

**PHILANTHROPY IRELAND**

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**THE BUSINESS OF PHILANTHROPY**

**19 NOVEMBER 2008**

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**ENGAGING IN PHILANTHROPY:  
LEGAL AND TAX ISSUES**

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## **ENGAGING IN PHILANTHROPY: LEGAL AND TAX ISSUES**

*"I still believe in the philosophy – Fortune quoted me saying this 20 years ago – that a very rich person should leave his kids enough to do anything but not enough to do nothing." Warren Buffett, January 2006. Fortune magazine.*

### **1 BENCHMARKING DECISIONS**

- 1.1 The most important decision to be made by any philanthropist is the decision to apply some of their wealth in order to achieve certain charitable purposes.

Many Irish philanthropists wish to make these decisions in a discrete fashion and to establish a charitable body (a "Foundation") to fulfil these.

- 1.2 A number of fundamental issues require to be considered at the outset. These include

- whether the Foundation is to have a narrow or broad ranging focus across the heads of charity being relief of poverty, education, religion and benefit to community;
- whether the Foundation is to be active in developing and implementing its program of activity or a funder in identifying and working with charities which are actively engaged in delivering projects.

It will be necessary to decide whether to use a trust or a company as the legal structure for the Foundation. This decision is important in the context of the disclosure of information, managing the Foundation assets, and ensuring that limited liability is available to protect against risks of third party claims.

- selecting suitable fiduciaries, whether trustees or directors of a company. As the officers who will be responsible for implementing the philanthropic agenda, their identity is crucial. The communication of the intention of the founder is of great importance because the Foundation established will continue in the future, often beyond the life of the founder and the lives of the first fiduciaries.

In this context, a decision is required to be made by the founder as to whether the Foundation should be capable of supporting projects across the four charitable heads already referred to, or should have a narrower focus. A decision on this issue is often driven by the extent to which the founder has identified and communicated the objective or objectives to be pursued.

- In many cases, the establishment of a Foundation forms part of a broader formalising of the manner in which family wealth is held, managed and used. There can be material benefits from harnessing the charitable contributions previously made on an ad hoc basis and bringing them together in a Foundation with appropriate governance and discipline applied to the making of any donations.

### **2 STRUCTURE**

- 2.1 In Ireland, a Foundation is usually established either by way of trust deed or a company limited by guarantee and not having a share capital. There are advantages and disadvantages to both structures.

- 2.2 A company limited by guarantee offers its members limited liability and perpetual succession. The company is obliged to comply with company law. It must submit annual returns and its directors are bound by the duties for directors set out in company caselaw. A company limited by guarantee and not having a share capital must have at least seven members. The company law requirements must be satisfied in addition to any requirements imposed by the Revenue Commissioners to achieve and maintain charitable status. In order to obtain charitable status, the Revenue Commissioners will generally insist that at least three independent directors be appointed, of whom a majority are resident in Ireland and for the central management of the company to be

carried on in Ireland, to ensure that the charity has a real presence in the jurisdiction. The founding documents are the memorandum and articles of association.

2.3 Rather than a memorandum and articles of association, a charitable trust may be established with only the deed as its establishment document. Unlike a company, trustees of the trust do not have limited liability, although the trust usually contains a standard indemnity for trustee liability in all cases save for fraud or wilful neglect. It does not have the compliance requirements imposed on a company as there is no formal regulation of trusts in this jurisdiction at present. The Revenue Commissioners generally require at least three Irish resident independent trustees of a charitable trust. One disadvantage of the trust structure, however, is that the statute law governing the operation of trusts in Ireland is outdated and often does not offer sufficient flexibility in managing the trust. Accordingly, it is very important that the trustees are empowered in the trust deed to carry out all necessary activities for the effective running of the charity.

