adoption. At EU level through the use of Recommendations, Opinions, Notices, Action Programmes and other forms of social dialogue, the Commission regularly engages in soft law. Soft law, therefore, is sometimes presented as a more flexible instrument in achieving policy objectives. Chapter 6 revisits the study of transparency of Public Benefit Organisations conducted by DAFNE and EFC in 2011. It reviews the status of soft law today at both national and regional level and considers the less than successful previous attempts of the EU Commission to use this tool successfully in its regulation of non-profits.

## 4. Locating the International Regulatory Space: The Interplay with European Philanthropy

Turning from legal infrastructural and legal structural issues within the context of the European Treaties, one further aspect of hard regulation merits attention for its capacity to impinge upon the space for European philanthropy, namely, the specific European and national regulations controlling and (sometimes) restricting the movement of philanthropic funds within Europe. These regulations take different forms and spring from differently motivated sources but the end result in all cases tends to be the same – their potential either directly or indirectly to adversely affect the movement of philanthropic funds. To this end, this chapter focuses on three related areas: firstly, the macro effect of the EU's attempted adherence to the Financial Action Task Force Recommendations on anti-money laundering and counter terrorist financing measures and the consequent impact on European philanthropic organisations; secondly, the emergence of the European Commission's Supranational Risk Assessment (SNRA) regime, specifically intended to give effect to the EU's FATF commitments and the challenges for philanthropy inherent in this regime; and finally, consideration of emerging national regulation that impacts on philanthropic flows in Europe with particular attention on recent developments in Hungary.

### The FATF Regime in Europe – A Brief Description

The FATF is an intergovernmental body charged with setting standards to promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. As a regional FATF member in its own right, the European Commission is charged with giving effect to the FATF's recommendations in the areas of anti-money laundering and anti-terrorist financing. Recommendation 8 deals specifically with the vulnerabilities of the non-profit sector to terrorist exploitation. It charges FATF members (both member states and regional members such as the European Commission) to: “review the adequacy of laws and regulations that relate to non-profit organisations which the country has identified as being vulnerable to terrorist financing abuse. Countries should apply focused and proportionate measures, in line with the risk-based approach, to such non-profit organisations to protect them from terrorist financing abuse, including:

- (a) by terrorist organisations posing as legitimate entities;
- (b) by exploiting legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset-freezing measures; and
- (c) by concealing or obscuring the clandestine diversion of funds intended for legitimate purposes to terrorist organisations.”<sup>107</sup>

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<sup>107</sup> International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation: The FATF Recommendations. Paris: FATF/OECD, February 2012, Updated October 2016. p.13.



Recommendation 8 ('R8') has become one of the unintended drivers of the shrinking space of civil society. When misapplied, counter-terrorism legislation can be used by some governments to justify a clamp down on civil society. Because it particularly affects the flow of funds from one jurisdiction to another, the shrinking of civil society space in this instance translates into a shrinking of philanthropic capability.

For the European Commission, the FATF recommendations count as informal political commitments rather than binding Treaty obligations, to which it nevertheless strives to give effect. The 40 Recommendations cover a whole host of financial institutions and intermediaries and the EU has sought to give effect to FATF commitments through its promulgation of a series of Anti-Money Laundering Directives.<sup>108</sup> Like many FATF members, the Commission has experienced difficulties in the past in giving full effect to R8.<sup>109</sup> A particular issue for the Commission is, as we have seen in chapter 2, that legislative competence in relation to non-profits lies at the Member State level. The Commission's Communication 2005/620 (from DG Justice), recommending, inter alia, a Framework for a Code of Conduct to enhance transparency and accountability of NPOs and to reduce the risk of abuse of the non-profit sector, represented the Commission's first foray into regulating non-profit compliance in this area.<sup>110</sup> The Communication made recommendations to EU Member States as well as to NPOs, to "verify the identity and good faith of their beneficiaries, donors and associate NPOs," and "keep full and accurate audit trails of funds transferred outside their jurisdiction." Although conceding that "the Framework for a Code of Conduct should not in any way hinder legal cross border activities of NPOs," and declaring that "the aim of the European approach is thus to establish common principles on which national implementation can be based," the Commission provided no guidance on how these common principles were to be achieved and following non-profit concerns, the code was never implemented.<sup>111</sup>

Nevertheless, the Stockholm Programme, negotiated by the European Council and published in 2010, set out a five-year framework for the EU in the then area of justice and home affairs and mandated the Commission "to promote increased transparency and responsibility for charitable organisations with a view to ensuring compatibility with Special Recommendation (SR) VIII of the Financial Action Task Force (FATF)."<sup>112</sup> To this end, the Commission sought to develop and introduce voluntary anti-terrorist

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<sup>108</sup> The most recent of which is the Fourth EU Anti-Money Laundering Directive (EU 2015/849) (AMLD4) which came into effect in June 2015 and replaced the Third Anti-Money Laundering Directive (2005/60/EC). AMLD4 must be transposed into the national law of Member States by June 26, 2017.

<sup>109</sup> See Ben Hayes, Transnational Inst./Statewatch, *Counter-Terrorism, 'Policy Laundering' and The FATF: Legalising Surveillance, Regulating Civil Society* (2012), <http://www.statewatch.org/analyses/no-171-fafp-report.pdf>, illustrating the low compliance rates with R8 – with 69 countries non-compliant and 66 countries only partially compliant with R8 in 2012.

<sup>110</sup> Commission of the European Communities, *The Prevention of and Fight Against Terrorist Financing through Enhanced National Level Coordination and Greater Transparency of the Non-Profit Sector*, COM (2005) 620 final (Nov. 29, 2005) [hereinafter Commission Communication (2005) 620 final].

<sup>111</sup> See further, Oonagh B. Breen, "Through the Looking Glass: European Perspectives On Nonprofit Vulnerability, Legitimacy And Regulation" (2010) 36(3) Brooklyn Journal of International Law 947; Oonagh B. Breen, "European Non-Profit Oversight: The Case for Regulating from the Outside In" (2016) 91(3) Chicago-Kent Law Review 991.

<sup>112</sup> Council of the European Union, *The Stockholm Programme - An Open and Secure Europe Serving and Protecting Citizens*, 2010 O.J. (C 115).

financing guidelines for EU based non-profit organizations to achieve R8 regulatory compliance in the form of a Commission Discussion Paper of 2010.<sup>113</sup> Varying little in style or substance from the earlier ill-fated 2005 Code of Conduct, the 2010 Discussion Paper did not garner much support from non-profit respondents and no final guidelines have emerged from this process. The Commission, however, remains wedded to the principle of oversight, stating that:

“The great majority of non-profit organisations (NGOs) carry out completely legitimate and valuable work. However, the potential vulnerability of NGOs for terrorist financing has been revealed by cases in the EU and in non-EU countries. . . . Voluntary guidelines for the sector could be a means to enhance transparency and accountability of NGOs and to reduce their potential abuse for terrorist financing. The Commission aims to closely involve the NGO sector and EU States in its work in this field.”<sup>114</sup>

### **Impact on Sector**

The impact of FATF measures on the sector has been the subject of several European studies over the past decade. Three reports of note, commissioned by the European Commission are worthy of particular mention – the Independent Scrutiny Report (2007), the Matrix Report (2008) and the ECNL Report (2009).<sup>115</sup> The 2007 Independent Scrutiny Report evaluated the EU’s efforts in the fight against terrorist financing under the FATF’s Special Recommendations and the EU Counter Terrorist Financing Strategy.<sup>116</sup> The Report identified a number of structural difficulties that complicated the EU’s task of giving effect to the FATF’s ordinances at European level, many of which are particularly pertinent to European non-profit regulation efforts and the associated difficulties experienced at EU level with regard to the implementation of R8. These difficulties included, inter alia, the lack of an informed baseline assessment of the threats and risks to the EU and the cultural differences between older Member States (all of whom are FATF members) and newer EU member states (who are members of MONEYVAL) resulting in different degrees of reticence towards European legislative efforts. On foot of these findings, the Commission sought to remedy the information deficit by commissioning the Matrix Report in 2008.<sup>117</sup> Based on its empirical research, Matrix concluded:

“If the available information is to be believed, the incidence and prevalence of NPO financial abuse in the EU are limited. Nevertheless, some level of criminal and terrorist misuse exists. The extent to which this is judged to be “a serious threat” depends on

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<sup>113</sup> See European Commission, *Discussion Paper on Voluntary Guidelines for EU Based Nonprofit Organisations* (July 2, 2010).

<sup>114</sup> Commission DG Migration and Home Affairs at [https://ec.europa.eu/home-affairs/what-we-do/policies/crisis-and-terrorism/financing\\_en](https://ec.europa.eu/home-affairs/what-we-do/policies/crisis-and-terrorism/financing_en) (last accessed May 3, 2017).

<sup>115</sup> For a full discussion on each of these reports see Oonagh B. Breen, “Through the Looking Glass: European Perspectives on Nonprofit Vulnerability, Legitimacy And Regulation” (2010) 36(3) *Brooklyn Journal of International Law* 947, 962-974.

<sup>116</sup> EU Commission, *Independent Scrutiny in Response to Recommendation 41 of the EU Counter Terrorist Financing Strategy to Assess the EU’s Efforts in the Fight against Terrorist Financing: Final Report* (Directorate-General Justice Freedom & Security, 2007) [hereinafter ‘Independent Scrutiny Report’].

<sup>117</sup> Matrix Insight, *Study to Assess the Extent of Abuse of Non-Profit Organisations for Financial Criminal Purposes at EU Level*, European Commission, DG Justice, Freedom and Security (Apr. 3, 2008) [Hereinafter ‘Matrix Report’].

the tolerance levels of the observers . . . . [W]ithout better databases, reporting mechanisms and monitoring systems there is no way of knowing whether the expert group estimates are realistic or merely badly informed.”<sup>118</sup>

Finally, the Commission appointed ECNL to carry out a *study on Recent Public and Self-Regulatory Initiatives Improving Transparency and Accountability of Non-Profit Organisations in the European Union*. The research examined the measures adopted in the twenty-seven EU Member States to improve non-profit transparency and accountability in the overall context of international and European initiatives to address the risk of non-profits being used as conduits for terrorist financing.<sup>119</sup> Published in 2009 and identifying more than 140 self-regulation and public regulation initiatives relating to non-profit accountability and transparency undertaken between 2004-2009, the ECNL report studied 19 of these initiatives in detail before concluding that “the need to overcome the basic differences between the two major legal systems in addition to the varying cultural and historical factors may make any attempt at a pan-European regulatory or self-regulatory initiative extremely challenging.”<sup>120</sup>

Thus, all three commissioned reports highlighted the low level of proven documented threat to philanthropic funds in the EU in the periods examined and the need for any subsequent measures intended to protect such funds to be risk-related, proportionate and evidenced-based. Despite these findings, the ongoing EU rhetoric of counter-terrorist measures has continued to view the non-profit sector, in contrast to the private sector, as vulnerable to exploitation and a potentially high-risk area where specific regulation at a European level is required.<sup>121</sup>

### ***FATF-Non-profit Collaboration: Turning challenges into opportunities***

Despite the demands presented by FATF-influenced measures that often fail to understand the level of threat and the actual level of non-profit vulnerability, philanthropic organisations have responded to the challenge by seeking to liaise with policymakers to educate them on the need to take a more risk based approach when it comes to regulating the non-profit sector in the context of terrorist financing.

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<sup>118</sup> Ibid, at 66.

<sup>119</sup> European Centre for Not-for-Profit Law [ECNL], *Study on the Recent Public and Self-Regulatory Initiatives Improving Transparency and Accountability of Non-Profit Organisations in the European Union*, at 94 (2009) (by Nilda Bullain & Katerina Hadzi-Miceva) (commissioned by the European Commission Directorate-General Justice, Freedom and Security) [hereinafter ‘*ECNL Study*’].

<sup>120</sup> *ECNL Study*, at 15.

<sup>121</sup> In this respect, see Communication from the Commission to the European parliament and the Council: An Area of Freedom, Security and Justice Serving the Citizen, at 23, COM (2009) 262 final (June 10, 2009) (noting “Recommendations must be prepared for charitable organisations to increase their transparency and responsibility”); Council of the European Union, The Stockholm Programme—An Open and Secure Europe Serving and Protecting Citizens, 2010 O.J. (C 115) [hereinafter Stockholm Program]. See also the more recent challenging feedback from the Nonprofit Platform to the Commission’s apportioning of high levels of risk and vulnerability to the European non-profit sector, CSE, ECNL, EFC and HSC, “NPO input for the European Commission Supranational Risk Assessment on Money Laundering and Terrorist Financing (SNRA) following the EC consultation meeting on 4 October 2016” (November 2016).

