

Tax incentives as a measure to support the arts in a globalizing world

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Abstract

The notion of common goods or shared goods can help explain the expansion of audiences for arts organizations due to globalization. This expanded audience provides new fundraising opportunities for the arts. Governments, however, often have not anticipated to these new opportunities. In many countries government support for the arts remains a domestic issue. By only granting tax incentives in a domestic situation governments can even discourage their taxpayers to contribute to an arts organization resident abroad, hindering cross-border fundraising activities of arts organizations. This article puts forward the new fundraising opportunity for the arts that occurs due to globalization, as well as how this opportunity is hindered by tax barriers. An overview is provided of the current existing private- and state solutions to overcome these tax barriers. The solutions are illustrated by means of examples derived from the Netherlands.

Key words: cultural policy, tax incentives, globalization, financing art.

1. Introduction

Globalization has a large influence on art and culture. The content of art changes: the increased interaction between cultures influences the type of art made. Furthermore, artists and arts organizations increasingly work across countries, performing, showing and selling their products across the globe. Audiences have easy access to all this art from all over the world. Globalization thus changes many aspects of the arts sector.

The focus in this paper is on the different approach globalization requires towards support for the arts. For the sake of this paper, the term art includes both contemporary visual art and performing art, as well as cultural heritage. Direct government support is historically only granted to arts organizations resident in the country. This assumes that it are merely the taxpayers of that country that benefit from the art in the country. In a globalizing society, this no longer holds. The concept of shared good is put forward as an argument to illustrate this. The application of tax incentives to cross-border situations is proposed as a method to support art in a globalizing society. It would allow a more balanced type of government support for the arts, in which those who benefit from art contribute most and the government stimulates this through tax incentives.

At this point in time the support of individuals for art abroad is, however, often still hindered by the solely domestic application of tax incentives. Since donations to domestic arts organizations are stimulated by tax benefits, foreign arts organizations cannot compete with domestic arts organizations when it comes to private fundraising. Large environmental and social charitable causes, such as Doctors without Frontiers and the World Wide Fund for Nature, solve this by establishing themselves in multiple countries. By doing so, they can guarantee that donors in these countries can benefit from tax incentives when donating. However, it is very costly to establish oneself in multiple countries. Therefore, this is not feasible for most arts organizations.

By granting tax incentives in cross-border situations, cross-border donations are relieved from its tax barriers. This allows arts organizations to compete with each other on an

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international level for private donors. Private donors could take over part of the support for arts organizations on an international level, with the governments contributing indirectly through the tax benefit they grant to donors.

By applying tax-incentives in cross-border situations the support of the art is no longer solely bound to the national level. How this can be done is explained in a comprehensive overview of the current existing state solutions and private solutions that allow for tax incentives on cross-border donations to foreign charities. The Netherlands serves as a case to illustrate the different solutions, since it is a country where all the current solutions can be applied.

Before discussing the different solutions that allow for the application of tax incentives on cross-border donations, I first discuss how art is shared across countries in a globalizing world, by using the notion of common goods. Next, I briefly discuss government support for the arts and more specifically indirect support for the arts. I will then continue to the tax barriers that now exist on cross-border charitable giving to the arts. After this I provide the overview of solutions that are currently used by states and private organizations to overcome this problem. To conclude I summarize the different solutions and provide suggestions for further research in order to weigh their comparative advantages and disadvantages.

2. Arts in a globalizing world

Works of art are sold across borders, performing artists tour around the world, museum collections have been digitized and are online accessible. These are just a few examples of the influence of globalization on the arts sector. Due to globalization people are no longer solely exposed to art in their own country, but have easy access to art in other countries as well. This influences the manner in which art is perceived (Throsby, 2010, pp. 2, 3, 157-170). The notion of common goods or shared goods, which Klammer (2002, pp. 468-470; 2004) elaborated on with reference to the conversation as a metaphor, offers an approach to gain more insight in the relation between globalization and art.

Art can be categorized in three types of goods: private goods; public goods and common goods. Public goods are those goods that are non-rival and non-excludable, think of the canals in Amsterdam. Private goods are those goods that are privately owned, are rival and excludable. The owner can exclude others from enjoying the good and only a limited amount of people can own and thus enjoy the good, for example a painting in a home. The painting is owned by the family that lives in the house and only those that are invited by the family will get the chance to enjoy the painting, until the family abandons it. In relation to globalization the concept of the common good is important. Common goods are “the goods that are shared by a group of people in consumption and possession” (Klammer, 2004, p. 1). The ownership of the good is far less well defined than with the private good or public good. No particular person owns the good, nor is the good publicly owned. Instead, the good is owned by a group.² Members of the group cannot be excluded from ownership of the good, but non-members are usually excluded. Within as well as outside the group there can be rivalry.

Art derives large parts of its value from shared knowledge on the piece of art. So, if people share knowledge on a specific piece of art, it becomes valuable. The more widespread and profound the knowledge, the more valuable the work of art becomes. The work of art will only keep its value if the knowledge is continuously shared between people and thus sustained. Whenever the sharing of knowledge ends, the value floats away and the piece of art is no longer a common good. Those who participate in sharing knowledge on the work of art, benefit from this. It is not so much economic value that they gain, but social value such as recognition, membership and status. The amount of persons sharing knowledge on art is limited to some extent, but it is not a well-defined group. Everyone who is involved in the sharing owns the knowledge, however, this does require active

² Ownership here refers to cultural ownership, not to juridical ownership.

participation. The contribution of each participant is important, whether it is consuming the work of art or making a theoretical contribution. It is a manner of producing shared knowledge (Klamer, 2004, p.5).