2.4 Whether the Foundation is to be established by way of trust or by way of company limited by guarantee and not having a share capital, the governing instrument of the entity must contain the following mandatory standard clauses in order to qualify for charitable status

- non-distribution of income, assets or profits to the organisation's members;
- the keeping of annual audited accounts and making these available to the Revenue Commissioners on request;
- a majority of the trustees/officers/directors must be resident in Ireland;
- prohibition on the payment of fees and/or salaries (other than out of pocket expenses) to trustees/officers/directors for services rendered in that capacity;
- providing that should the organisation be wound up, the requirement that any surplus assets be transferred to some charitable body having similar objects to itself, or failing that, to some other charitable body; and
- that prior approval be obtained from the Revenue Commissioners before making any amendments to the organisation's governing instrument. This particular clause enables the Revenue Commissioners to assess whether the organisation should continue to benefit from the tax exemption in the light of the proposed changes to its constitution and protects the organisation from potentially acting *ultra vires* the exemption and incurring tax liabilities.

2.5 The sequence of steps in order to establish a Foundation and obtain charitable status from the Revenue Commissioners in Ireland is as follows:

- the Memorandum and Articles of Association or Trust Deed must be drafted;
- a Statement of Activities and a Financial Statement must be drafted by the client;
- the draft Memorandum and Articles or Trust Deed and the Statement of Activities and Financial Statement are forwarded to the Revenue Commissioners, together with a charity application form, for approval;
- in the case of a company, following approval of the draft Memorandum and Articles of Association by the Revenue Commissioners, the company is incorporated;
- once the Revenue Commissioners approve the Memorandum and Articles of Association or Trust Deed, the company or trust applies for its tax registration number which is then submitted to the Charities Section of the Revenue Commissioners; and
- the Revenue Commissioners issue the company or trust with its charity number (CHY Number).

- 2.6 In April 2007, the Department of Community, Rural and Gaeltacht Affairs published the first substantial Bill reforming charity law in over forty years (the “Charities Bill 2007”). A product of a lengthy process of consideration and consultation with the charities sector and law reform committees, its main aim is to increase public confidence in Irish charities by introducing Ireland’s first comprehensive system of registration and regulation.
- 2.7 It should be noted that although there is no regulating body in respect of charities in place at present in Ireland, the Charities Bill 2007 does provide for the establishment of the Charities Regulatory Authority. The Dáil completed its revision of the Bill at Report Stage on 5 November, and the approved version of the Bill, which is now available on the Oireachtas website for download, has been sent to the Seanad for debate. A date for consideration of the Bill in the Seanad has not yet been determined.

### 3 TAX STATUS OF IRISH CHARITIES

- 3.1 Irish tax legislation provides exemptions for charities in respect of certain taxes in certain circumstances. In order to avail of these tax exemptions it is necessary to apply to the Revenue Commissioners in Ireland for charitable status.
- 3.2 The Revenue Commissioners will only grant charitable status if it is satisfied that the objects and powers of the charity provide that the income of the charity can only be applied for purposes that are legally charitable. Given that there is no comprehensive statutory definition of what constitutes a charity, the legal definition derives from judicial authorities. The approach of the Courts has been to rely on the House of Lords decision in the *Pemsel [1891] AC 531* case. It should be noted that the Charities Bill 2007 proposes a statutory definition of charitable purposes. However, this Bill has not yet been enacted and a date for its enactment has not been set.
- 3.3 The *Pemsel* decision set out that, in order to qualify as charitable, a two tier test must be satisfied. Firstly, the objects of the charity must be one or more of the following:-
- The relief of poverty;
  - The advancement of education;
  - The advancement of religion; and
  - Other works of charitable nature beneficial to the community.

The heading ‘*other works of charitable nature beneficial to the community*’ is the heading most availed of nowadays to obtain charitable status from the Revenue Commissioners. It is considered to be the broadest of the four *Pemsel* headings but requires a much higher standard of public benefit to be displayed than in any of the preceding categories. Given the lack of judicial interpretation on the scope of this heading, the Revenue Commissioners are the primary arbiters in determining what other works of a charitable nature are beneficial to the community.