In 2013, the FATF began bilateral discussions with a group of interested non-profits with a view to entering into dialogue on the future of R8.<sup>122</sup> The non-profits concerned coalesced into a global non-profit policy platform,<sup>123</sup> which over the next four years engaged with the FATF Secretariat, the European Commission and the US Treasury in raising awareness of non-profit concerns regarding the implementation of R8 at national, regional and global levels. Through the creation of the Nonprofit Platform, more effective non-profit participation in the FATF's consultation processes was made possible. This led to a number of significant achievements including the formalisation of a risk-based approach, leading to more proportionate and context-specific implementation of FATF standards;<sup>124</sup> in-depth revision of the FATF Best Practices Paper (June 2015),<sup>125</sup> a policy guidance document that countries use to help them implement the standards; and a significant revision of Recommendation 8 and its Interpretive Note, resulting in the June 2016 revision of R8, retracting the claim that the non-profit sector is 'particularly vulnerable' to terrorist abuse.<sup>126</sup>

In 2017, the Nonprofit Platform was offered four seats on the Financial Action Task Force's (FATF) Private Sector Consultative Forum (PSCF). The PSCF consists of representatives of the financial sector and other businesses and professions subject to anti-money-laundering and counter-terrorism-financing obligations as well as of civil society. These sectors play a key role in ensuring an effective implementation of FATF Recommendations. The formal inclusion of the Nonprofit Platform in these deliberations, with one seat specifically allocated to institutional philanthropy,<sup>127</sup> is significant as the PSCF frequently discusses FATF matters that directly impact on non-profits.<sup>128</sup>

### **Country Mutual Evaluation Reports – Sharing the Learning**

The FATF conducts mutual evaluations of its members' levels of implementation of the FATF Recommendations on an ongoing basis. Since the Fourth Round of Mutual Evaluations, evaluations now have two basic components: effectiveness and technical compliance. The assessed country must provide information on the laws, regulations and any other legal instruments it has in place to combat money laundering and the financing of terrorism and proliferation – it must show that it is technically compliant with the Recommendations. But since 2013, technical compliance is not enough. The main component of a mutual evaluation is now effectiveness. The expert assessment team requires evidence that demonstrates that the assessed country's measures are working and delivering the right results.

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<sup>122</sup> For a full discussion of these negotiations, see Oonagh B. Breen, "European Non-Profit Oversight: The Case for Regulating from the Outside In" (2016) 91(3) *Chicago-Kent Law Review* 991, 1012.

<sup>123</sup> See the Non-Profit Platform on the FATF, <http://fatfplatform.org/about/>.

<sup>124</sup> Transnational NPO Working Group on FATF, Recommendations: Financial Action Task Force Typology Review (February 2014); FATF, Risk of Terrorist Abuse in Non-Profit Organisations (June 2014).

<sup>125</sup> FATF, Best Practices: Combating the Abuse of Non-Profit Organisations (Recommendation 8) (2015).

<sup>126</sup> FATF Revised Recommendations and Interpretive Note (October 2016), [http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF\\_Recommendations.pdf](http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf).

<sup>127</sup> This seat is currently held by EFC on behalf of the Worldwide Initiative for Grantmaker Supports (WINGS). The remaining seats are held by Human Security Collective (HSC) as co-chair of the Global NPO Coalition on FATF, the European Center for Not-for-Profit Law (ECNL) on behalf of the ICNL Alliance, and the Norwegian Refugee Council as a representative of service delivery/humanitarian assistance organisations.

<sup>128</sup> The March 2017 PSCF focused on country evaluation and risk assessment. See the reports of the forum at <http://fatfplatform.org/private-sector-consultative-forum/>.

This is particularly important in the context of R8 – where disproportionate restrictions on the movement of funds can often cause hardship for philanthropic organisations -- and it requires governments to engage with the non-profit sector and to take account of their experiences in readiness for the expert site visit.

To this end, the Non-Profit Platform facilitated several workshops on the FATF and its effects on civil society organisations in various EU member states 2016, bringing together non-profit stakeholders accompanied, on occasion, by government officials, thereby upskilling participants to play more informed roles in the mutual evaluation processes in a number of countries.<sup>129</sup>

### The Next Frontier: The EU Supranational Risk Assessment Scheme

Under the 4th Anti Money Laundering (AML Directive), the Commission is required to conduct an assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border activities.<sup>130</sup> The Commission is required by Art 6 of the Directive to make recommendations to Member States on the measures suitable to address those risks on a "comply or explain" basis. With the first such Commission report in June 2017,<sup>131</sup> it was recognised that the European Union needed to identify, understand and seek to mitigate risks of money laundering and terrorism financing which are relevant from an EU perspective and could not be addressed effectively by individual Member States. Consequently, it created its Supranational Risk Assessment scheme (SNRA) to adopt a "risk based approach" aimed at ensuring that resources and measures to prevent or mitigate money laundering and terrorist financing risks are commensurate with the risks identified. Specific focus would then be placed on situations representing a higher risk of money laundering and terrorist financing. The supranational risk assessment is meant to complement (as opposed to substitute) Member States' approach<sup>132</sup> and to support Member States in their own processes. Member States are therefore required to take into account the results of the EU supranational risk assessment for their own risk assessments.

The Commission adopted an Action Plan in February 2016,<sup>133</sup> providing for short term and medium term strands of action, namely tracing terrorists in the first instance and preventing their movement of assets and funds before then focusing on disrupting the sources of revenue used by terrorists by targeting their capacity to raise funds in the medium to long term. The SNRA is intended as a tool of

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<sup>129</sup> Workshops were held with civil society organisations in Denmark (April 2016), Sweden (May 2016), Ireland (September 2016), the Czech Republic (July 2017) and a regional experts meeting was also held in London in September 2016 bringing together non-profits, government and revenue officials and representatives of the FATF Secretariat.

<sup>130</sup> Article 6 Directive (EU) 2015/849.

<sup>131</sup> And thereafter every two years.

<sup>132</sup> See Art 7 of Directive (EU) 2015/849.

<sup>133</sup> Communication from the Commission to the European Parliament and the Council on an Action Plan for strengthening the fight against terrorist financing, COM(2016) 50 final.

the Commission under EU law to enable it to understand risks and elaborate policies with a view to addressing the identified risks of money laundering and terrorist financing.

The SNRA covers not only those areas of risk currently covered by the 4<sup>th</sup> AML Directive<sup>134</sup> but also other areas considered at risk but not yet covered, including non-profit organisations and for this reason it is important to consider its implications in the context of protecting the European philanthropic space. The Commission Roadmap for the implementation of the SNRA, published in February 2017, outlined the steps undertaken and to be taken by the Commission in advance of the June Report.<sup>135</sup> Throughout 2016 and leading up to the COM report's adoption in June 2017, the SNRA process focused on identifying the risks, assessing the threat and assessing the vulnerabilities of the various sectors as well as the management of that risk through risk analysis and risk mitigation procedures.

What has this meant for non-profits generally and philanthropy more specifically? The Commission has consulted the private sector and civil society during the SNRA process. It organised dedicated workshops with the four main groups of private sector stakeholders (financial sector, legal professions, other obliged entities, civil society and academia) at three steps in the process: 1) following the preliminary risk identification (February 2016); 2) following the preliminary outcome (November 2016) and 3) when it was considering possible mitigating actions to address the identified risks (March 2017).

A group comprising Civil Society Europe (CSE), the European Center for Not-for Profit law (ECNL), the European Foundation Centre (EFC), and the Human Security Collective (HSC), took the lead on behalf of an informal and wide European NPO coalition working on the impact of counterterrorism (CT) policy on non-profits. In their November 2016 response to the Commission's consultation on its preliminary outcomes, this non-profit coalition concluded that:

“good governance arrangements, financial checks and risk management policies and procedures that fit the specific needs and size, activities and areas of operation of NPOs, are the best tools to safeguard against a range of potential abuse, including terrorist financing and money laundering. NPOs are aware of potential risks but in most cases do not consider themselves at risk because of the careful mitigation measures and practices in place. However, that said, a zero-risk scenario does not exist.”<sup>136</sup>

In particular the coalition warned of the dangers of engaging in policy-making before undertaking the relevant assessment and the importance of cross-checking EU initiatives with global counter-terrorism policy as well as the need to ensure policy coherence between various EU initiatives. The importance

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<sup>134</sup> Credit institutions; financial institutions; and the following natural or legal persons: (a) auditors, external accountants and tax advisors; (b) notaries and other independent legal professionals, when they participate in certain activities; (c) trust or company service providers; (d) estate agents; (e) traders in goods (payment in cash >EUR 10 000); and (f) providers of gambling services.

<sup>135</sup> Commission Roadmap on the EU Supranational Risk Assessment on money laundering and terrorist financing, Ref. Ares(2017)1060803 - 28/02/2017.

<sup>136</sup> CSE, ECNL, EFC and HSC, *NPO input for the European Commission Supranational Risk Assessment on Money Laundering and Terrorist Financing (SNRA) following the EC consultation meeting on 4 October 2016* (November 2016).

of any EU counter-terrorism policy being fit for purpose and having a rights-based approach was also highlighted in light of non-profits previous experience of the unintended consequences of counter terrorism/money laundering policies, including large-scale de-risking by banks and the overregulation of the sector.<sup>137</sup> The Commission's initial findings relating to non-profits under the SNRA found that the "when they are misused, NPOs represent a *significant threat*, in particular as far as foreign terrorist fighters are concerned." The Commission also found the terrorist financing vulnerability related to the collection and transfer of funds by NPOs *to be significant*. Both findings were disputed by the non-profit coalition which argued that the threat analysis lacked an evidence- and risk-based approach and wrongly singled out non-profits as specifically prone to risk in the collection or transfer of funds while the vulnerability analysis was equally flawed for failing to take account of the high level of awareness of risk amongst non-profits. Moreover, the coalition argued that organisations with access to significant financial resources (from different sources) and engaging in transfers across borders was a scenario with a medium (rather than high) level of risk. The fact that an organisation's activities had a major international scope was of itself generally not considered to pose a risk.<sup>138</sup>

In a final consultation meeting between the European Commission and European civil society organisations in March 2017, non-profits urged the Commission to distinguish more clearly between the separate processes of the collection (e.g., fundraising) and transfer/distribution of funds, given the different terrorist financing risks associated with both. In counselling the Commission to adopt a more nuanced risk-based approach to its treatment of terrorist financing risk in the non-profit arena, the Nonprofit Platform Coalition pushed the Commission to analyse whether existing measures for non-profits potentially addressed the risks while making several recommendations on how the Commission might best tackle the planned risk mitigation matters in its report in so far as they related to non-profits.<sup>139</sup>

In June 2017, the Commission published the Supra National Risk Assessment Report.<sup>140</sup> The Report does not propose any new European regulation of non-profits but it does recommend Member States to ensure appropriate non-profits coverage in their national risk assessments as part of their risk mitigation measures.<sup>141</sup> It is most likely therefore that any European level implementation measures are likely to occur by way of soft law, to which end this report is discussed in greater detail in Chapter 6.

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<sup>137</sup> Ibid, at 2-3.

<sup>138</sup> Ibid, at 5.

<sup>139</sup> NOTE (17/03/2017) – prepared by EFC, ECNL, HSC and CSE NPO input for the European Commission – March 2017 Supranational Risk Assessment (SNRA) on Money Laundering and Terrorism Financing following a consultation meeting on March 14, 2017.

<sup>140</sup> Report from the Commission to the European Parliament and the Council on the assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border activities, COM (2017) 340 final.

<sup>141</sup> Ibid, at 16.

### ***Beneficial Ownership Registers – FATF Recommendations 24 and 25 and the Fourth Anti-Money Laundering Directive***

One further emerging issue at both international and European level that will have a regulatory impact on institutional philanthropy concerns the requirements around beneficial ownership transparency and information availability. Briefly, in an effort to tackle money laundering and terrorism financing, FATF Recommendations 24 and 25 require countries to enhance the transparency of the beneficial ownership of legal entities. These measures are targeted at for-profit entities and the regulatory requirement to know who is the ultimate beneficiary behind a legal corporation or a trust. Working from first principles, charitable institutions and trusts are created for the public benefit. They do not have ascertainable, fixed or numerically negligible beneficial owners. They are created for charitable and public benefit purposes from which ultimately individuals benefit but these individuals cannot be compared to the fixed and certain beneficial owners behind a for-profit corporation or a private trust. There is thus a need to ensure that Member State application of R24 and R25 excludes non-profits or is adapted in such a manner as to appreciate the nature of such entities.

The EU implements R24 and R25 through the Fourth Anti-Money Laundering Directive (4AMLD).<sup>142</sup> The 4AMLD requires the creation of a public Register of Beneficial Ownership of Legal Entities. The Directive also imposes reporting requirements on certain ‘obliged entities’ that fulfil certain criteria. Under these criteria, non-profits will, on occasion, qualify as obliged entities and therefore be subject to the ‘know your customer’ and ‘know your beneficiary’ verification and monitoring procedures laid down by 4AMLD, which given its commercial basis, is not always appropriate or proportionate for the non-profit and philanthropic sector. A further worrying feature is that 4AMLD calls on Member States to extend the application of the Directive to those entities ‘engaged in activities particularly likely to be used for money laundering or terrorist financing purposes.’ In light of the recent revisions of FATF R8, a blanket coverage by 4AMLD of non-profits would be unwarranted. Nevertheless, the fear remains that in the absence of appropriate European guidance around implementation, Member States may over-regulate non-profits under both headings.<sup>143</sup>

The implications of these developments for European philanthropy should not be under-estimated. As of June 2017, all Member States were required to establish registers of beneficial ownership. Most countries have required non-profit corporations to register and some have extended this requirement to trusts,<sup>144</sup> in advance of the Commission’s expected move to do so. Further proposed moves by the

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<sup>142</sup> Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing [hereinafter ‘4AMLD’]. The 4AMLD is currently undergoing amendment in line with the Commission’s Communication to the European Parliament and the Council on an Action Plan for strengthening the fight against terrorist financing COM(2016) 50 final, February 2, 2016.