This should be clarified with an example. If I purchase a painting and keep it at home above the couch, then it is a private good. It derives its main value from its decorative characteristics. However, as soon as the gallery where I bought the painting shares with me information on the origin of the painting this gives a new dimension to the value of the painting for me. If I loan my painting to a museum, the sharing of knowledge expands among a larger group. The more people sharing knowledge on the painting I own, the higher my social status. Others who share knowledge on the painting and have contemplated -or consumed- the painting will also derive value from it. They can contribute to the shared knowledge on the painting and thus are partial owner of the culture the painting belongs to.

Common goods require cooperative behavior: sharing knowledge. This specific characteristic of common goods triggers loyalty, altruistic actions and the prevalence of trust and responsibility. In this manner free-riding is circumvented when it comes to common goods (Klamer, 2004, p.1). In case people share a common good, they thus become more willing to contribute, for example by volunteering for the common cause or by making a donation.

Now the concept of art as a common good is described, I would like to expand the notion of common good to a globalized world. Due to globalization, time and space are compressed and interactions and activities of people have stretched across the globe. The consciousness of the individual has expanded due to globalization. Notions about a larger global community have surpassed the sense of belonging to a national community (Scholte, 2008). Traveling around the world, doing business with people in different countries, having friends at the other end of the globe etcetera have become feasible options for many people. It also entails that information on a common good can be shared around the globe. Instead of sharing a common good with those in your physical proximity, common goods can be shared with those interested from all over. This results in communities that share their culture, instead of nations sharing a culture. Due to the larger consciousness, individuals explore art beyond the boundaries of their own countries and perceive (parts of this) art as belonging to their community. With the sense of belonging to a larger global community comes the feeling of responsibility for this particular community. Exactly here lies the motivation for individuals to donate to charitable arts organizations in other countries.

An example from cultural heritage is that of the Buddha's of Bamiyan in Afghanistan. These two 6th century Buddha sculptures in classical Greek-Buddhist style controlled the news in Western countries in 2001, when the Taliban threatened to demolish these ancient sculptures³. When they did, a shock ran through Western countries⁴. People were devastated by the loss of these sculptures. This event demonstrated that the Buddha's of Bamiyan not only belonged to the culture of Afghan people or Buddhists, but to communities stretching way further. This is reflected in, amongst others, the governments of Japan and Switzerland offering to help reconstruct the sculptures.

A similar shock went through the world when it became clear that the financial crisis in Greece and the austerity measures implemented by the International Monetary Fund, the European Union and the European Central Bank could impact the preservation of ancient Greek cultural

³ The case appeared in the British newspaper 'The Telegraph', amongst others. Alex Spillius, *Devastation of Afghan Buddha statues begins*, The Telegraph 2 March 2001.
<http://www.telegraph.co.uk/news/worldnews/asia/srilanka/1324790/Devastation-of-Afghan-Buddha-statues-begins.html>

⁴ Luke Harding, *How the Buddha got his wounds*, The Guardian, 3 March 2001
<http://www.theguardian.com/books/2001/mar/03/books.guardianreview2>

heritage. That people derive a shared value from these cultural icons and are willing to contribute to conserve and protect them is illustrated by initiatives such as Saving Antiquities for Everyone.⁵

Other examples of a global common good can be derived from fine art. The French artist Claude Monet in 1901 painted several scenes in London. The paintings titled *Waterloo Bridge, London* and *Charing Cross Bridge, London* belong to the collection of the Dutch Triton Foundation. The scenes might appeal to the English; therefore they can argue that the paintings belong to their culture. People from France, the Netherlands and Europe as a whole could also argue that the paintings belong to their culture as well, because of the French origin of the artist or the Dutch legal ownership of the paintings. What these groups all have in common is that they derive value from the shared knowledge on the paintings, which might even reach further than Europe. This gives people feelings of loyalty towards the paintings. The international shared value derived from the works of art of Claude Monet and several other artists came to light when a major art theft took place at the Kunsthal in Rotterdam on the 16th of October 2012.⁶ The two paintings, together with works of Henri Matisse, Jacob Meijer de Haan, Paul Gauguin, Picasso and Lucien Freud were stolen. The in total seven stolen paintings have, most likely, been burned by one of the relatives of the thieves. Art enthusiasts around the world considered this as major loss.⁷

The works of Van Gogh are also highly appreciated by people from different countries. Citizens from France, the Netherlands, Japan and other countries consider it as part of their culture. This became tangible when the Japanese businessman Rieoi Sato, who purchased the painting for 75 million dollar, stunned the world when he announced that he wanted to be cremated Van Gogh's *Portrait of Dr Gachet* (Klamer, 1996, pp. 14).

Many more examples exist of art that is shared in cultures across countries, also in the performing arts. MacBeth by Shakespeare and works of Bach have been performed by theater companies and orchestras around the world. The international shared value of art becomes tangible whenever its conservation is at stake. Similar feelings of loyalty arise among people from different countries, which are expressed in their urge to help preserve art.