- 3.4 Secondly, in conjunction with satisfying the above, the charitable body must possess sufficient public benefit (it must benefit the community as a whole or an appreciable section of the community) and its purpose must be exclusively charitable. In order to qualify for charitable status, the Revenue Commissioners must be satisfied that the charity benefits an appreciable section of the community. In general, this means that the gift must provide assistance to beneficiaries in respect of whom the donor has no moral or legal duty to provide. Consequently, there must exist a sufficient degree of emotional or obligational distance between the donor and the recipient in order for the gift to be charitable.

- 3.5 The Charities Bill 2007, for the first time in Irish history, proposes to set down in legislation the definition of charitable purpose.

Recognising the need for greater certainty in the definition, the Bill proposes four categories of charitable activity:

- The prevention or relief of poverty or economic hardship
- The advancement of education
- The advancement of religion
- Any other purpose of benefit to the community

The final category is then further developed with a non-exhaustive list of purposes that are beneficial to the community, such as relief of those in need by age or disability, the promotion of health, the promotion of racial harmony, the protection of the natural environment and the advancement of arts.

In addition, a charity may promote a political cause which is directly related to the advancement of its charitable purposes, but it cannot promote a political party or candidate.

- 3.6 The taxes from which charities may receive certain exemption in certain circumstances are as follows:-

- Income Tax
- Corporation Tax
- Capital Gains Tax
- Deposit Interest Retention Tax (DIRT)
- Capital Acquisitions Tax (gift and inheritance tax)
- Stamp Duty
- Dividend Withholding Tax

- 3.7 There is no general exemption in respect of Value Added Tax for organisations which are granted charitable tax exemption. However, in certain circumstances, specific reliefs from VAT are available and, where appropriate, charities may be entitled to claim such relief. Not all trading income will qualify for tax exemption and that charitable tax exemption does not relieve a charitable entity of its obligations as an employer to operate the P.A.Y.E. system for its employees.

- 3.8 It should be noted that it is important that charitable status is granted by the Revenue Commissioners in Ireland before any property is acquired by the charity in order that the charity can avail of the stamp duty tax exemption. Otherwise, the acquisition of non-residential property over €150,000 attracts stamp duty tax liability at the rate of 6% in Ireland.

## 4 TAX ISSUES FOR DONORS

- 4.1 In dealing with tax relief for donors to charity, separate reference is made to capital tax relief and corporation/income tax relief. Capital tax relief is available to match donations in full, as is corporation tax relief for donations to an approved body. Income tax relief is restricted.

### 4.2 Capital Taxes Relief

Under this heading, reference is made to Capital Gains Tax (“CGT”), Capital Acquisitions Tax (“CAT”) and stamp duty (“SD”).

Section 611 Taxes Consolidation Act (“TCA”) 1997 provides that where an asset is disposed of to a charity, otherwise than under a bargain at arms length, it is treated as a disposal giving rise neither to a gain nor a loss.

A benefit received which is applied for public or charitable purposes in accordance with Irish law, is exempt from CAT by reference to Section 76 Capital Acquisitions Tax Consolidation Act (“CATCA”) 2003. The benefit received by the charity must be applied for purposes which are public or charitable in accordance with Irish law.

No SD is chargeable on a transfer of land for charitable purposes in the State or Northern Ireland. The exemption is contained in Section 82 TCA 1999. An exemption from SD is also available on the transfer of designated securities to an approved body within the meaning of Section 848A TCA 1997.

4.3 Taken together, the reliefs from capital taxes available to donors are significant.

#### 4.4 **Corporation/Income Tax Relief**

A separate regime applies for tax relief in the case of donations out of income by companies or individuals. In every case, a donation to qualify for tax relief must be made to an approved body within the meaning of Section 484A TCA 1997.