<sup>143</sup> See further, ECNL, EFC and HSC, *Beyond FATF Recommendation 8: How Anti-Money Laundering and Counter-Terrorism Financing Measures impact NPOs in Europe* (August 2017).

<sup>144</sup> Interestingly, the UK’s Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (SI 692 of 2017) require trusts to register only if the trust is liable to tax, which would exclude most philanthropic institutions. Similarly, the Irish European Union (Anti-Money Laundering: Beneficial Ownership of Corporate Entities) Regulations 2016 currently apply to a number of corporate entities and other legal entities



EU (acting under the 4AMLD, the SNRA and the 2016 Counter Terrorism Action Plan) include the creation of an EU blacklist of certain countries with AML/CTF deficiencies and the introduction of compulsory due diligence checks and enhanced due diligence checks by financial institutions on money flows to these black-listed countries. These amendments are likely to make the carrying out of philanthropic activities in these regions even more difficult and burdensome.<sup>145</sup>

## Cross Border Barrier Issues: National Ripples in a European Context

Despite the failure of the Commission's proposal for the European Foundation Statute in late 2014, many of the difficulties experienced by foundations seeking to operate across member state borders in the European Union persist today. These fiscal and legal barriers are a result of incompatible national laws that impose separate regulatory requirements on philanthropic organisations seeking to be established or operate in a particular Member State. The vast majority of these regulations are not in breach of European law per se but their existence is a symptom of lack of harmonisation between various Member States that leads to additional administrative burdens on organisations working in more than one Member State.

These cross border barriers were examined in the Feasibility Study on a European Foundation Statute in 2009.<sup>146</sup> Chief amongst those issues identified as potentially problematical were: cross-border transfer of a foundation's registered seat; lack of merger possibilities and taxation issues (the last of which will be discussed in chapter 5).

### *Cross-Border Transfer of a Foundation's Registered Seat*

Of the 27 EU member states, 14 Member States follow the real seat doctrine (which is based upon the assumption that the state in which an entity has its real seat is typically the state that is most strongly affected by the activities of the entity, and therefore should have the power to govern the internal affairs of that entity)<sup>147</sup> while 11 Member States follow the State-of-Incorporation doctrine (under which the existence of a foundation, as well as its subsequent dissolution, are governed by the law of the state of incorporation).<sup>148</sup> The two doctrines represent contrasting values and belief systems – as the *EFS*

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incorporated in the State, including companies limited by guarantee but do not currently apply to charitable trusts or to charitable unincorporated associations.

<sup>145</sup> ECNL, EFC and HSC, above, n.143.

<sup>146</sup> University of Heidelberg and Max Planck Institute for Comparative and International Private Law, *Feasibility Study on a European Foundation Statute: Final Report* (2009), Part 4 [hereinafter '*EFS Feasibility Study*']. See also Eszter Hartay and Ivana Rosenzweigová, *The Regulatory Framework for Fundraising in Europe* (Budapest: ECNL, 2017), a report seeking to build a dialogue on how best to regulate fundraising and create a more enabling environment for the financial sustainability of civil society organisations throughout Europe.

<sup>147</sup> Real seat theory applies in the member states of Austria, Belgium, Finland, France, Germany, Greece, Italy, Latvia, Lithuania, Poland, Portugal, Romania, Slovakia, and Spain.

<sup>148</sup> Applied by Bulgaria, Cyprus, Denmark, Estonia, Hungary, Ireland, Luxembourg, the Netherlands, Slovenia, Sweden and the UK. As noted by the *EFS Feasibility Study*, at 110, "The importance of the law of the state of incorporation is greatly enhanced by the fact that the law of the state of incorporation also applies, with rare exceptions, to the internal affairs of the entity."

*Feasibility Study* explains, “traditionally, States that recognise a political, or even a constitutional, need to protect certain (local) interests will favour the real seat doctrine. In contrast, states that support the idea of party autonomy in corporate and foundation law matters will, at least in principle, be in favour of the state-of-incorporation rule or similar choice-of-corporate-law principles.”<sup>149</sup>

To date, the European Court of Justice has not had an opportunity to rule on a foundation’s right of establishment and it is unclear what the legal situation is if a foundation wants to transfer its registered seat from one Member State to another. Legal commentators suggest that if a foundation decides to transfer its seat to another member state, member states that subscribe to the real seat doctrine will require the foundation to dissolve itself and to reconstitute itself in the other member state. This will be dependent upon the dissolution being permitted or approved by the competent government authority in the first instance.<sup>150</sup> Since the foundation’s dissolution and liquidation effectively terminates the will of the original benefactor or settlor, the board’s decision to dissolve and liquidate will generally require government approval. Formation of a new foundation in another member state, in turn, will be subject to a set of entirely new and different laws that may be based on a totally different perception and conception of non-profit organisations and foundations.<sup>151</sup> This situation has the potential to present problems for philanthropic organisations currently residing in ‘real seat’ jurisdictions that are contemplating a transfer of their seat.

### **Cross-Border Merger Issues**

In the same way that moving seat can cause issues for philanthropic organisations, cross border mergers can also prove difficult in certain cases. The *EFS Feasibility Study* points out that there is neither European Court of Justice jurisprudence nor pertinent secondary EU legislation on the rules for cross-border mergers between, and acquisitions or restructurings of, foundations. The closest that the ECJ has come to addressing the issue was in *Sevic Systems AG v. Amtsgericht Neuwied*, where it held that structural changes such as a cross-border merger fell within the ambit of Articles 43 and 48 of the EC Treaty.<sup>152</sup> These treaty articles, however only apply to foundations engaged in economic activities and not necessarily to all those engaged in philanthropic endeavours, making such mergers the extremely rare exception rather than the common rule.<sup>153</sup>

### **Restrictions on Foreign Funding: A Hungarian Case Study**

One of the more blatant barriers to cross-border philanthropy in recent years has been the emergence of Foreign Agents legislation. The aim of such legislation has been to restrict the inflow of ‘foreign’ funding to civil society organisations within the promulgating state and to stigmatize such organisations

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<sup>149</sup> *EFS Feasibility Study*, n. **Error! Bookmark not defined.** above, at 111.

<sup>150</sup> *Ibid*, at 112.

<sup>151</sup> *Ibid*.

<sup>152</sup> Case C-411/03, *Sevic Systems AG v. Amtsgericht Neuwied* [2005] ECR I-4321 at [21].

<sup>153</sup> *EFS Feasibility Study*, n. **Error! Bookmark not defined.** above, at 139. The Study notes that even then “In order to make this kind of cross-border transaction viable, the two jurisdictions concerned would need to allow this kind of transaction, and the parties concerned would have to comply with the requirements of the laws of both jurisdictions, including any governmental approval requirements.”

by forcing them to register with the State, declare how much foreign funding they receive and to name their donors. The rationale often advanced for such legislation is to protect sovereignty and the democratic will of the state in question and not to have it corrupted or undermined by foreign powers using civil society organisations as a conduit.

In the past, examples of such foreign agent legislation have been found in Russia<sup>154</sup> and India,<sup>155</sup> while attempts to introduce similar legislation in Kyrgyzstan failed in 2016, thanks to the engagement of civil society with the Kyrgyz Parliament.<sup>156</sup>

The most recent (and first EU Member State) attempt to introduce a Foreign Agents Act arose in Hungary. The Hungarian Parliament adopted the Law on the Transparency of Organisations Receiving Support from Abroad, on June 13, 2017.<sup>157</sup> The new law provides that NGOs receiving more than €24,000 in foreign funding in a given tax year are required within 15 days of receipt to register as a 'foreign funded organisation,' to display this status on their websites and all other external documentation and to report the details of each donor to the registering court. Failure to register, upon prosecutorial summons, can result in fines of up to €2,900 while continuing non-compliance can ultimately result in the prosecutor seeking an order to dissolve the foundation or association through a simplified liquidation process and its removal from the register. The law covers all monetary allocations received from abroad (including private donations) except for EU funds that are paid to a foundation or association through a Hungarian government institution. The law does not apply to sports or religious organisations, political parties or their foundations, trade unions, mutual insurance associations or public foundations. The rationale for the law, according to the Hungarian Government, is the need to ensure national security and sovereignty and to comply with anti-money laundering and counter-terrorist financing measures.

The international response to the law has been overwhelmingly negative, with commentators (including philanthropic funders) criticising the flawed rationale for promulgation, the non-consultative legislative procedures adopted and the inappropriate substantive content of the promulgated Act which fails to

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<sup>154</sup> On July 20, 2012, Russia enacted the *Federal Law Introducing Amendments to Certain Legislative Acts of the Russian Federation Regarding the Regulation of Activities of Non-commercial Organizations Performing the Function of Foreign Agents*, which came into effect on November 21, 2012. The law requires all non-commercial organizations (NCOs) to register in the registry of NCOs, which is maintained by the Ministry of Justice, prior to receipt of funding from any foreign sources if they intend to conduct political activities.

<sup>155</sup> Indian Foreign Contribution (Regulation) Act 2010, an Act consolidating the law to regulate the acceptance and utilisation of foreign contribution or foreign hospitality by certain individuals or associations or companies and to prohibit acceptance and utilisation of foreign contributions or foreign hospitality for any activities detrimental to the national interest.

<sup>156</sup> On May 12, 2016, the Kyrgyz Parliament voted on the draft law formerly known as the "Foreign Agents Law (FA Law)." 46 MPs voted in favour of the draft FA Law, and 65 MPs voted against it. Thus, the draft FA Law was rejected and, according to the Procedures of Parliament, it can only be reintroduced in Parliament after 6 months. The draft FA Law could therefore be revived in December 2016, although civil society hopes this will signal end of the draft FA Law. Source: ICNL Civic Freedom Monitor – Kyrgyz Republic (see <http://www.icnl.org/research/monitor/kyrgyz.html>).

<sup>157</sup> For a copy of the law's provisions, see [http://www.venice.coe.int/webforms/documents/default.aspx?pdffile=CDL-REF\(2017\)031-e](http://www.venice.coe.int/webforms/documents/default.aspx?pdffile=CDL-REF(2017)031-e).

comply with FATF requirements and the European AMLDs, and does not respect the rights guaranteed by the European Convention on Human Rights and the European Treaty's Free Movement of Capital.<sup>158</sup> These criticisms are worth considering in a little further detail, in turn.

*a) The flawed rationale for promulgation*

Three main grounds are advanced for the promulgation of this draft Hungarian law, namely, that it is required in the interests of national security, sovereignty and to prevent money laundering and terrorist financing. The Hungarian Government, however, produced no evidence to support its claim that the targeted foundations and associations were undermining democracy or supporting money-laundering or terrorist financing. In fact, prior to introducing the Bill, Hungary carried out no national risk assessment which is required both by the FATF and by Article 7 of 4AMLD. No evidence was proffered either as to why religious and sporting organisations along with political parties and public foundations are excluded from the scope of the Bill, a matter on which the Venice Commission unsuccessfully sought clarification.<sup>159</sup>

*b) The non-consultative legislative procedures adopted in the passage of the Act*

The Hungarian Government's failure to carry out any meaningful public consultation on the Bill violated Art 25 of the International Covenant on Civil and Political Rights (ICCPR),<sup>160</sup> the UN Human Rights Council Resolutions regarding participation<sup>161</sup> and the Council of Europe Code of Good Practice for Civil Participation in the decision-making process.<sup>162</sup> In the words of the Council of Europe,

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<sup>158</sup> See Conference of INGOs of the Council of Europe, Expert Council on NGO Law, *Opinion on the Hungarian Draft Act on the Transparency of Organisations Supported from Abroad* (April 2017); Council of Europe Commissioner for Human Rights, *Letter to the Speaker of the Hungarian Parliament* (April 2017); Civil Liberties Union for Europe, ECNL, Hungarian Helsinki Committee, TASZ, *Analysis of Hungarian Parliament Bill T/14967 in light of EU rules on anti-money laundering and terrorist financing and free movement of capital* (April 25, 2017); Hungarian Helsinki Committee, Hungarian Civil Liberties Union, TASZ, *Short Analysis of the Proposed Bill on Foreign Funded NGOs* (April 11, 2017); Statement of International Funders Supporting NGOs in Hungary (April 27, 2017, available at <http://www.efc.be/wp-content/uploads/2017/11/2017-07-Statement-Supporting-NGOs-in-Hungary.pdf>). Letter from the UN Special Rapporteurs on the promotion and protection of the right to freedom of opinion and expression; on the rights to freedom of peaceful assembly and of association; and on the situation of human rights defenders to Hungary OL HUN 2/2017 (May 9, 2017) available at <http://www.ohchr.org/Documents/Issues/Opinion/Legislation/OL-HUN-2-2017.pdf> and the Venice Commission Opinions of June 1 and June 19, 2017, n. 159, below.

<sup>159</sup> At the request of the Parliamentary Assembly of the Council of Europe, the Venice Commission visited Budapest and produced both a Preliminary Opinion and a further subsequent Opinion on the draft Hungarian Law in June 2017. The opinions (CDL-AD(2017)015 and CDL-PI(2017)002) can be accessed at: <http://www.venice.coe.int/webforms/documents/?country=17&year=all>.