The willingness to contribute to shared goods shows the high degree of loyalty, altruistic- and cooperative behavior that is involved in common goods. People want to contribute to the shared culture they are part of. A Japanese tourist visiting the Latvian Song and Dance Festival⁸, for example, was so moved by the event that he decided that he would establish his own choir in Japan, practice for five years in order to participate in the next edition of the Song and Dance Festival in Riga⁹. This might be an extreme case, but many tourists feel a sense of loyalty as soon as they visited a place. This might not always result in them wanting to participate actively, but could also result in them wanting to contribute in some way, for example by making a financial contribution.

In short, it can be stated that globalization has caused common goods, such as art, to be shared among worldwide communities instead of within a country. This influences the manner in which art is perceived. No longer is culture solely attached to a country. Due to the loyalty that arises for expressions of culture outside the own country, cross-border donations increase. As these communities expand across the globe, there are more members of one community and thus more potential donors. This creates new opportunities to finance the arts. First, however, the discrepancies

⁵ <http://www.savingantiquities.org/>

⁶ The Dutch newspaper NRC published the full story in e-book form titled *The tragic fate of the masterpieces stolen from Rotterdam* by Lex Boon in e-book form on <http://www.nrc.nl/kunsthal-en/>.

⁷ Ernest Oberlander-Tarnoveanu, director of the National History Museum of Romania, for example, referred to it as "a crime against humanity". <http://www.bbc.com/news/world-europe-23349744>.

⁸ <http://youtu.be/WeovGfNEesk>

⁹ <http://bobe.me/en/news/3377-choir-from-japan-surprises-latvian-song-festival-visitors>

with the current financing system have to be removed, before arts organizations can benefit from the new financing chances.

3. Government support for the arts

In most Western countries the arts receive government support. For many years this has been topic of debate among scholars. Arguments have been put forward why governments should support the arts, but these arguments have also been countered. Dworkin (1985, pp. 226-227), Klammer (1996, pp.16-19), Heilbrun & Gray (2001, pp. 219-249), Throsby (2001, pp.137-152) and Frey (2003, pp. 389-398), amongst others, provide insight in arguments used in the debate. Since most countries grant direct or indirect government support to the arts, they subscribe that arguments do exist for them to support art and culture. Therefore it is likely that according to the ethical convictions of most voters and ruling politicians there are arguments that support the claim that the arts should be supported by the government.

Governments can provide financial support to the arts in two manners. First, governments grant direct support, such as subsidies, which are direct expenses of the government to support the arts (Koopmans, de Kam, Sterks, & Wellink, 2005; Schuster, 1999, p. 59). These expenditures are financed through the collection of taxes and other revenue by the government. The government takes them into account on the expenditure side of the balance (Hemels, 2005, p. 11). Surrey (1970, p. 713) sums up examples of direct financial government support: "...direct grants, loans, interest subsidies, guarantees of loan repayment or interest payments, insurance on investment and so on".

A second way used to support the arts is through tax incentives. Tax incentives do not take place at the expenditure side of the balance, therefore, they are indirect subsidies. Instead of first collecting money from taxpayers and then spending it on subsidies, the government allows donors, who are also taxpayers, to pay fewer taxes if they contribute to organizations that promote certain policy goals. Examples of indirect support are preferential tax rates, tax deductions, tax exclusions, tax deferrals and tax exemptions. The aim of these measures is to influence the behavior of taxpayers, in order to achieve policy goals. Because of their nature they are also described as tax incentives or tax expenditures (Feld, O'Hare, & Schuster, 1983, pp. 26-27; Gruber, 2011, p. 540; Surrey, 1970, p.711).

This paper focusses on tax incentives for charitable donations to the arts. The advantage of tax incentives for charitable donations to the arts over direct subsidies to the arts is the relation that is created between the donor and the arts organization, which is absent in the case of direct subsidies. Besides, in the case of tax incentives part of the contribution is paid by the art enthusiasts among the tax payers. Only the tax benefit on the contribution is financed by taxpayers in general. This puts a smaller burden on the taxpayers as a whole in comparison to direct support for the art (Hemels, 2013).

Countries use different schemes to grant tax incentives on donations. Charitable donations can be deductible from taxable income and thus reduce the tax liability of the donor. This is known as the gift deduction. Gift aid, or top up-schemes, is similar to the deduction from taxable income. However, in that system the charitable organization can claim the tax benefit instead of the donor. A last scheme is the tax credit, where the donor can deduct -usually a percentage of- the donation from its taxes due.

Regardless of the scheme used, the idea behind tax incentives is that they decrease the relative cost of a gift compared to other consumption. Since a decrease in price leads to an increase in consumption it encourages to give more, whether it is the tax benefit, more private money or both (Feld et al., 1983, pp. 26-27; Gruber, 2011). Since the 1970s the effects of tax incentives on charitable contributions have been studied extensively. A review of these studies conducted over time suggests that giving is price elastic, at least among high incomes (List, 2011, p. 172). The meta-study by Pelozo & Steel (2005, p.266) also demonstrates a price elasticity of giving, with rates between -1.11 and -1.44 and thus show that tax incentives encourage charitable giving.

4. Tax barriers to cross-border donations

Due to globalization people do not only derive benefits from art in their own country, they also benefit from art in other countries, as was explained in section 2. Therefore, most arguments behind government support for the arts are also valid in an international setting, since they are not restricted to a certain geographical area.

