RUSSELL-COOKE | SOLICITORS

A Watershed?: Tax Relief on Charitable Donations across EU Member Countries

Cautious optimism might best sum up commentators' reactions to the recent Decision of the Court of Justice[1] involving charitable giving across national boundaries and the rights for a donor to benefit from the tax incentives available in his country of residence.

The Persche decision has at last confirmed the principle that a taxpayer should be allowed the same reliefs for a gift made to a charitable organisation established in another Member State as are available for a gift made to a charity established on home soil. This decision, whilst not unexpected, is important as it provides confirmation that refusal to allow a deduction for tax purposes on the grounds that the beneficiary of the gift was not established in the Member State in which the taxpayer was resident, constituted a restriction on the free movement of capital which is, as a rule, prohibited.

The case details relate to a German national, Mr Hein Persche, who in his Tax Return for 2003 claimed a tax deduction in respect of a gift in kind made to the "Centre Popular de Lagoa in Portugal" (a retirement home to which a children's home is attached). The District Tax Office in Germany refused to allow the deduction. German law provides for the deduction for tax purposes of gifts to charitable bodies within Germany which satisfy certain requirements but excludes any tax advantages for gifts to bodies established and recognised as charitable in another Member State.

The Bundesfinanzhof (the German Court with jurisdiction in tax matters) referred the matter to the Court of Justice and in particular whether a deduction for tax purposes can lawfully be made subject to the condition that the beneficiary is established in that same Member State.

In its judgment of 27 January 2009, the Court of Justice confirmed that the gift (even in the form of everyday consumer goods) was potentially within the ambit of the Treaty provisions on the free movement of capital.

The Court then went on to decide that as obtaining a tax deduction can have a significant influence on the donor's attitude to making the gift, if the donor is prohibited from deducting a gift made to a body recognised as charitable but established in another Member State, this may affect the willingness of German taxpayers to make gifts to such bodies. This therefore constitutes a restriction on the free movement of capital which is, as a rule, prohibited.

A Member State may, quite justifiably, as part of its legislation on the deductibility of gifts for tax purposes treat national charitable bodies and those established in other Member States differently, if the bodies established in these other Member States pursue objectives other than those defined by its own legislation.

[1] Persche v Finanzampt Lüdenscheid [2009] EUECJ C-318/07.

In other words, where a body is recognised as charitable in one Member State and it can satisfy the requirements imposed to gain charitable status by the law of another Member State and where its object is the promotion of the same general public interest, so as to qualify for charitable status in the other Member State, that State cannot deny the foreign charitable organisation the right to equal treatment on the grounds that it is not established within its own territory.

This means that the argument previously made by the UK government that tax relief for gifts to charitable organisations was only available for charities located within the donor's home state, i.e. the UK, is now illegal. The UK government had previously argued that there was no breach of the principles of free movement of capital and the Court has now clearly stated that restriction is not justified.

The Court went on to state that the necessity for having in place procedures to obtain proof that the conditions for deductibility of expenditure in the other state have been met was not a reason to impose a blanket prohibition.

In summary, therefore, the principle of the free movement of capital demands that any legislation in a Member State which only allows a benefit of a deduction for tax purposes in respect of gifts made to bodies established in that Member State (having charitable status) is not permitted where there is no possibility for the taxpayer to prove that the gift to the foreign charitable entity satisfies the local law requirement for the obtaining of a benefit.

Whilst the development is to be welcomed and had in fact been widely anticipated, it is not at all clear how and when the decision will be put into practice in the UK. From a UK perspective, HMRC will need to review all the tax advantages available to donors for gifts to UK charities. No response from HMRC has so far appeared.

UK tax payers who make gifts to EU charities which would qualify as "charitable" under English law can now consider making a claim for relief in their tax returns. In practice, however, it is not as yet clear how quickly and on what basis the ruling will be followed.

For more information please contact:

Dawn Alderson
Partner
020 8394 6373
Dawn.Alderson@russell-cooke.co.uk

April 2009