<sup>160</sup> Art 25 ICCPR provides that every citizen shall have the right and the opportunity . . . and without unreasonable restrictions: (a) To take part in the conduct of public affairs, directly or through freely chosen representatives.

<sup>161</sup> UN Human Rights Council Resolution on Equal participation in political and public affairs A/HRC/RES/27/24 (October 3, 2014); UN Human Rights Council Resolution on Equal participation in political and public affairs 33/22 A/HRC/RES/33/22 (30 September 2016).

<sup>162</sup> Conference of INGOs of the Council of Europe, Code of Good Practice for Civil Participation in the Decision-Making Process, CONF/PLE(2009)CODE1, available at <http://rm.coe.int/CoERMPublicCommonSearchServices/DisplayDCTMContent?documentId=09000016802eed5c>.

“The draft Act does not offer publicly available evidence of imminent threat by foreign funded NGOs that would merit further scrutiny over their funding, especially funding from abroad.”<sup>163</sup>

c) *Inappropriate substantive content of the Act*

ii. *Failure to comply with FATF requirements and the European AMLDs*

In failing to carry out any risk assessment prior to the introduction of the draft law, the Hungarian Government violated the FATF’s requirements<sup>164</sup> and the related requirements of the 4AMLD. The required risk assessment should have focused precisely on the NGOs in question; it should have identified which categories within that cohort were at risk of terrorist financing; and for those particular entities, it should have then assessed whether existing national measures were sufficient to address the risk and if not, what proportionate adaptation was required. Moreover, Hungary’s national risk assessment conducted in the context of the MONEYVAL Mutual Evaluation process rated the risk of NGOs to be low in 2016.<sup>165</sup>

ii. *Failure to respect the rights guaranteed by the European Convention on Human Rights*

All the submissions<sup>166</sup> point to the Hungarian law’s violations of the freedom of expression,<sup>167</sup> the freedom of association<sup>168</sup> and the right to personal data protection and privacy.<sup>169</sup>

iii. *Breach of the European Treaty’s Free Movement of Capital*

EU law prohibits Member States from restricting the free flow of capital between EU Member States. The definition of capital includes philanthropic funds and donations made to charitable organisations.<sup>170</sup> Therefore, any legislative measure that deters individuals or organisations from transferring capital between member states will constitute a restriction and therefore violate the rights set down in Article 63 TFEU and Directive 88/361.

The Hungarian Act requires the relevant associations and foundations that receive a threshold amount of foreign funding to notify the court, which will then register the organisation as an ‘organisation supported from abroad.’ The register is maintained by the Ministry responsible for the Civil Information Portal and organisations must annually declare

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<sup>163</sup> Conference of INGOs of the Council of Europe, Expert Council on NGO Law, n. 158 above, at [27].

<sup>164</sup> See Recommendation 1 and 8 and the Interpretive Notes of the Financial Action Taskforce.

<sup>165</sup> Council of Europe’s Committee of Experts on the evaluation of anti-money laundering measures and the financing of terrorism (MONEYVAL), “Anti-money Laundering and Counter-Terrorist Financing Measures: Hungary” Fifth Mutual Evaluation Report, September 2016, at [18]. Moneyval recommended at 36 that “A more detailed ML/FT-threat and vulnerability analysis – by collecting in-depth data - should be undertaken by updating the NRA. A similar exercise should be undertaken for FT threats and vulnerabilities. The authorities should focus particularly on NPOs and cross-border movements of cash.”

<sup>166</sup> See n. 158, above.

<sup>167</sup> See, in particular, violations of Article 11 of the EU Charter of Fundamental Rights, Article 19 ICCPR and Article 10 ECHR.

<sup>168</sup> See Article 12 of the EU Charter of Fundamental Rights, Article 22 ICCPR and Article 11 ECHR.

<sup>169</sup> See, in particular, Article 8 EU Charter of Fundamental Rights, Article 17 ICCPR, Article 8 ECHR and Article 9 of the EU General Data Protection Regulation (2016/679).

<sup>170</sup> See Chapter 2.

details of the support received each year – including the amount of donation received and name of the donor of each foreign transaction, with details of their location (e.g., city and country for individuals, full registered addresses for donating organisations). The reporting of such personal details per se is likely to deter donors making cross border donations to Hungarian foundations and associations.

The creation of such an obstacle to the free flow of donations counts as a restriction on the free movement of capital between Member States unless it can be justified by Hungary on the basis of public policy and security.<sup>171</sup>

There is thus widespread European and international concern over the promulgation of Hungary's foreign funding law, the passage of which seriously impedes the free flow of philanthropic funds into Hungary and thereby threatens not only national philanthropic space within one Member State but more significantly endangers European philanthropic space within the EU in a manner that would not be compatible with European law. On July 13, 2017, the European Commission launched an infringement procedure against Hungary, sending it a letter of formal notice for its new law on foreign-funded NGOs.<sup>172</sup> For its part, the European Parliament has called on Hungary to repeal the law while simultaneously finding that Hungary's actions warrant the launch of an Article 7(1)TEU action against it.<sup>173</sup>

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<sup>171</sup> Article 65(1)(b) TFEU.

<sup>172</sup> European Commission Press Release, IP/17/1982.

<sup>173</sup> European Parliament resolution of 17 May 2017 on the situation in Hungary, P8\_TA-PROV(2017)0216, (2017/2656(RSP)). The Parliament instructed its Committee on Civil Liberties, Justice and Home Affairs to initiate the proceedings and draw up a specific report with a view to holding a plenary vote on a reasoned proposal calling on the Council to act pursuant to Article 7(1) and this now awaits the Committee's decision (see [http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=&reference=2017/2131\(INL\)](http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=&reference=2017/2131(INL))).

## 5. Enabling the Fiscal Space for European Philanthropy

Philanthropy and associated tax relief go hand in hand. Policymakers in almost every country seek to encourage and indeed incentivise philanthropy through the provision of tax exemptions for the charitable organisations and foundations involved and often tax reliefs or credits for the related philanthropic donors.<sup>174</sup> While European Member States remain sovereign in the area of taxation and for the most part, national tax regimes may be internally consistent in their treatment of domestic philanthropy, the same clarity of principle does not always follow in tax matters when cross border philanthropy is at issue. The free movement of philanthropic funds between Member States and its treatment under European Law raises questions related to the free movement of capital, mentioned earlier in Chapter 2, and more specifically brings the principle of non-discrimination into action. To this end, the European Court of Justice's developing jurisprudence in this area has begun to clarify the law but its implementation in Member States remains a work in progress that is often slow to give full effect to these principles.

In May 2017, the EFC together with the Transnational Giving Europe Network (TGE) jointly published a report on the cross border philanthropy operating environment.<sup>175</sup> The 2017 Report follows on from a previous 2014 study by the EFC and TGE that highlighted the varied and, in some cases, incomplete implementation by Member States of the non-discrimination principle on the tax treatment of philanthropy, as set out in a series of key rulings by the European Court of Justice (*Hein-Persche, Stauffer, Missionswerk*).<sup>176</sup> The 2017 Report highlights good and bad existing practice in various Member States and seeks to develop recommendations and ideas which could potentially lead to a simplification of the procedures for implementation of the non-discrimination principle.

This chapter briefly summarizes those findings and seeks to contextualise them for policymakers' future consideration and implementation.

### Making it easier to Give and Invest: The Outcomes of the EFC/TFE 2017 Report

One of the main problems identified by the 2017 Report is the lack of publicly available information and a lack of clarity around the comparability processes operated by Member State tax authorities when faced with a claim from a donor to a foreign philanthropic organisation or from the recipient charity. Only 10 of the 27 Member States have identified processes for dealing with such claims. The majority of Member States operate on an ad hoc basis in which no guidance is available and long waiting times (often many years) ensue before a claim is dealt with, if at all.

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<sup>174</sup> EFC, *Comparative Highlights of Foundation Law in Europe: The Operating Environment for Foundations in Europe* (Brussels, 2015)

<sup>175</sup> EFC and TGE, *Boosting cross-border philanthropy in Europe: Towards a Tax Effective Environment* (Brussels, 2017) [hereinafter 'Boosting Philanthropy Report'].

<sup>176</sup> EFC and TGE, *Taxation of cross-border philanthropy in Europe after Persche and Stauffer - From landlock to free movement?* (Brussels, 2014).

The Report considers possible avenues to resolve this administrative impasse. Starting from a realistic basis, the Report acknowledges that multi-lateral treaty based solutions will not achieve the necessary unanimous support amongst Member States to make them a viable option. Similarly, the lack of common ground between Member States makes the provision of automatic Member States exemptions for EU foreign based tax-exempt also an unlikely starter in the current political climate. There is much wisdom in this concession, given the recent negative experience of Member States' engagement with the tax provisions in the ill-fated European Foundation Statute proposal.<sup>177</sup>

Turning then to more pragmatic solutions, the 2017 report offers four possibilities for further consideration:

- a. Provision of greater public information on the principle of equal tax treatment and its application to cross-border philanthropic tax claims coupled with better training for tax staff in each Member State on the existence of and how to deal with the comparability test;
- b. Learn from the Luxembourg model – adopt a simple certificate approach, supported by certain minimal translated documents;
- c. Go Dutch – model a solution on the Dutch requirement for ABNI status and registration with the Tax Authority;
- d. Develop common principles for Member States around 'public benefit' status concept rather than requiring comparability in all detailed respects.

## Unpacking the Policy Options

The Luxembourg and Dutch comparability models, both of which are commended by the Report as possible models for wider adoption, set out clear requirements for a resident donor to donate to EU/EEA based public benefit entities in a tax efficient manner.

### *Learning from Luxembourg...*

The simpler of the two models is the Luxembourg model. It requires a donor declaration that the recipient organisation meets the requirement of Luxembourg tax law<sup>178</sup> and certification by the recipient public benefit organisation of four requirements. These relate to a) the legal establishment of the recipient; b) that it directly and exclusively pursues one or more of the following nine purposes: Art, Education, Philanthropy, Worship/Religion, Science, Social issues, Sports, Tourism or Development cooperation; c) that under the laws of the state of establishment, these selfless aims are recognised as being of general interest and fiscally favoured; and d) the recipient is exempt from income and wealth

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<sup>177</sup> See further Oonagh B. Breen, "The European Foundation Statute Proposal: Striking the Balance between Supervising and Supporting European Philanthropy?" (2014) 5(1) *Nonprofit Policy Forum* 5-43.

<sup>178</sup> This declaration speaks to the fact that the EU/EEA-based organisation is recognised by its state of residence as a public-benefit body and as such is entitled to receive tax-deductible donations from residents of its state and is also exempt from income and wealth tax. *Boosting Philanthropy Report*, n. 175 above, at 16.



tax in its country of establishment for the year of the received donation and that such donations are fiscally deductible by donors residing in its country of establishment.<sup>179</sup>

### **Going Dutch...**

In the Netherlands, a Dutch donor's cross border philanthropy will enjoy tax advantages if the foreign based recipient has been granted ABNI status<sup>180</sup> and registered with the Dutch tax authority. The criteria for obtaining ABNI status are listed in the 2017 report and 300 foreign organisations to date have successfully applied for and been granted this status.<sup>181</sup> While the process of recognition is more burdensome than the Luxembourg model, the advantage of the Dutch approach is that once the foreign public benefit organisation gains this status by registration as an ABNI, the status is valid for tax purposes in respect of all subsequent Dutch tax-paying donations received thereafter, provided that the organisation maintains its registered status.

A similar system operates in Ireland whereby EU/EEA based public benefit organisations can seek registration with the Revenue Commissioners to enable receipt of tax-advantaged donations from Irish donors.<sup>182</sup> A public benefit organisation seeking this status under Irish tax law must be legally established in an EEA State or in an EFTA State and have its centre of management and control therein. It must ensure that its objects and powers are so framed that every object to which its income or property can be applied is charitable, and it must be bound, as to its main object(s) and the application of its income or property, by a Governing Instrument.

### **From Principles to Pragmatism?**

A fourth and final option outlined by the 2017 Report is to develop common principles for Member States around the 'public benefit' status concept rather than requiring comparability in all detailed respects. This policy option seeks to adopt a functional approach whereby the notion of comparability between Member State tax regimes would be broadened to look at the lowest common denominator core principles of public benefit rather than insisting on the presence of higher common factor elements. Under this approach, Member State tax authorities would be encouraged to consider whether the same principles underpinned their tax regime and if so, then to pay less attention to the strict fact that the rules for achieving those principles might not match exactly in each jurisdiction. In other words if the rules when compared holistically might be described as equivalent in effect overall then tax relief would be granted.

To this end, the *Boosting Philanthropy Report* proposes the creation of a new national comparability test based on three core public benefit requirements:

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<sup>179</sup> *Boosting Philanthropy Report*, n. 175 above, at 16.

<sup>180</sup> ABNI stands for *Algemeen Nut Beogende Instelling* status, or in English: Public Benefit Pursuing Entity status.

<sup>181</sup> *Boosting Philanthropy Report*, n. 175 above, at 17-18.

<sup>182</sup> See Revenue Commissioners, Guidance on Non-Resident Charities (Resident in and Operating in an EEA/EFTA State) Seeking a Determination under the Provisions of Sections 208A and 208B Taxes Consolidation Act 1997 (DCHY1, April 2015) available at <http://www.revenue.ie/en/tax/it/leaflets/dchy1.pdf>.