The term “approved body” includes

- a body approved for education in the arts; or
- an eligible charity, which means a charitable body which has received tax exempt status by having received a CHY number at least two years previously; or
- any institutes of higher education.

The donation must be in the form of cash and/or designated securities, must not be subject to a condition as to repayment, and nobody can receive a benefit in consequence of making the donation, either directly or indirectly. The payment cannot be conditional and the minimum donation must be €250 to any one approved body in either the company’s accounting period or during the individual’s year of assessment.

4.5 Different conditions apply for various donors making a payment to an approved body:

#### 4.6 **Corporate Donors**

For a company making a donation, there is no maximum limit on the amount of the donation, which can be deducted in the company’s accounts as a trading expense, or an expense of management when calculating the company’s taxable income for a year of assessment. The company claims the relief in its annual tax return.

#### 4.7 **Individual Donors**

For an individual making a donation from 1 January 2007, certain Irish tax resident self employed high income individuals are restricted in the extent to which specified tax reliefs, including relief in respect of charitable donations, may be applied to reduce the individual’s tax bill.

Where the restriction is applicable, the amount of specified tax reliefs against adjusted income which may be claimed are limited to the greater of €250,000 or 50% of the individual’s adjusted income in any one tax year. Adjusted income is

calculated by adding together an individual's taxable income and the aggregate of the specified reliefs used in respect of a tax year. The restriction will apply to individuals whose adjusted income is equal to or greater than €250,000; and the aggregate of the reliefs used by the individual in the tax year is equal to or greater than €250,000.

However, the restrictions do not apply in a tax year where one-half of the individual's adjusted income is equal to or greater than the total of the specified reliefs used by the individual in that tax year. Any excess reliefs can be carried forward to the following and subsequent years.

In relation to donations made after 6 February 2003, if the aggregate of the donations made in a year of assessment by an individual to an approved body or approved bodies which are associated with that individual, exceeds 10% of the total income of that individual for that year of assessment, then the excess over the 10% will not be treated as a donation that would qualify for tax relief under Section 848(A) TCA 97.

- 4.8 For a self-employed person making a donation the amount of the donation can be deducted when calculating the individual's taxable income for the year of assessment when the payment was made. If necessary, tax will be repaid to the individual or the individual's spouse if applicable.
- 4.9 For a PAYE person making a donation they must give to the approved body a certificate stating the amount of tax paid by the donor in relation to the payment. The approved body is then deemed to receive the grossed up amount of the payment, and can claim a repayment of the tax paid by the donor.

## 5 REGULATION

- 5.1 The Charities Bill 2007 is to be welcomed as a long-overdue framework for the regulation of Irish charities, and knowledge of its features is important for people active in the charities sector, their financial and legal advisors, donors and foreign charities wishing to establish in the State.

### 5.2 The Charities Regulatory Authority (the "Authority")

For the first time in Ireland, a single, independent body will be established to regulate the charities sector. The Authority will have administrative functions (registering charities, keeping records of annual accounts and annual returns) and also law enforcement functions (overseeing the compliance with charity law, investigating and summarily prosecuting offences).

When the Authority is established by Ministerial order after the Bill has passed into law, the Commissioners for Charitable Donations and Bequests will be dissolved. All of their functions will be transferred to the Authority. At the same time, the role of the Attorney General as protector of charities will also be transferred to the Authority.

### 5.3 Registration and Regulation

#### *The Charities Register*

To function as an Irish charitable organisation, a body must apply to the Authority to be added to the register. Importantly, the Bill has been amended at Report Stage to provide an automatic entitlement for existing charities which hold a CHY number to be added to the register.

However, there is no provision in the Bill in relation to new applicants for automatic tax exempt status on acquiring charitable status. Rather, an application would need to be made to the Authority for a charity number, and a separate application would need to be made to the Revenue Commissioners for tax exemption.

As drafted, charitable bodies not holding a CHY number must apply to be added to the register within six months of the Minister's order establishing the register, or such later time as the Minister may prescribe.