Government support, however, is often only granted in the domestic situation. Direct subsidies are given to arts organizations located in the country. Tax incentives on donations are only granted on donations made to resident arts organizations. So although governments recognize the arguments for government support to the arts, which also hold in international situations, they often restrict their support to domestic charities. The merely domestic orientation of government support for the arts is not a problem as long as arts organizations function within one country. As soon as they start working across borders – which is the case due to globalization – this can cause barriers to financing the arts. Arts organizations that work on an international level, risk solely receiving direct subsidies in the country of tax residence. Consequence could be that they cannot rely on direct support for all the activities they perform outside their resident country.

Due to globalization new opportunities to finance the arts arise. Both arts organizations and their audiences are mobile. This expands the potential support base for the arts organizations, as was explained in section 2. To finance their international activities, arts organizations can approach their new and potentially larger audience in order to increase private and corporate donations.

Since arts organizations can reach a larger audience due to globalization, this might seem like an easy and interesting new alternative to compensate for not being able to rely on direct subsidies from other countries than the country of residence. This is, however, less easy than it seems. The newly generated audience is located outside the country of residence of the arts organization. Indirect support is often only granted on the donations donated to resident charities. Therefore, tax incentives do not automatically apply to cross-border donation, creating a tax barrier to donate to a non-resident arts organization. This makes it more costly for a donor to donate to a foreign charity than to a domestic charity. Thus unequal competition arises between the two where it is likely that the foreign charity will lose.

When there is no tax incentive applicable in the domestic situation, it cannot be granted in cross-border situations either. This is not an issue, since there is no unequal competition between the domestic and foreign arts organizations either if there is no tax incentive applicable in the domestic situation. Besides, this leaves governments the option to refrain from applying tax incentives on cross-border donations if their position is that support for the arts is not a task of the government.

The inapplicability of direct subsidies and tax incentives to donations in cross-border situations is an obstacle for arts organizations to raise funds abroad for their activities. The domestically oriented government support for the arts is outdated in comparison to the international activities in the arts. New opportunities that arise due to globalization are even hindered by the inapplicability of tax incentives on cross-border donations. This might refrain arts organizations from engaging in international activities.

5. Solutions to overcome tax barriers on cross-border charitable giving

I propose the application of tax incentives in cross-border situations as a solution to overcome the barriers to cross-border fundraising for the arts. Relieving cross-border donations from the tax barriers would create a situation where domestic and foreign arts organizations have an equal position to raise funds among their audiences. It would allow arts organizations to benefit from the expansion of their outreach to audiences. To reach this effect several solutions can be used. In section 6 state solutions are discussed. In section 7 private solutions are discussed.

6. State solutions to apply tax incentives in cross-border situations

The application of tax incentives in cross-border situations can be regulated at different legal levels. At the national level countries can allow their tax incentives to be granted in cross-border situations if requirements are met. At the international level countries can engage in bilateral solutions by concluding tax treaties in which they recognize each other's charities and mutually apply their tax incentives on cross-border donations. A multilateral solution could be the introduction of a charity status that is recognized internationally. In the European Union (EU) context such a charity status was proposed by the European Foundation Proposal¹⁰. I will exemplify these solutions states can implement to enable cross-border charitable giving with the benefit of tax incentives in the next paragraphs. The Netherlands is used to illustrate these solutions, since unilateral-, bilateral- and multilateral solutions apply here.

6.1 Unilateral solutions

A country can decide to open up its tax incentives on charitable donations made to foreign charities. This can be done by removing geographical restrictions from the specific tax provision. In addition, other requirements, such as host- or home country control, can be used by governments to determine to what extent they allow for tax incentives on cross-border donations.

The Netherlands does not put geographical restrictions on the tax benefits for gifts. Dutch taxpayers can deduct their gift, whether it is a domestic gift or a cross-border gift, from personal income tax when the donation is made to an organization that is recognized as a 'Public Benefit Pursuing Entity' (*Algemeen Nut Beogende Instelling* hereinafter public benefit entity or PBE) by the Dutch tax authorities. This holds for both domestic and foreign charities. Resident charities of the Kingdom of the Netherlands, another EU Member State or a state designated by the Ministry of Finance have to meet the same requirements to qualify as a PBE in the Netherlands.¹¹ States with which the Netherlands has an information exchange agreement on personal income tax, corporate income tax and gift- and inheritance tax are states designated by the Ministry of Finance. If a charity resides in a country that does not have such an agreement with the Netherlands, it can still meet the requirements of a PBE by accepting the obligation to provide additional information to the Dutch tax authorities¹². By putting its own requirements on foreign charities to be eligible to receive tax deductible gifts the Netherlands thus uses a host country control system. If the charity wants to raise funds in multiple countries this might complicate matters.

To obtain the PBE status an organization needs to meet certain requirements, of which the most important requirement is that the organization pursues the public benefit exclusively or almost exclusively (at least 90%). The tax authorities provide a list with public benefit activities. Culture is included in this list.¹³ Besides the facilities on which organizations with a PBE status can rely, additional facilities exist for PBE's that engage for at least 90% in cultural activities. Both domestic and foreign PBEs that mainly focus on art and culture can request a registration as a 'Cultural PBE'.¹⁴ Gifts to cultural PBEs are deductible from the donor's tax base for 125%.¹⁵ So a donation of €100 to a museum that qualifies as a Cultural PBE allows a donor to deduct €125 from its income tax base. In the highest tax bracket of 52% this leads to a tax benefit of €65. The maximum additional deduction is €1.250.