1. Tax Exempt status in the home country;
2. Pursuance of a public-benefit purpose accepted in the tax legislation in the home country or according to a defined closed list of purposes;
3. Exclusive usage of assets for the public-benefit purpose.<sup>183</sup>

According to the *Boosting Philanthropy Report*, adoption of this broader comparability test that focuses less on detailed rules and more on shared ultimate principles would “give to the concerned countries some room for a ‘give and take’ negotiation between country A and country B by saying for instance, ‘We admit that the requirement of your legislation does not exist in our legal system but, on the other hand our legal system is stricter in other respects that also relate to the control of the received funds.’ The same purpose can be pursued through different means, i.e. through different kinds of requirements.”<sup>184</sup>

It is debateable whether tax authorities would have the power to engage in such a functional equivalency determination without the sanction of domestic legislation authorising a departure from the more strictly literal interpretation of the tax laws that normally applies. Whether the appetite for such tax law reform exists at national government level is also open to question, particularly in light of the failed European Foundation Statute Proposal experience.

## Claiming the Right of Philanthropic Transfer

In 2007, the European Commission appointed an expert group to identify and review good practices in university fundraising for research from European philanthropic sources.<sup>185</sup> One of the recommendations of this expert group was to claim the ‘right of philanthropic transfer’ within the EU. Addressed to national governments and to European institutions, the recommendation sought to establish a more ‘level-playing field’ to encourage cross-border giving within the EU. Specifically, the Expert Group proposed in its report the creation of:

“[A] ‘European passport’ for all philanthropy recipients . . . . A move towards the mutual recognition of ‘public benefit/qualifying organisations’, leading to tax benefits at the national level, would be an important step to facilitate cross-border giving . . . National developments could be supported by bilateral agreements. Very few treaties currently address the issue of cross-border giving, and few double tax treaties – which provide tax relief for gifts or legacies across borders – deal with inheritance and/or gift tax

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<sup>183</sup> The exclusivity requirement is elaborated upon in six further sub-requirements (at p21 of the Report), one of which is that there be “No unreasonable remuneration of board members.” The notion of remunerating board members (as opposed to reimbursing them for expenses incurred) flies in the face of established common law practice so it will be interesting to see whether the civil law/common law divide can surmount this difference in approach.

<sup>184</sup> See *Boosting Philanthropy Report*, n. 175 above, at 23.

<sup>185</sup> For details on the context of this project and the objectives of the Expert Group, see [http://ec.europa.eu/invest-in-research/policy/expert\\_en.htm](http://ec.europa.eu/invest-in-research/policy/expert_en.htm).

‘charity friendly’ provisions. EU Member States should be encouraged to review these issues.”<sup>186</sup>

A decade on, these proposals mirror the starting options considered by the EFC/TGE team in its 2017 Report. The focus remains on the need for the development of greater mutual recognition but, as illustrated in the Boosting Philanthropy Report, less reliance is being placed on the capacity of bilateral agreements or multilateral tax treaties to meet the needs of philanthropists and their donees.

When one thinks of previous pragmatic philanthropic endeavours to claim the ‘philanthropic right of transfer’ one of the most successful to date has been the TGE’s own Transnational Giving Europe Project. Developed by the sector for the sector, the scheme covers 19 countries and in 2016 TGE enabled 5,084 gifts and a total amount of €6,380,054 to be transferred to 334 non-profit organizations across those 19 European countries, to support education, culture, international development, health, social matters, third sector initiatives, environment or religion.<sup>187</sup>

One of the more low-key proposals of the Boosting Philanthropy Report is the recommendation that there be greater provision of public information on the principle of equal tax treatment and its application to cross-border philanthropic tax claims coupled with better training for tax staff in each Member State on the existence of and how to deal with the comparability test.<sup>188</sup> The recommendation is clearly aimed at tax authorities in terms of the provision of clearer information and staff training. While the latter training very much lies within the gift of the revenue authorities, there is arguably space for the first part of this recommendation – the provision of clearer public information – to be acted upon by others.

An opportunity exists – just as it did with the creation of Transnational Giving Europe<sup>189</sup> – for philanthropic organisations to assist in filling the information deficit that exists when it comes to unpacking the different national tax reclaim procedures for donors and recipient organisations in the various EU Member States. The creation of a website resource, providing details on existing or emerging Member State tax authority procedures, coupled with the explanatory guidance or links to the relevant application forms necessary for both donors and public benefit recipient organisations to begin the tax refund/exemption process would be a valuable step forward. Engaging with individual Member State tax authorities and encouraging them to identify a specific contact within each tax authority as a central contact point for queries would also help to create an informed channel for philanthropic communication on tax matters and might prompt tax authorities to ensure that the official in receipt of all such queries was well versed to deal with them.

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<sup>186</sup> European Commission, *Engaging Philanthropy for European Research: Report by an Expert Group on Fundraising by universities from philanthropic sources: developing partnerships between universities and private donors* (European Commission, DG for Research, 2007) at 82.

<sup>187</sup> TGE Annual Report 2016, at 5.

<sup>188</sup> *Boosting Philanthropy Report*, n. 175 above, at 15.

<sup>189</sup> <http://www.transnationalgiving.eu/en/>.

## The Potential Reach of the OECD Multilateral Competent Authority Agreement and its Impact on Philanthropy

The Common Reporting Standard (CRS), developed in response to a G20 request and approved by the OECD Council on 15 July 2014, calls on jurisdictions to obtain information from their financial institutions and automatically exchange that information with other jurisdictions on an annual basis. It sets out the financial account information to be exchanged, the financial institutions required to report, the different types of accounts and taxpayers covered, as well as common due diligence procedures to be followed by financial institutions.

The standard is implemented at EU level in a Directive on Administrative Cooperation in the field of taxation.<sup>190</sup> The CRS Multilateral Competent Authority Agreement (CRS MCAA), signed in October 2014 with currently over 90 signatory jurisdictions, operationalises the automatic exchange of information under the CRS on the basis of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters.<sup>191</sup>

The CRS came into force in January 2016 and by August 2017, there were over 2000 bilateral exchange relationships activated with respect to more than 70 jurisdictions committed to the CRS, with first exchanges scheduled to take place in September 2017. At its heart, the CRS is an information exchange regime aimed at international tax transparency: 'financial institutions' are required to pass information about their clients to their clients' domestic tax authorities with the aim of preventing the use of offshore structures to evade tax. The implementation of this regime has given rise to new difficulties for certain UK philanthropic institutions which may qualify as 'financial institutions' as defined by the UK's International Tax Compliance Regulations 2015, introduced to give effect to both the European Directive and the CRS MCAA. The UK's regulations affect charities in two ways:

- (a) the definition of a 'financial institution' (to which CRS applies) is drawn widely and many charities fall within the definition; and
- (b) charities may be asked by their bank or investment manager to provide details of their CRS status or classification.

The impact of these UK regulations on charities would appear to be that there is no charity exemption. A charity considered to be a 'Financial Institution' has active obligations to HMRC, while others have to self-certify their status as 'Active Non-Financial Entities' to third parties such as banks. In this regard, if more than 50% of a charity's incoming resources in the last three calendar years was derived from investments and at least some part of the charity's assets are managed by an external investment manager, the charity is likely to be caught as a 'Financial Institution' and required to gather data and report on 'Account Holders.' The definition of the latter depends on legal form – incorporated charities will not have to treat their grantees as account holders whereas charitable trusts and unincorporated

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<sup>190</sup> See Council Directive 2011/16/EU as amended by Council Directive 2014/107/EU.

<sup>191</sup> List of CRS MCAA Signatories at August 30, 2017 available at <http://www.oecd.org/tax/automatic-exchange/international-framework-for-the-crs/MCAA-Signatories.pdf>.

charitable associations will be obliged to treat their grantees as account holders. An incorporated charity that holds property on special trusts (including permanent endowment) will be treated in the same manner as a charitable trust for UK CRS purposes.

No other European jurisdiction appears to have adopted a similar approach to the UK to date in its implementation of the CRS MCAA and so philanthropic institutions outside of the UK should not encounter similar problems in terms of tax reporting. What this example highlights, however, is the constant possibility for differing interpretations of international tax obligations to cause new obstacles to the facilitation of European philanthropy and thus the constant need for vigilance by the philanthropic community.

## 6. Testing the Strength of Soft Law to Enhance Philanthropic Space in Europe

*“Soft law instruments range from treaties, but which include only soft obligations (“legal soft law”), to non-binding or voluntary resolutions and codes of conduct formulated and accepted by international and regional organisations (“non-legal soft law”), to statements prepared by individuals in a non-governmental capacity, but which purport to lay down international principles.”<sup>192</sup>*

*“Strictly speaking, soft law does not include political or moral commitments; these are, if they exist in any meaningful way to begin with, commitments of a political or moral nature, and are thus on their own terms (or rather, on their interpreter’s terms) not legal at all. And if they are not legal at all, it follows that they cannot be softly legal either. The term soft law, thus (admittedly loosely) delimited, denotes those instruments which are to be considered as giving rise to legal effects, but do not (or not yet, perhaps) amount to real law.”<sup>193</sup>*

In defining the meaning of soft law in their 2000 seminal article on the concept of legalisation, Abbott et al state that “the realm of ‘soft law’ begins once legal arrangements are weakened along one or more of the dimensions of obligation, precision, and delegation. This softening can occur in varying degrees along each dimension and in different combinations across dimensions.”<sup>194</sup> For the purposes of this chapter, soft law is approached from two different perspectives: sector designed regimes (which may take effect at a national or cross-regional level, respectively) and initiatives by policy makers at EU level (looking at European Commission efforts to utilise soft law in the regulation of public benefit organisations) and includes the use of principles of good practice, ethical codes of conduct, charters, quality marks and civil society framework initiatives instead of, or as a complement to, hard law options.

Research on the interaction between regimes of soft and hard law (commonly also referred to as self-regulation and statutory regulation) in the context of the non-profit sphere has sought to unpack the relationship between the two modes of regulation and to better understand the factors prompting the adoption of one mode over the other and the basis for switching from soft to hard law (and vice versa).<sup>195</sup> The threat of government action is a key driver for self-regulation efforts. Self-regulatory regimes are often a pre-emptive response to a feared statutory regulatory regime such that sector-led soft law may

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<sup>192</sup> Christine Chinkin, “The Challenge of Soft Law: Development and Change in International Law” (1989) 38(4) *The International and Comparative Law Quarterly*, 850-866, at 851.

<sup>193</sup> Jan Klabbers, “The Redundancy of Soft Law” (1996) 65 *Nordic Journal of International Law* 167-182, at 168.

<sup>194</sup> Kenneth W. Abbott, Robert O. Keohane, Andrew Moravcsik, Anne-Marie Slaughter and Duncan Snidal, “The Concept of Legalization” (2000) 54(3) *International Organization*, 401-419; see also Kenneth W. Abbott and Duncan Snidal, “Hard and Soft Law in International Governance” (2000) 54(3) *International Organization*, 421-456, at 422.

<sup>195</sup> See Oonagh B. Breen, Alison Dunn and Mark Sidel (eds.), *Regulatory Waves: Comparative Perspectives on State Regulation and Self-Regulation Policies in the Nonprofit Sector* (Cambridge: Cambridge University Press, 2017).

be used as a risk-mitigation mechanism to ward off unwanted legally binding intervention.<sup>196</sup> As well as the threat of government action, a complementary driver for self-regulation efforts is under-regulation often brought about by a lack of government action to regulate. This regulatory gap may be seen in Scotland where, in the face of an inadequate charity regulatory framework and lack of action by government, the non-profit sector initiated self-regulation in order to stem falling trust and confidence as a result of various sector governance scandals. This in turn led the non-profit sector to lobby government to provide a workable sector-specific state regulatory regime, demonstrating how one regulatory initiative pushes for the next regulatory wave.<sup>197</sup>

The main advantages usually associated with self-regulatory codes that come from the sector itself are:

- (a) The direct relevance of the principles developed is assured if those principles are developed by an engaged sector for and on behalf of the sector;
- (b) Unlike hard law, soft law principles can more easily be amended as they evolve both because of their non-statutory basis and their closeness to the grassroots organisations who both develop and apply them;
- (c) Using soft law provides an opportunity to raise the governance standards in a progressive way which can be more relevant and effective than externally imposed compliance-based regulation that is based on a command and control model.<sup>198</sup>
- (d) Politically, some states are more willing to allow public benefit organisations to experiment with self-regulation mechanisms which, if effective, may pre-empt the state introducing statutory regulation<sup>199</sup> or inform the later statutory regulation adopted.<sup>200</sup>

The classic disadvantages associated with self-regulatory codes are the ease with which an organisation can self-certify compliance and the lack of active monitoring of compliance levels by the coordinating body. Lack of effective sanctions is also commonly cited as a factor that undermines the robustness of non-statutory regimes with relatively few examples of disciplinary action against or expulsion of non-compliant members from the circle of code adherents. Without the pressure of legal enforcement, low participant take-up rates can also be a disadvantage of self-regulatory codes, leading to a lack of critical mass for the code's acceptance.<sup>201</sup> Coordinating bodies will often ascribe the low subscription rate to inadequate investment in the publication of the codes to the sector rather than lack of interest on the part of organisations. Research has shown that state support is often crucial to the initial establishment of self-regulatory codes and the state's willingness to step in with regulation in the

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<sup>196</sup> Breen et al, *Regulatory Waves*, n.195 above, at 4.