#### *Accounting and Auditing*

For the first time in the State, charitable organisations will be required to prepare an annual statement of accounts and present it to the Authority with an annual report, much like the annual return requirement for Irish companies.

While much of the detail required in the annual statement of accounts has been left to be determined by Ministerial order, the Bill does include a threshold under which the accounting requirements will be relaxed. For charities whose gross income or expenditure is under €100,000, only an income and expenditure account and statement of assets and liabilities will be required.

A threshold also applies to the audit requirement, which is not specified in the Bill but which will be determined by Ministerial Order and will not exceed €500,000. Charities exceeding the threshold must have annual accounts audited, while charities under the threshold may either have accounts audited or examined by an independent person who is approved by the Authority. It is not clear from the Bill how an examination significantly differs from an audit.

For charities established as companies under the Companies Acts, the accounts and auditing requirements will continue to be those set out in Company Law. Within ten months of the end of a charity's financial year, that body must submit to the Authority an annual report. Again, the details of the report's contents have been left to Ministerial order, but the Bill does require that the report include a description of the charity's activities and that the audited or examined statement of accounts be attached. Through amendments introduced at report stage, the Companies Registration Office ("CRO") will provide the authority with copies of the annual returns submitted to it by charitable companies. Those companies will not have to separately submit accounts to the authority unless they are companies which do not have to submit accounts to the CRO with their annual returns. This is a further effort to enhance information – sharing between public bodies and ease the regulatory burden on charities.

Annual reports and accounts will be available for public inspection, save for those submitted by private charitable trusts, being charitable trusts not funded by donations from the public.

Failure to comply with the accounting, auditing and reporting requirements is an offence under the Bill. Offences prosecuted summarily by the Authority can attract a fine up to €5,000 and/or 12 months imprisonment. Offences prosecuted on indictment by the DPP can attract a fine up to €300,000 and/or ten years imprisonment.

The Bill also sets out for the first time a list of factors which will automatically disqualify a trustee or officer of a charity from acting in that capacity. These include bankruptcy, conviction of an indictable offence, sentencing to prison, disqualification as a company director, or removal by the High Court.

## **5.4 Investigations**

Much like the powers given to the Office of the Director of Corporate Enforcement to investigate and enforce Company Law, the Authority will be authorised to order investigations, examine a charity's books and records, question those involved with the charity, and seek orders from the High Court where it believes it is necessary in order to protect a charity's assets. These powers are far more extensive than those currently held by the Commissioners for Charitable Donations and Bequests, and the change is to be welcomed as a key factor in increasing public confidence in Irish charities.

## 5.5 **Updating Fundraising Regulation**

The Bill updates the existing fundraising legislation to bring within its scope two forms of fundraising that are common and currently unregulated: the selling of tokens, badges, pins and emblems; and the collection of promises of money (such as direct debits). Under the Bill, charities must now apply for a permit from the local Garda Superintendent in order to legally carry out these activities. This puts the regulation of these activities on par with other public collections.

## 6 **CONCLUSION**

For those who have a focus on philanthropy, the current economic uncertainty is clearly a factor in their thoughts. In many cases, the economic uncertainty is not interfering with the intention to proceed along a road of philanthropy. The uncertainty is causing donors to consider the timing of and size of donations.

There is much focus in this paper on the income and corporation tax reliefs which are available for donations to an approved body. For those who wish to establish any charitable Foundation which they wish to remain driven by their selected officers, now is an ideal time to establish a Foundation. There are two reasons for this. First, the 2 year period before a charity with a CHY number becomes an approved body is being run down. Second, the provision that enables charities holding a CHY number to be passported through the regulatory system with the Authority is an appreciable easing of the administration burden.

For those who have a focus on philanthropy, we hope these presentations assist in making the process more accessible, and will ultimately serve to strengthen and enhance the provision of benefits to the community.

**Paraic Madigan  
November 2008**