¹⁰ COM(2012) 35 final, 2012/0022 (APP).

¹¹ NL: article 5b (1)b AWR.

¹² NL: article 1c Uitvoeringsregeling AWR

¹³ NL: article 5b AWR.

¹⁴ NL: article 5b (4) AWR.

¹⁵ NL: article 6.39a IB.

By consulting the PBE register at the Dutch tax authorities the donor can see for donations to which cultural organizations it can receive a deduction from taxable income. Several arts organizations located outside the Netherlands have registered as a Cultural PBE. Not only arts organizations located in the border area with the Netherlands, such as the Emsländisches Kammermusikensemble – a chamber music ensemble in the German border town of Lingen, register as Cultural PBEs in the Netherlands. Also arts organizations located in different European cities register as such, for example the Tate Gallery in London, the Royal Museum for Fine art and History in Brussels. Examples from outside Europe are the Museum of Modern Art in New York, the Museum of Contemporary Arts in San Diego, the San Diego Museum of Art in La Jolla and The Israel Philharmonic Orchestra in Tel-Aviv.¹⁶

6.2. Bilateral solutions

Another manner to overcome the tax barriers to cross-border charitable giving is for countries to mutually agree on granting tax incentives on cross-border donations. This can be done in bilateral tax treaties. The model tax treaties by the United Nations (UN)¹⁷ and the Organisation for Economic Co-operation and Development (OECD)¹⁸, however, do not include a provision on the mutual recognition of charities in the other contracting state for income tax purposes. Since many tax treaties between countries are based on these model tax treaties, countries explicitly have to decide to include a provision on the mutual recognition of each other's charities for donations to these charities to be tax deductible.

Again, as with the unilateral solution, countries have to decide whether they base the control over recipient charities on host country control, home country control or both. Here it also applies that home country control would be most efficient from the charities perspective and the other options would have a restricting effect.

An example of a tax treaty that includes a provision on charitable contributions is the income tax treaty between the Netherlands and Barbados.¹⁹ The treaty states: ” *Contributions by a resident of a Contracting State to an organization constituting a charitable organization under the income tax laws of the other Contracting State shall be deductible for the purposes of computing the tax liability of that resident under the tax laws of the firstmentioned Contracting State under the same terms and conditions as are applicable to contributions to charitable organizations of the firstmentioned State where the competent authority of the first-mentioned State agrees that the organization qualifies as a charitable organization for the purposes of granting a deduction under its income tax laws.* ”²⁰ The treaty requires both home- and host country control, since the charity has to be recognized as such by the tax laws in its place of residence and it also has to meet the requirements put upon charities in the country of the donor. This complicates cross-border fundraising if the charity wants to raise donations in multiple countries.

6.3 Multilateral solution

Multiple countries can together agree to overcome the tax barriers to cross-border charitable giving. These multilateral solutions can take several forms, of which two can be found in the EU. Although in the EU it has proven to be impossible to harmonize taxes, since countries do not want to give up their sovereignty over their tax systems, EU law does have the potential to overcome tax barriers to cross-

¹⁶ http://www.belastingdienst.nl/rekenhulpen/giften/anbi_zoeken/.

¹⁷ UN – United Nations Model Double Taxation Convention between Developed and Developing Countries (2011).

¹⁸ OECD - Income and Capital Model Convention and Commentary (2010).

¹⁹ Barbados – The Netherlands Income Tax Treaty (2006, as amended through 2009).

²⁰ Article 22 Barbados – The Netherlands Income Tax Treaty (2006, as amended through 2009).

border charitable giving. This potential lies in the four fundamental freedoms as stipulated in the Treaty on the Functioning of the European Union (TFEU)²¹ and its enforcement by the European Court of Justice (ECJ). Furthermore, the Proposal for a Council Regulation on the Statute for a European Foundation (FE)²² (hereinafter: the Proposal) is an initiative of the European Commission to overcome barriers that currently hinder the philanthropic sector in the EU. In the Proposal specific tax provisions are included, although it is questionable whether these will be maintained during negotiations. Both the EU law and the Proposal are discussed in the next two sub-paragraphs.

6.3.1 EU Law

The four freedoms in the TFEU have the potential to overcome the tax barriers involved in cross-border charitable giving within the EU. In four landmark cases the ECJ has ruled that if a country provides fiscal facilities for charities and charitable giving, these facilities should also apply in comparable situations within the EU. EU Member States remain the right to decide whether they want to provide these fiscal facilities and under what conditions. A residence requirement is prohibited, since this would go against the four freedoms. The cases in which this was ruled are Stauffer²³, Persche²⁴, Missionwerk²⁵ and Commission v. Austria²⁶. The Persche case is most important for this article, since it concerned the applicability of a tax incentive on a charitable donation to a charity in another EU Member State.