<sup>197</sup> See Alison Dunn, 'Eddies and Tides: statutory regulation, co-regulation and self-regulation in charity law in Britain' in Breen et al, *Regulatory Waves*, n.195 above, at 21.

<sup>198</sup> See EFC and DAFNE, *Exploring Transparency and Accountability Regulation of Public-Benefit Foundations in Europe* (2011) at 38 [hereinafter '*EFC/DAFNE Report 2011*'].

<sup>199</sup> This approach, sometimes referred to as hybrid or co-regulation has been trialled in Ireland and in England and Wales in relation to fundraising regulation. See Oonagh B. Breen, "The Perks and Perils of Non-Statutory Fundraising Regulatory Regimes: An Anglo-Irish Perspective" (2012) 23(3) *Voluntas* 763-790.

<sup>200</sup> See the Finnish case study presented below as an example of this in action.

<sup>201</sup> See *EFC/DAFNE Report 2011*, n.198 above, at 39.

event that the self-regulatory code is unsuccessful is also a critical factor in ensuring survival and sustainability of a code.<sup>202</sup> An interesting statutory power in this regard is the power of the Irish Charity Regulator under the Charities Act 2009 to approve existing self-regulatory codes, thereby giving regulatory imprimatur to a voluntary code, developed by the sector.<sup>203</sup>

Equally, the necessity of there being coherent leadership – through a peak or umbrella body within the sector – that can foster sufficient consensus and buy-in from public benefit bodies has also proved to be an important factor in the success of self-regulatory regimes.<sup>204</sup>

## Sector Designed Self-Regulatory Regimes

In the 2011 EFC/DAFNE *Report on Exploring Transparency and Accountability Regulation of Public-Benefit Foundations in Europe*, the authors' field study of European national associations of donors and foundations in 24 countries found that 15 associations of foundations had developed codes of practices or standards for their members resulting in a total of 19 codes of conduct/ethical codes directly relevant to public benefit foundations.<sup>205</sup> Of these 15, six were donors' forum initiatives while a further nine were from national associations of foundations in the countries concerned. Four of the initiatives were the result of collaboration by informal groups of foundations and non-profit organisations and two of the codes examined had an intrinsically international scope.<sup>206</sup>

Common features of the codes reviewed were that they were mainly self-certifying and in general there was no active monitoring of compliance<sup>207</sup> and no certification procedure as such.<sup>208</sup> It was a common practice to publish the list of professed adherents to the codes of practice on a coordinating association's website.<sup>209</sup> The codes focused on issues relating to governance and management, reporting requirements and the stewardship of funds. A number also considered the issues pertaining

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<sup>202</sup> Breen et al, *Regulatory Waves*, above n. 195.

<sup>203</sup> Charities Act 2009, s.14(1)(i). The Irish Charities Regulatory Authority exercised this power for the first time in 2017 by statutorily approving a revised version of the non-profit sector's Statement of Guiding Principles for Fundraising. See CRA, *Guidelines for Charitable Organisations on Fundraising from the Public* (September 2017), available at [http://www.charitiesregulatoryauthority.ie/en/CRA/Guidance%20for%20Fundraising%20\(English\).pdf/Files/Guidance%20for%20Fundraising%20\(English\).pdf](http://www.charitiesregulatoryauthority.ie/en/CRA/Guidance%20for%20Fundraising%20(English).pdf/Files/Guidance%20for%20Fundraising%20(English).pdf)

<sup>204</sup> Ibid.

<sup>205</sup> See *EFC/DAFNE Report 2011*, n.198 above, at 21.

<sup>206</sup> Namely, *Spain's Asociación Española de Fundaciones Principes* (see [http://www.fundaciones.org/EPORTAL\\_DOCS/GENERAL/AEF/DOC-cw57697e9f07c87/BuenGobiernoYBuenasPrActicasdeGestiOnparalasFundaciones.pdf](http://www.fundaciones.org/EPORTAL_DOCS/GENERAL/AEF/DOC-cw57697e9f07c87/BuenGobiernoYBuenasPrActicasdeGestiOnparalasFundaciones.pdf)) and the *EFC/Council on Foundations Principles of Accountability in International Philanthropy* (2007) available at <https://www.cof.org/sites/default/files/documents/files/PrinciplesAccountability%20for%20International%20Grant%20making.pdf>.

<sup>207</sup> Only six of the Codes studied by the *EFC/DAFNE Report 2011* indicated mechanisms for actively monitoring compliance.

<sup>208</sup> An exception in this case was Luxembourg's Code de Bonne Conduit which used a combination of peer and third-party certification with five out of six of its commitments being peer-reviewed while the financial transparency commitment was outsourced to an external auditor to certify the annual accounts of adhering organisations.

<sup>209</sup> *EFC/DAFNE Report 2011*, n.198, at 22.



to overhead costs, 'know your beneficiary rules' and fiduciary principles relating to the control and use of such funds.<sup>210</sup> While many of the codes indicated that non-compliance with the code principles could incur sanction, only one DAFNE member reported having excluded a member for non-compliance with the self-regulatory mechanism.<sup>211</sup> Anecdotal evidence from DAFNE in the period since the Report on Transparency's publication suggests that self-regulatory codes have helped to clarify conditions for membership of national associations and to raise professional standards and are primarily perceived as motivating instruments encouraging self-reflection and performance improvement - rather than as mere compliance instruments.

### ***The potential of self-regulatory regimes to protect the space for philanthropy in Europe***

Regulation does not exist in a vacuum and the complementary nature of statutory regulation (hard law) and non-statutory regulation (soft law) is worthy of study if we are serious as to how best to leverage this relationship in the interests of promoting philanthropy in Europe. Two national case studies illustrate the ways in which traction between the state and the sector on issues of regulation can be used to support rather than stifle philanthropy.

### ***The Council of Finnish Foundations Codes of Governance***

Established in 1970, the Council of Finnish Foundations has 180 members who account for more than 70 percent of the total wealth of the Finnish foundation sector.<sup>212</sup> In 2010, the Council drafted and issued for consultation a Code of Good Governance for Foundations. The Code, approved by the membership, aims to encourage foundations to prepare and maintain their own operational guidelines in accordance with best practice.<sup>213</sup> Updated and reissued in 2015, following the passing of Finland's new Foundation Act 2015,<sup>214</sup> the Code of Good Governance is based both on the mandatory requirements of the new law and best practices drawn from the Council's earlier operational code, Best Practices for Finnish Foundations (2004).<sup>215</sup> Focussing on pragmatic guidelines for strategy, board procedures, and asset management, the Code is written more in the form of a manual for the Board's use than necessarily a set of rules and in its written form, it does not distinguish between mandatory

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<sup>210</sup> The growing awareness of philanthropic actors of the risks of terrorist financing and the development, at self-regulation level by the sector, of controls and due diligence measures on transfers and collections of funds is acknowledged by the European Commission in its *Staff Working Document accompanying the Report from the Commission to the European Parliament and to the Council on the assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border situations COM(2017) 340 final Annex 2*, at 187-188 available at [http://ec.europa.eu/newsroom/document.cfm?doc\\_id=45653](http://ec.europa.eu/newsroom/document.cfm?doc_id=45653).

<sup>211</sup> *EFC/DAFNE Report 2011*, n.198, at 25.

<sup>212</sup> See <https://www.saatiopalvelu.fi/en/coff-council-of-finnish-foundations.html>.

<sup>213</sup> The revised 2015 Code of Good Governance for Foundations may be accessed at [https://www.saatiopalvelu.fi/media/srnk\\_good-governance-of-foundations.pdf](https://www.saatiopalvelu.fi/media/srnk_good-governance-of-foundations.pdf).

<sup>214</sup> Finnish Foundations Act 2015, 487/2015 available in Finnish at <http://www.finlex.net/fi/laki/kokoelma/2015/sk20150487.pdf>.

<sup>215</sup> The Council of Finnish Foundations Best Practice for Finnish Foundations may be accessed at [https://www.saatiopalvelu.fi/media/tietolaari-files/julkaisut/best-practice\\_screen.pdf](https://www.saatiopalvelu.fi/media/tietolaari-files/julkaisut/best-practice_screen.pdf).

legal requirements and best practice guidelines but conveys both in indicative language. The Code also clearly indicates that it is not a binding document, and its application is not supervised.<sup>216</sup>

In developing the new law on foundations, which amended the existing Finnish Foundations Law from the 1930s, the Finnish Ministry of Justice set up a working group on 5 January 2012 to draft a proposal for the new Foundations Act. The working group's report on the new Foundations Act was submitted to the Minister of Justice on 15 May 2013,<sup>217</sup> following which a public consultation was held in the summer of 2013. The Finnish Code of Governance was a key resource in the drafting of the new Act, illustrating the powerful persuasive influence of good non-statutory regulation on new statutory regulation.<sup>218</sup> The new Foundations Act clarifies the distinction between permitted and prohibited activities of foundations, establishes an effective framework for the development of the administration and operations of a foundation, and creates better means to conduct the internal and external monitoring of foundations. The increased emphasis on the regulation of the administration and greater disclosure and transparency requirements for foundations along with the focus on related party transactions all stem from the self-regulatory Code on the Governance of Foundations.

### ***The Swiss Foundation Code 2015***

In 2004, "SwissFoundations," the Association of Swiss Grant-making Foundations set up a task force to compile a guide containing recommendations for the establishment and management of Swiss foundations. First published in 2005, the Swiss Foundation Code was developed for use by grant-making foundations, i.e., foundations with ample assets and sufficient income to support and further their own or third-party projects. In the words of the Code, such grant-making foundations "are not subject to owner or market controls, and thus, are independent of the "outside world."<sup>219</sup> Despite the deliberate focus on grant-making foundations, the Code authors consider it also useful to other types of foundation.

The Code, which has been revised twice, in 2009 and most recently in 2015, is based on three main principles and supported by a further 29 recommendations.<sup>220</sup> The central principles focus on:

1. Effective realization of the foundation's purpose: 'The foundation is obliged to carry out the foundation's purpose as set out by the founder in the most effective, efficient and sustained manner possible.'
2. Checks and balances: 'By taking appropriate organizational and administrative measures, the foundation ensures that, in all important decisions and dealings, there is a balance between management and monitoring.'

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<sup>216</sup> Finnish Code of Good Governance for Foundations, above n.213, at 6.

<sup>217</sup> Mietintöjä ja lausuntoja, *Uusi säätiölaki Säätiölain uudistamistyöryhmän mietintö*, 23/2013 (report only available in Finnish from the Ministry of Justice website).

<sup>218</sup> Source: Liisa Suvikumpu, Council of Finnish Foundations, at the European Foundation Centre Annual General Assembly Meeting 2016, Amsterdam.

<sup>219</sup> Swiss Foundation Code 2009, at 12.

<sup>220</sup> *The Swiss Foundation Code 2015: Principles and recommendations for the founding and leadership of grant-making foundations*, (co-written by Thomas Sprecher, Philipp Egger, Georg von Schnurbein).

3. Transparency: 'The foundation board ensures that the foundation's goals, activities and structures are as transparent as possible and appropriate to the foundation's purpose.'<sup>221</sup>

The subsequent recommendations focus on four areas of foundation life, namely, establishment, governance, grant-making and finances. The Code is non-binding and forms part of a broader self-regulatory jigsaw which provides Swiss philanthropic bodies with the possibility of adherence to Swiss GAAP ARR 21 for social non-profit organizations<sup>222</sup> or certification by the Zewo Standards for non-profit institutions,<sup>223</sup> which since January 2016 have been revised to incorporate more fully the Swiss NPO Code 2006,<sup>224</sup> which covers all Swiss non-profit organisations, including foundations.<sup>225</sup> This latter code, created in 2006 by a parallel working group to that which developed the Swiss Foundation Code, operates on a comply-or-explain basis thus leaving code signatories with less discretion regarding adoption of its principles than the Swiss Foundation Code when they sign up. From a philanthropic perspective, the Swiss Foundation Code is seen by many as a landmark code, given its particular focus on large grant-making bodies. Reflecting on the 2015 revised code, Specking notes:

"The beauty of the code is that it is voluntary; it guides and enhances reflection on the matter according to the specific circumstances of a foundation, and is not binding. I believe the SFC 2015 is a very valuable piece of wisdom that should be taken into consideration by all players in the philanthropy sector. Grant-making foundations should reflect on the recommendations and guiding principles. But lawyers, trustees and other charitable structures are responsible for discussing and implementing the suggested content from within the code at their own discretion."<sup>226</sup>

In evaluating the impact of the Swiss Foundation Code in the 2015 edition of the Code, the authors point to the Code's frequent use by the Swiss Federal Administrative Court when citing objective criteria for the proper establishment of foundations as well as the reliance of the Liechtenstein Supreme Court on the Code in 2009 in a case concerning a conflict of interest in which the Court ruled that in all such cases the foundation in question should take account of Swiss Foundation Code Recommendation 11 on dealing with conflicts. Aside from the courts, the Swiss Federal Council has also cited the Code in Parliamentary initiatives and in its reports to the Swiss Parliament in 2013.<sup>227</sup>

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<sup>221</sup> Thomas Sprecher, "Switzerland: the Swiss Foundation Code 2009—from corporate governance to foundation governance" (2010) 16(6) *Trusts & Trustees*, 523-532.

<sup>222</sup> See <https://www.fer.ch/>.

<sup>223</sup> See [www.zewo.ch](http://www.zewo.ch). Zewo sets standards for Swiss charities. These standards cover the following aspects: ethics and integrity, corporate governance, efficient use of funds, results, true and fair accounting, transparency, accountability as well as fundraising and communication. Zewo monitors applicant charities against these standards and award those organizations, which meet the standards the Zewo-seal.

<sup>224</sup> See [http://www.swiss-npocode.ch/cms/images/swiss\\_npocode/swiss\\_npo\\_code\\_maerz\\_2010.pdf](http://www.swiss-npocode.ch/cms/images/swiss_npocode/swiss_npo_code_maerz_2010.pdf).

<sup>225</sup> See <http://www.swiss-npocode.ch/cms/>.

<sup>226</sup> Heiko Specking, "The Swiss Foundation Code 2015: A state of the art regulatory for grant-making foundations" (October 20, 2015) available at <http://www.alliancemagazine.org/blog/the-swiss-foundation-code-2015-a-state-of-the-art-regulatory-for-grant-making-foundations/>.

<sup>227</sup> Swiss Foundation Code 2015, n. 220 above, at 173.

## **Regulatory Consequences**

Returning to Abbott et al's definition of soft law occurring when legal arrangements are weakened along the dimensions of obligation, precision and delegation, one can see that the Finnish and Swiss case studies are classic examples of soft law. In neither of these cases is there a legal obligation to sign up to the codes other than sector peer pressure and public expectation (to varying degrees depending upon how high the public profile of the code is). The codes are based on high level, and at times one might say vague, principles, leaving individual organisations to determine how best to meet their requirements further supported with a 'comply or explain' approach – so common in many self-regulatory regimes now -- in either case. Finally, in both cases, the extent to which codes delegate authority to designated third parties including courts, arbitrators, and administrative organizations to implement agreements is non-existent, marking out both codes in their primary form as non-legalized. Notwithstanding their clear designation as forms of soft law, their influence on the form of subsequent hard law cannot be ruled out and gives further support to the Regulatory Waves theory.<sup>228</sup>

## **EU Level Attempts at Soft Law Regulation of Non-Profits**

Moving away from sector-designed national and regional attempts at soft law regulation and turning to more European-led efforts, the European Commission has dipped its toe into the soft law arena on several occasions in the past in an attempt to create a regulatory framework for non-profits operating in the EU. As will be recalled from Chapter 2, the European Commission lacks a legal treaty basis on which to promulgate European measures to regulate non-profits *qua* non-profits. While the Commission can regulate non-profits (including philanthropic bodies) as part of cohort of entities when it is acting under more generalized powers relating to labour law, competition law, etc., regulating non-profits in the non-profit regulatory space has proven to be more difficult given the lack of capacity for the Commission to propose hard laws relating to non-profits. To this end, the Commission has, on occasion, resorted to soft law attempts to encourage the type of non-profit behaviour that it would like to see. In practice, the Commission in its regulatory efforts does not distinguish between civil society space and philanthropic space when it comes to soft law, making its application a blunt instrument at times.

### **Commission Communication on a Framework for a Code of Conduct (2005)**

In 2005, following the London and Madrid bombings, the Commission issued Communication (2005)620 recommending, inter alia, a Framework for a Code of Conduct to enhance transparency and accountability of non-profits and to reduce the risk of abuse of the non-profit sector.<sup>229</sup> In short, the aim of Commission Communication (2005)620 was to introduce a European regulatory (albeit it voluntary) regime for public benefit entities. Commission Communication (2005) 620 spoke to two issues—the

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<sup>228</sup> Breen et al, *Regulatory Waves*, n. 195, above.

<sup>229</sup> Commission of the European Communities, *The Prevention of and Fight Against Terrorist Financing through Enhanced National Level Coordination and Greater Transparency of the Non-Profit Sector*, COM (2005) 620 final (Nov. 29, 2005) [hereinafter *Commission Communication (2005) 620 final*].

need for enhanced national coordination by Member States and ‘relevant actors’ in the exchange of information to cut off terrorist financing; and secondly, the need to address vulnerabilities of non-profit organizations to terrorist financing and other criminal abuse.<sup>230</sup> The actual provisions of the Framework for the Code relate predominantly to the need for registration of non-profit organisations and the proper keeping of accounts. Although the Commission recognised the need for coordination amongst Member States in the Code’s operation, no guidance was given in the Communication as to how this could best be achieved; nor was there any consideration of how the additional Code requirements would affect existing national regulatory requirements.<sup>231</sup> Despite subsequent European Council endorsement of the Code<sup>232</sup> and Commission attempts to encourage wide-spread application, implementation has been sporadic.<sup>233</sup>

### ***Commission Discussion Paper on Non-profit Organisation Guidelines under Consultation (2010)***

Drawing heavily from its 2005 Framework for a Code of Conduct, the Commission issued a 4-page Discussion Paper to a select group of invited NGOs and Member State representatives at its third transparency and accountability in the non-profit sector conference in 2010.<sup>234</sup> The Discussion Paper identified six specific areas in which the Commission intended to develop guidance, namely: a) basic principles for good non-profit organization practice; b) good governance; c) accountability and transparency; d) relations to the donor; e) relations to the beneficiary; and f) suspicious activity reporting. The principles set out under these headings although addressed broadly to ‘non-profit organizations’ were aimed at entities that use their assets “exclusively for charitable or other legitimate purposes” and whose activities are “directed towards the attainment of the organisation’s stated public benefit goals.”<sup>235</sup> The Commission consulted only those select NGOs invited to the launch of the Discussion Paper and no broader public consultation was held nor was the Discussion Paper made publicly available on DG Justice and Home Affairs’s website. Some NGOs published both their responses, many of which voiced concerns about the both the guidelines and the Commission’s approach to the consultation, along with the Discussion Paper itself bringing some badly needed transparency and clarity to the area.<sup>236</sup>

To date, the Commission’s expressed intention to develop these guidelines for publication in the form of Commission Communication has not occurred. Nevertheless, the website of DG Home Affairs

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<sup>230</sup> Oonagh B. Breen, ‘Through the Looking Glass: European Perspectives on Non-profit Vulnerability, Legitimacy and Regulation’ (2011) 36(3) *Brooklyn Journal of International Law* 947.

<sup>231</sup> *Ibid.*, at 961.

<sup>232</sup> Press Release, Council of the Eur. Union, 2696th Council Meeting: Justice and Home Affairs (Dec. 1–2, 2005), at 32, available at <http://europa.eu/rapid/pressReleasesAction.do?reference=PRES/05/296&format=HTML&aged=0&lg=sl&quiLanguage=en>.

<sup>233</sup> Breen, “Through the Looking Glass,” n. 230 above, at 961. See also, Oonagh B. Breen, “European Non-Profit Oversight: The Case for Regulating from the Outside In” (2016) 91(3) *Chicago-Kent Law Review* 991-1020.

<sup>234</sup> European Commission, DG Home, *Discussion Paper on Voluntary Guidelines for EU Based Non-profit Organisations* (July 2, 2010) [hereinafter Discussion Paper].

<sup>235</sup> Breen, “Through the Looking Glass,” n. 230 above, at 977.

<sup>236</sup> For a full discussion of the substantive content of the Voluntary Guidelines outlined in the Discussion Paper and the concerns raised by respondent NGOs, see Breen, “Through the Looking Glass,” n. 230 above.

continues to advocate the need for voluntary guidelines to further enhance the accountability and transparency of non-profits, providing:

“The great majority of non-profit organisations (NGOs) carry out completely legitimate and valuable work. However, the potential vulnerability of NGOs for terrorist financing has been revealed by cases in the EU and in non-EU countries (studies). Voluntary guidelines for the sector could be a means to enhance transparency and accountability of NGOs and to reduce their potential abuse for terrorist financing. The Commission aims to closely involve the NGO sector and EU States in its work in this field.”<sup>237</sup>

Thus, like its predecessor the 2005 Framework Code, the 2010 Discussion Paper has not achieved the impact hoped for by the Commission. As a form of soft law, the ability of the Commission to enforce the voluntary guidelines on unwilling non-profits has been limited to date. While the Framework and Guidelines have exhibited quite a degree of precision in terms of their asks of non-profits in some respects, the lack of precision in how such requirements are to be coordinated by and between Member States or how the guidelines interact with existing national requirements has not been addressed by the Commission. Finally, no mechanism has been included in either the 2005 Communication or the 2010 Discussion Paper that would solve the delegation issue raised by Abbott et al.<sup>238</sup>

#### ***Likely Next Steps: The Supra-National Risk Assessment Framework and Mitigation Measures***

In June 2017 the European Commission published its *Supra National Risk Assessment Report*, assessing the vulnerability of financial products and services to risks of money laundering and terrorist financing, including also risks related to the non-profit sector, the first time ever such an analysis is conducted at EU level.<sup>239</sup>

Building on the engagement and constructive feedback received from non-profit representative organisations over the course of the consultation period in 2016-17, the Report acknowledges the analytical challenges of assessing the non-profit sector’s vulnerability to Terrorist Financing given that the sector is characterised by a variety of structures and activities which present varying degrees of risk exposure and risk awareness.<sup>240</sup> Identifying the common characteristics of non-profit vulnerabilities, the Commission reports that existing AML/CFT requirements are not necessarily considered by the competent authorities as adequate to address the specific needs of the non-profit sector and controls in place differ, depending on the Member State concerned. Interestingly, from the perspective of European philanthropy, the Commission recognises that “controls in place are more efficient when dealing with collection of funds within the EU which makes the level of vulnerabilities lower than for transfers of funds or expenditure outside the EU where more material weaknesses remain.”<sup>241</sup> The

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<sup>237</sup> [http://ec.europa.eu/home-affairs/what-we-do/policies/crisis-and-terrorism/financing\\_en](http://ec.europa.eu/home-affairs/what-we-do/policies/crisis-and-terrorism/financing_en).

<sup>238</sup> Abbott et al, *The Concept of Legalization*, n. 194, above.

<sup>239</sup> See [http://ec.europa.eu/newsroom/just/item-detail.cfm?item\\_id=81272](http://ec.europa.eu/newsroom/just/item-detail.cfm?item_id=81272).

<sup>240</sup> Report from the Commission to the European Parliament and the Council on the assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border activities, COM (2017) 340 final, at 7.

<sup>241</sup> *Ibid.*

report also acknowledges non-profit organisations' concerns over exposure to de-risking or financial exclusion (when financial institutions become reluctant to provide financial services to non-profits) as a concern that should be kept in mind when addressing AML/CFT policy. In its Report recommendations, the Commission does not propose any European regulation of non-profits but it does recommend Member States to ensure appropriate non-profit coverage in their national risk assessments as part of their risk mitigation measures.<sup>242</sup> In its more detailed analysis,<sup>243</sup> the Commission specifically proposes:

- The provision of Commission guidance and/or training to non-profits in receipt of EU funding on the relevant EU legal framework, as well as on how to identify risks and meet due diligence requirements;
- The organisation of multi-stakeholders exchange involving all professional sectors, in particular the financial sector, involved in business with non-profits.

At a member state level, it advises that:

- Member States should ensure better non-profit involvement into national risk assessments, into the development of informational and awareness programs designed to counteract the risk of being abused - support non-profits by providing awareness raising materials for non-profits (at member State as well as at EU level); and
- Member States should also further analyse the risks faced by the non-profit sector.

The provision of any further Commission guidance on the identification of risks and the need to meet due diligence requirements when dealing with the transfer of funds is likely to take the form of soft law which will impact on philanthropic organisations. If the Commission has learnt anything from its forays over past decade into the realm of framework codes of conduct and voluntary guidelines, it will need to share its draft guidance and consult more broadly with non-profit stakeholders than on previous occasions and be willing to amend and adapt its proposed guidance in light of received feedback if it is to have any hope of emulating the more successful national experiences of soft law implementation. To this end, there is also a window of opportunity available to philanthropic organisations to engage with the Commission and national competent authorities in facilitating more informed conversations around the risks and challenges facing philanthropic giving within and without Europe. It is now more than five years since the last comprehensive field study of donors and foundations' codes of practice in Europe<sup>244</sup> and much has happened in this time. To this end, further research is now required around the possible role that self-regulation could play in enlarging the space for philanthropy in different European countries.

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<sup>242</sup> Ibid, at 16.

<sup>243</sup> *Commission Staff Working Document accompanying the Report from the Commission to the European Parliament and to the Council on the assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border situations* Annex 2, at 189 available at [http://ec.europa.eu/newsroom/document.cfm?doc\\_id=45653](http://ec.europa.eu/newsroom/document.cfm?doc_id=45653).

<sup>244</sup> See n.198 above.

## 7. Conclusions: Mapping the Enabling Space for Philanthropy in Europe and Identifying New Horizons for Further Research

This report set out to examine the enabling environment for institutional philanthropy in Europe. In this regard, it focused first on the identification of ‘the philanthropic space’ which it separated from civil society space more generally and defined as the environment within which donors/funders (and the philanthropic organisations they may create) are facilitated in their use of their private wealth for the public benefit. Secondly, it assessed the current climate for European philanthropy before outlining ways in which an enabling environment – i.e., one in which institutional philanthropy could thrive without suffering unduly from political interference or legal or administrative obstruction at European or national level – might be brought about. To this end, the preceding chapters have questioned how big the space for institutional philanthropy is within Europe and how this space is currently changing and what steps could be taken to further support and facilitate the growth of European philanthropy within Europe.