In the Persche Case²⁷, the German resident Hein Persche claimed a tax deduction with regards to contributions in kind which he made to a Portuguese charity. The charity was recognized by the Portuguese tax authorities as a charitable body and was therefore under Portuguese tax law eligible to receive tax deductible donations. The German tax authorities, however, did not grant the deduction since the recipient of the gift was not established in Germany and the required donation certificate did not meet German standards. In line with the previous decision in the Stauffer case, the ECJ ruled that this decision was not in line with the free movement of capital. The German authorities tried to justify this by the need to safeguard the effectiveness of fiscal supervision, which was refused by the ECJ. This implies that tax laws which discriminate against donations to charities based in other EU Member States, but equivalent to resident charities, are against the TFEU. The ECJ however did highlight that the tax authorities can require the taxpayer to provide such proof as they may consider necessary in order to determine whether the conditions for deducting expenses provided for in the legislation at issue have been met and, consequently, whether to allow the deduction requested.²⁸

At this point the most important question on the non-discrimination of charities in other EU Member States is whether the charity should comply with the national standards set out by the host state or with the standards of the state of which it is resident. The ECJ focusses on the requirements imposed by the country that has to grant the tax benefit, which leads to a host country control (Jochum, 2012).

6.3.2 The Proposal for a Council Regulation on the Statute for a European Foundation (FE)

²¹ Treaty on the Functioning of the European Union (TFEU) and EU Treaty (as amended through 2007).

²² COM(2012) 35 final, 2012/0022 (APP).

²³ Case C-386/04, *Centro di Musicologia Walter Stauffer v. Finanzamt München für Körperschaften* (2006).

²⁴ C-318/07, *Hein Persche v. Finanzamt Lüdenscheid* (2009).

²⁵ Case C-025/10, *Missionwerk Werner Heukelbach eV v. État Belge* (2011).

²⁶ Case C-10/10, *European Commission v. Republic of Austria* (2011).

²⁷ C-318/07, *Hein Persche v. Finanzamt Lüdenscheid* (2009).

²⁸ C-318/07, *Hein Persche v. Finanzamt Lüdenscheid* (2009).

On February 8th, 2012 the European Commission has presented a Proposal for a Council Regulation on the Statute for a European Foundation (FE).²⁹ The Commission is of the opinion that part of the charity organization's funds is inefficiently spent due to juridical and administrative costs when working across borders within the EU. Aim of this new proposed European legal form is to overcome this inefficiency and make it easier for charitable organizations to conduct cross-border activities within the EU. The Commission explicitly mentions: "*It will allow foundations to more efficiently channel private funds to public benefit purposes on a cross-border basis in the EU*".³⁰ As a result more funds should end up at the public benefit purpose activities. On its turn, this has to benefit the public welfare and the economy of the EU.

A European Foundation or *Fundatio Europaea* (hereinafter FE) is a separately constituted entity for a public benefit purpose which must serve the public interest at large – as defined by the Council Regulation by means of uniform and agreed-upon joint material and formal standards. Each Member State shall appoint a supervisory body that monitors whether the FEs registered in that Member State meet the requirements.³¹

Arts, culture and historical preservation are the first activities on the list that qualify as serving the public interest at large.³² Arts organizations could thus qualify as an FE. Furthermore, amongst others, the FE shall have assets equivalent to €25.000.³³ This potentially limits the possibility for arts organizations with little assets to register as an FE. Another important requirement is that the FE shall have activities, or an objective to carry out activities, in at least two EU Member States.³⁴ The FE does not aim at replacing the foundation or other legal forms at the national level, but is proposed as an alternative.

Member States should regard the FE in the same way as domestic public benefit entities. This implies that its donors and beneficiaries should get the same tax benefits as those of domestic charities. Chapter VIII of the Proposal on the fiscal treatment of FE's states that all EU Member States should treat FE's equally to public benefit entities under its national legislation. Article 50 of the Proposal specifically monitors the equal treatment of beneficiaries of the FE to beneficiaries of public benefit entities within the country of residence of the beneficiary.³⁵ This provision thus removes the tax barrier to cross-border charitable giving within the EU.

Research shows, though, that a European Foundation is only a partial solution. Although it is effective in removing tax barriers from cross-border charitable giving, it might not be efficient for countries that have to establish a supervisory structure. Besides, the Proposal does not address the risk of abuse. For fundraising charities that choose to get the status of an FE, the solution is efficient. For charities with another legal status, the problem remains. The biggest problem with the FE however is that it does not seem a feasible solution, due to the fact that it requires Member States to trust on each other's supervision (Hemels, 2012).

Although the initial Proposal could be a partial solution to the inapplicability of tax incentives on cross-border donations, it seems unlikely that it will be adopted, at least not in the short run. At the time of writing the latest news was that the negotiations continue, but apparently

²⁹ COM(2012) 35 final, 2012/0022 (APP).

³⁰ COM(2012) 35 final, 2012/0022 (APP), p. 3.

³¹ Article 47 FE Proposal.

³² Article 5 FE Proposal.

³³ COM(2012) 35 final, 2012/0022 (APP).

³⁴ Article 6 FE Proposal.

³⁵ Article 50 FE Proposal.

without the tax provisions.³⁶ Without its tax provisions the FE is not a solution to the problem sketched in this article.

7. Private solutions

Private organizations try to overcome the inapplicability of tax incentives on cross-border donations by creating networks of organizations with a charity status. Through this collaboration and the use of available fiscal facilities donors can get the same tax benefit on cross-border donations as on domestic donations (von Hippel, 2009, p. 291). In these networks the donor donates to an intermediary party with a charity status in their own country and can therefore benefit from the tax incentive. The intermediary party transfers the donation to the charity abroad. The intermediary party charges a percentage fee of the donation for this service. Prerequisite for this structure to work, is that the country where the donor pays its taxes (host country), allows organizations with a charity status to spend its donations on activities abroad.