### Measuring the Space

Chapter 2 identified that one of the major infrastructural challenges faced by policymakers seeking to introduce enabling European legislation for institutional philanthropy is the lack of an apparent specific legal Treaty basis on which to ground such proposals. The first lesson taught by the previous failed legislative attempts in this area is that “If you always do what you’ve always done, you always get what you’ve always gotten.” A changed approach to legislative proposals is thus required if we are serious about developing European legal vehicles to facilitate cross border philanthropy by way of European regulation. One proposal would be to avail of the ‘enhanced cooperation’ mechanism, set out in Art 20 TFEU, when using Art 352 TFEU as the legal basis to adopt any future non-profit oriented European regulatory measures. The advantage of the enhanced cooperation mechanism is that it overcomes the need for unanimity in Council that is required by Art 352, which has been a constant stumbling block for European non-profit regulation.

In conjunction with this proposal, it may also be worth considering other, perhaps more flexible legislative options to EU Regulations when seeking to legislate for new non-profit European-wide legal vehicles. Use of an EU Directive instead of an EU Regulation would provide Member States with greater flexibility as to the means to achieve the agreed ends, overcoming perhaps the looming threat of Council veto that exists whenever Art 352 TFEU forms the legal basis. To this end, the potential for an EU Directive that would create a new legal form for institutional philanthropy at national level with a minimum common denominator in all EU countries, thereby facilitating cross border recognition, could be explored. The option for such a Directive for philanthropic organisations, modelled along similar lines to the Proposal for a Directive on Single-member private limited liability companies,<sup>245</sup> may thus warrant further analysis in this regard. Instead of creating a new European legal form, the Directive would ask Member States to recognise in their national law a philanthropic organisation with a number of

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<sup>245</sup> COM/2014/0212 final.



harmonised main requirements under one common name shared throughout Member States. The Directive could allow Member States the freedom to decide how to introduce such a legal form at national level, whether by way of an additional instrument or an instrument replacing currently existing foundation forms. Although not a risk free legislative avenue given the difficulties into which the proposed *Societas Unius Personae* (or SUP, as it is known) Directive itself has run,<sup>246</sup> it may nevertheless be worth further exploration from a philanthropic perspective.

Although the EU has been conscious of the shrinking space for civil society globally, its policy response to this challenge has been predominantly focused on external relations and actions to protect civil society space outside of the EU.<sup>247</sup> When it comes to the EU's internal policies on protecting civic space, chapter 2 also highlighted that the EU's framework is far less well developed. The policy framework and policy tools that exist in the context of internal relations are lacking, leaving the EU very ill-equipped to tackle restrictions on civil society space within the Union and growing threats to freedom of philanthropy within the EU, as illustrated by the situations in Hungary and recent developments in Poland. To this end, Chapter 2 mapped out the satellite institutions that play a role in protecting or legally enabling civil society and consequently impact on the philanthropic space. As the more general squeezing of civic space reverberates in the philanthropic space, further research establishing the implications and consequences of this shrinkage within Europe should be undertaken and the need for European protective measures and perhaps greater joined up thinking by stakeholder institutions to keep open the space for philanthropy is required.

## The Changing Contours of the Philanthropic Space – New Movements

Moving from further research to policy engagement, it would seem that despite the findings of EU commissioned reports to date (highlighting the low level of proven documented threat to philanthropic funds in the EU in the periods examined), the ongoing EU rhetoric of counter-terrorist measures has continued to view the non-profit sector, in contrast to the private sector, as vulnerable to exploitation and a potentially high-risk area where specific European level oversight is required. Chapter 4 endorsed the recommendations of these published research reports in their reiteration of the need for any subsequent measures intended to protect such funds to be risk-related, proportionate and evidenced-based. In the development of such measures the need for the engagement of and consultation with philanthropic institutions is paramount both in the context of the FATF (via the non-profit representative

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<sup>246</sup> See Chapter 2. The EESC Opinion on the Directive (EESC-2014-02794-00-00-AC-TRA (DE)) in September 2014 challenged the Commission's choice of Article 50 TFEU as the legal basis for the Directive and questioned whether it was compatible with the subsidiarity principle, arguing that the legal basis should more properly be Art 352 TFEU. In its opinion to the European Parliament's Committee on Legal Affairs, the EP Committee on Employment and Social Affairs proposed the rejection of the Commission proposal (COM(2014)0212–C7-0145/2014–2014/0120 (COD)) in June 2015. Within the lead committee, opinions are deeply divided on this subject, and majority agreement is so unlikely that the rapporteur has diplomatically refrained from tabling a draft report to date.

<sup>247</sup> See European Parliament, Directorate-General for External Policies Policy Department, *Shrinking space for civil society: the EU response* (April 2017).

seats on private sector consultative forum) and at national level in the context of Member State implementation of the EU's Supra-National Risk Assessment (SNRA) Report.

The continued existence of fiscal and legal barriers to cross-border philanthropy arising from incompatible national laws were identified in chapter 4 as an ongoing challenge. Chapter 4 highlighted that the majority of these regulations were not in breach of EU law per se but their existence is symptomatic of the lack of harmonisation between Member States that leads to additional administrative burdens on philanthropic institutions working across borders. National regimes that go further and actually breach EU law, such as the recent Hungarian Law on the Transparency of Organisations receiving Support from Abroad, tend to receive more political and media attention than the chronic obstacles referred to above and, perhaps because of their blatant or more dramatic nature, lead to European action. It is interesting to note in this regard the EU Commission's launch of infringement proceedings against Hungary in July 2017, being the mechanism identified in chapter 2 as the most effective tool available to the EU in protecting the philanthropic space. This highlights once more the lack of effective interim tools at the disposal of the European institutions, outside of the infringement procedure, to legally enable or enlarge the space for institutional philanthropy in the face of chronic obstacles described, which themselves can prove as invidious over the longer term.

Chapter 6 reviewed the Commission's 2017 SNRA Report recommendations which prompted Member States to ensure appropriate non-profit coverage in their national risk assessments as part of their risk mitigation measures. Specifically, the Commission outlined the need for:

- a) the provision of Commission guidance and/or training to non-profits in receipt of EU funding on the relevant EU legal framework, as well as on how to identify risks and meet due diligence requirements; and
- b) the organisation of multi-stakeholders exchange involving all professional sectors, in particular the financial sector, involved in business with non-profits.

While envisaged as involving soft law implementation options, moves on either of these issues will impact philanthropic organisations. It follows that the EU Commission should share its draft guidance and consult more broadly with philanthropy stakeholders than on previous occasions and be willing to amend and adapt its proposed guidance in light of received feedback if it is to have any hope of emulating the more successful national and sectoral experiences of soft law implementation, outlined in Chapter 6. A key point made in Chapter 6 is the importance of distinguishing soft law's lack of legally binding effect, on the one hand, from its potential impact in practice, on the other. To this end, there is also a window of opportunity available to philanthropic organisations to engage with the Commission and national competent authorities in facilitating more informed conversations around the risks and challenges facing philanthropic giving within and without Europe and opportunities to promote such engagement should now be explored.

One of the main problems when it comes to enabling the fiscal space for philanthropy in Europe, as identified by Chapter 5, is the lack of publicly available information and a lack of clarity around the

comparability processes operated by Member State tax authorities when faced with a claim from a donor to a foreign philanthropic organisation or from the recipient charity. Only 10 of the 27 Member States have identified processes for dealing with such claims. The majority of Member States operate on an ad hoc basis in which no guidance is available and long waiting times (often many years) ensue before a claim is dealt with, if at all.

Building on the work of the recent *Boosting Cross-Border Philanthropy in Europe Report*,<sup>248</sup> chapter 5 recommended that philanthropic organisations consider assisting in resolving the information asymmetries that exist when it comes to unpacking the different national tax reclaim procedures for donors and recipient organisations in the various EU Member States. The creation of a website resource and the pooling of national knowledge and knowhow, providing details on existing or emerging Member State tax authority procedures, coupled with the explanatory guidance or links to the relevant application forms necessary for both donors and public benefit recipient organisations to begin the tax refund/exemption process would be a valuable step forward for many philanthropic institutions, as would the identification of a tax official contact in each jurisdiction well versed in issues relating to tax equivalency. Chapter 5 also endorsed the recommendations of the *Boosting Cross-Border Philanthropy Report* regarding further exploration of the Luxembourg or Dutch models of tax equivalency practice as potential models of best practice for other Member States when it comes to engaging with philanthropic institutions.

Chapter 5, however, was less convinced around the proposal for common principles tax model that would seek to adopt a functional approach whereby the notion of comparability between Member State tax regimes would be broadened to look at the lowest common denominator core principles of public benefit rather than insisting on the presence of higher common factor elements. It is debateable whether tax authorities would have the power to engage in such a functional equivalency determination without the sanction of domestic legislation authorising a departure from the more strictly literal interpretation of the tax laws that normally applies. Whether the appetite for such tax law reform exists at Member State level is also open to question, particularly in light of the failed European Foundation Statute Proposal experience.

### Further Avenues for Exploration – Alternative Philanthropic Models of the Future?

In scoping the future of philanthropy in Europe, chapter 2 highlighted the need to further explore and better understand the potential and, equally, the limitations of emerging forms of venture philanthropy and social investment to provide new tools for facilitating philanthropic growth and outreach in Europe. In light of the EU Commission's moves to stimulate venture capital investment in, inter alia, social enterprises, by agreeing reforms to expand investment possibilities for funds, broaden the range of eligible managers and simplify administration which in turn will help investor capital reach the bodies,

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<sup>248</sup> EFC and TGE, *Boosting cross-border philanthropy in Europe: Towards a tax-effective environment* (2017).

such as social enterprises that need it,<sup>249</sup> chapter 2 concluded that research scope exists to scrutinise the opportunities and challenges for philanthropic engagement in both venture philanthropy and social impact investments at national and European level.

In reflecting on possible role models for future philanthropic institutional engagement, the work of the Non-profit Platform in the context of the FATF, discussed in chapter 4, is particularly noted. The policy engagement of this coalition of non-profit organisations with the FATF, the building of legitimacy through constructive cooperation with the FATF's Secretariat, the provision of detailed, well-reasoned and accurate policy submissions and the capacity of the Platform to provide a necessary channel of communication between the FATF and the philanthropic sector has paid dividends. As a result of its ongoing engagement, the Platform has helped to bring about incremental reform of the guidance documents related to R8 and more recently reform of R8 itself. The culmination of this collaboration with the formal inclusion of the Platform on the Private Sector Consultative Forum (PSCF) has shored up the legally enabling environment for philanthropy, even as efforts continue through the Platform to ensure that NGOs play a full role in the site evaluation visits of countries undergoing their Mutual Evaluation assessments. The work of the Non-profit Platform in building and enhancing its policy relationship with the FATF to such practical ends provides a useful role model that should be adopted in other policy arenas in which philanthropic institutions need to have their voices better heard. In the first instance, emulating the nature of this dialogue and this level of pragmatic policy engagement is something that philanthropic institutions should strive to bring about in relation to the implementation of the SNRA.

Through the identification of EU, broader European and regional players whose policies and actions are responsible for preserving, enlarging or constraining the space for institutional philanthropy in Europe, this report aims to provide a clearer sense of the historical rationale for the current state of the philanthropic enabling environment. In then considering the contributing legal, political, fiscal and administrative factors that influence this philanthropic space, the report unpacks some of the driving issues, worthy of further research, that are likely to affect and ultimately define the future contours of the European philanthropic space in the years ahead.

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<sup>249</sup> See Commission Press Release, Capital Markets Union: EU agrees to more support for venture capital and social enterprises (Brussels, 30 May 2017), IP/17/1477 available at [http://europa.eu/rapid/press-release\\_IP-17-1477\\_en.htm?locale=en](http://europa.eu/rapid/press-release_IP-17-1477_en.htm?locale=en).

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### European Foundation Centre

The EFC is the platform for and champion of institutional philanthropy – with a focus on Europe, but also with an eye to the global philanthropic landscape. With the aim of being the voice of institutional philanthropy in Europe, we communicate to stakeholders the value of organised philanthropy to society, to help nurture an environment in which it can flourish. We serve as a hub of sector exchange and intelligence, to help our members increase the impact of their added value in society. With over 25 years of experience and over 200 member organisations, the EFC gives its members access to a wealth of knowledge on the sector and to long-term relationships with philanthropic peers and external actors. Building on relationships and dialogue with policymakers which span several years, we help our members engage with high-level decision-makers. We also partner with a range of actors and catalyse joint projects which tackle many of today's greatest challenges.

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### DAFNE

The Donors and Foundations Networks in Europe, DAFNE, is Europe's largest network of donors and foundations associations. With 25 member associations with a collective membership of more than 10,000 foundations and grant-makers, DAFNE is a leading voice of European foundations. It underpins individual activities of its members by encouraging dialogue and collaboration between the national associations. DAFNE is currently chaired by Felix Oldenburg, General Secretary of the Association of German Foundations. He is supported by a Steering Committee comprising Magdalena Pekacka – Polish Donors Forum, Beate Eckhardt – SwissFoundations, and Beatrice de Durfort– Centre Francais des Fonds et Fondations.

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