The intermediary parties often have multiple purposes and do not only function as a conduit organization for cross-border donations. Instead, their core business is often to contribute to the public benefit by conducting charitable activities or fundraising for these activities. Furthermore, there are intermediary parties that provide quality checks of charitable organizations abroad as a service to donors.

Two examples of intermediary parties as private solutions to the tax barrier on cross-border donations are the King Baudouin Foundation United States and Transnational Giving Europe.

7.1 King Baudouin Foundation United States

The King Baudouin Foundation United States (KBFUS) is a private solution for American taxpayers that want to make a contribution to charities in Europe or Africa.³⁷ Over the period 2003-2012 €59.067.831 was donated through the King Baudouin Foundation United States, from donors in the United States to charities in Europe and Africa³⁸.

In the United States donations can be deducted from taxes when they are made to an organization that meets the requirements under section 501(c)(3) of the Internal Revenue Code (IRC), one of the requirements being that the organization is created in or under the laws of the US, any state, the District of Columbia or any possession of the US (including Puerto Rico). This puts territorial restrictions on the qualifying organizations, excluding all organizations that are not established under the laws of the US. It does not, however, restrict qualifying organizations to spend their assets within the US. This creates room for US charities to engage in activities abroad and for foreign charities to engage in the American fundraising market, by establishing themselves under US law. Foreign organizations can establish a ‘friends of’ organization in the US. This organization can be set up under the laws of the US to raise funds in the US for a specific foreign charitable organization.³⁹ Due to the administrative requirements under 501(c)(3) this, however, is still costly.

Another option for charities located outside the US is to rely on the support of a qualifying organization under IRC 501(c)(3). This is exactly what KBFUS offers. KBFUS qualifies as a 501(c)(3) organization. European and African charities can register at KBFUS, or create an ‘American friends fund’ at KBFUS as they call it. To do so, they need to fill out a due diligence form, in which KBFUS, amongst others, validates whether the charity qualifies as such under its own tax law. When the foreign charity meets the standards of KBFUS an ‘American friends fund’ can be created at

³⁶ http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/intm/141115.pdf

³⁷ <http://www.kbfus.org>.

³⁸ <http://kbfus.insight.foundationcenter.org/>

³⁹ US: IRC section 170 (f)(18).

KBFUS holding the name of the organization. This is not a legal status, it solely means that the foreign charity is supported by KBFUS and can benefit from KBFUS's 501(c)(3) status. This allows the American donors of the foreign charity to donate through KBFUS and deduct their donation from taxes. KBFUS takes care of all the administrative work involved. The foreign charity hands in an application for financial support at KBFUS and KBFUS decides whether it transfers the donation. The application for financial support is merely a formality imposed by the American tax authorities, since it requires that the American charity holds the control over the funds. To cover administrative costs involved with setting up an 'American friends fund' the KBFUS charges \$1.500. In addition a management fee is charged, between 5% and 0,5% of the cumulative total of contributions within one calendar year.⁴⁰

Several Dutch cultural charity organizations have registered an American friends fund at KBFUS: de Kunsthall, Museum Boijmans van Beuningen, Prins Bernhard Cultuurfonds, Museum Catharijneconvent, the Netherlands Institute for Art History, the Dutch Language Fund, Rijksmuseum, Van Gogh Museum.⁴¹

7.2 Transnational Giving Europe

Transnational Giving Europe (TGE) is a network of European charities that help each other channel gifts between donors and charities resident in certain EU Member States or Switzerland. It is remarkable that, despite the rulings by the ECJ as discussed in §6.3.1, there is an increasing demand for the TGE, as their figures show. In 2009 at the start of TGE €2.946.708 was channeled through them. By 2012 this has more than doubled up to around 7 million euro⁴². This demonstrates that the multilateral solution as currently applied in EU Member States is not sufficient yet to overcome the tax barrier. As TGE indicates, it might be a matter of time before the EU Member States adjust their legislation in line with the ECJ rulings and TGE becomes superfluous.⁴³ Currently though, there is still demand for the services TGE provides. TGE covers sixteen countries and serves more than 350 organizations and 6200 donors.⁴⁴

One of the beneficiaries of TGE is the Royal Concertgebouw Orchestra in the Netherlands.⁴⁵ If one of their donors resides in another country that is covered by TGE, the donor can make a donation to the Orchestra with a tax incentive. Let us assume their donor resides in Spain. In Spain a donation qualifies for a tax credit if the recipient meets the requirements under article 16 of Law 49/2002 of 24 November 2002 'law concerning the tax regime of non-profit entities and tax incentives for patronage'.⁴⁶ Since it refers to the term foundation as a foundation created under Spanish foundation law, it is not entirely clear how this should be interpreted. It could either entail that the Royal Concertgebouw Orchestra should establish itself as a Spanish foundation, or that the Royal Concertgebouw Orchestra has to meet the requirements that are put forward for the foundation status under Spanish civil law (European Foundation Centre & Transnational Giving Europe, 2014).

To circumvent the uncertainty whether the Royal Concertgebouw Orchestra is eligible to receive donations with a tax credit in Spain, the donor or the orchestra could approach TGE. The Dutch partner of TGE, being the Oranje Fonds, validates whether the orchestra is eligible for tax

⁴⁰ http://www.kbfus.org/wp-content/uploads/2013/05/EUR_AFR_american_friends.pdf.

⁴¹ <http://www.kbfus.org/our-services/services-for-nonprofits/list-of-american-friends-funds-at-kbfus>.

⁴² <http://www.transnationalgiving.eu/tge/default.aspx?id=219948&langtype=1033>.

⁴³ <http://www.transnationalgiving.eu/tge/details.aspx?id=219940&LangType=1033>.

⁴⁴ www.transnationalgiving.eu.

⁴⁵ <http://www.transnationalgiving.eu/tge/details.aspx?id=235178>,

<http://www.concertgebouwworkest.nl/en/Support>.

⁴⁶ C. Garcia de los Reyes and L. Marquez de la Calleja (2013)

http://www.transnationalgiving.eu/uploadedFiles/TGE/Cross_border/TGE_EFC_Spain.pdf accessed 6 March 2014.

deductible donations under Dutch tax law. If the orchestra turns out to be eligible, which is the case, the donor can make its donation to the Spanish TGE partner, being the Fundacion Carlos de Amberes. Since the Fundacion Carlos de Amberes holds a PBE status under Spanish tax law, the donor can deduct the donation from his taxable income. The Fundacion Carlos de Amberes then transfers the donation to the Royal Concertgebouw Orchestra. For this service TGE charges a fee of 5% for donations up to €50.000 and a 1% fee if the amount exceeds this number. The fee will, however, never be more than €6.500.⁴⁷

By using the services of TGE the donor knows beforehand that his donation is tax deductible. Furthermore, the costs for this service are transparent. This would not be the case if the donor had to go through the procedure of opting for the PBE status for the Royal Concertgebouw Orchestra and running the risk of having to go to court to reach this.

8. Concluding Remarks

Current government policy to finance the arts is obsolete compared to the global functioning arts sector. The notion of the common good helps gain insight in the functioning of the arts sector in a globalizing world. Communities that spread across borders share the consumption and possession of art. Although they reside in different countries, they are loyal and willing to contribute to the same art, since it belongs to their shared culture. This offers inspiration to broach new sources to finance international activities of arts organizations. The enlarged audience provides for a larger group of potential donors which arts organizations could benefit from. They are, however, hindered by unequal competition between domestic and foreign arts organizations due to tax barriers.

Granting tax incentives in cross-border situations can solve the unequal competition, but this is currently only exercised on a small scale. There are several state solutions and private solutions available that allow donors to receive a tax incentive on their cross-border gift. State solutions exist on different legal levels. On a unilateral level governments can remove residence requirements from their tax provisions. Tax treaties are bilateral solutions. Examples of multilateral solutions are the enforcement of EU law and the proposal for a European Foundation. Private solutions use the existing fiscal facilities and create networks among charities in certain countries to overcome the inapplicability of tax incentives in cross-border situations.

It would be valuable to know which solution is most successful in overcoming the tax barriers to cross-border charitable giving to the arts. It would provide arts organizations and their donors to lobby for a certain state solution, or to choose to invest in creating their own networks. When comparing the different solutions several factors have to be taken into account.

One of these factors is the level of legal certainty it provides beforehand. Some solutions do allow for tax incentives on cross-border charitable gifts, but first one might have to go to court for the tax incentive to be enforced, as is currently the case in the EU. This creates legal uncertainty on beforehand for the donor. Furthermore, it is also time consuming and costly to go to court.

Another factor is the level to which a solution prevents from a crowd out effect. If every single country removes geographical restrictions from its tax incentives on donations to the arts, all countries could benefit from it. However, if not all countries do so, the risk exists that a crowding-out effect arises. Countries can benefit from others granting tax incentives on donations, but refrain from granting these tax incentives in cross-border situations themselves. The more countries to which a solution is applicable, the smaller the chance of crowding out and the more successful the solution is in removing tax barriers.

A last issue I want to mention here is that of the supervising authority to which charities are subject. For tax incentives to apply in cross-border situations the legislator has to indicate what

⁴⁷ <http://www.transnationalgiving.eu/tge/details.aspx?id=219956&LangType=1033>.

authority is responsible for monitoring the charity. It could choose for home country control, host country control or both. In the case of home country control, the country where the charity resides decides whether the organization is a charity and therefore qualifies to receive tax rebate donations. From the perspective of charities this would be most efficient, since they then only need to meet one set of requirements. Host country control refers to control of the charity by the country that grants the tax incentive. This would entail that if the charity wants to raise funds both in the resident country and abroad, it has to meet multiple requirements, which can put severe restrictions on the charities. This also holds when a host country requires both home country control and host country control. In theory it could even be impossible to meet both the requirements of the home- and the host country if they use conflicting requirements. Therefore the success of a solution largely depends on the kind of control the legislator chooses.

More factors have to be taken into account when evaluating the different solutions. The private solutions for example are more costly in comparison to the state solutions, whereas the state solutions might require a large time investment to gain knowledge of a foreign tax system. Further research is therefore necessary to gain thorough insight in the solutions that would allow for tax incentives on cross-border donations, for arts organizations to benefit from the new fundraising opportunities that globalization offers.

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