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Regulating European grant-making foundations. Lessons from the USA experience?[☆]

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Abstract

Grant-making foundations are private institutions that distribute their income to deserving organisations. In the USA, they enjoy fiscal incentives, but have to comply with complex rules securing that incentives are well deserved. In contrast, European countries have an embryonic legislation. This paper investigates whether the different tax rules adopted in the USA for independent and community foundations influence the grant-making behaviour of these organisations. Our econometric investigation underlines the existence of a large heterogeneity in the activities of both types, suggesting that the introduction of new regulations could benefit from a careful analysis of the nature and the features of these organisations.

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1. Introduction

Grant-making foundations and trusts (GMFs) are nongovernmental, nonprofit organisations whose assets (the endowment, generally donated by one or more donors) are managed by a board of trustees to generate the financial resources that are distributed in grants to pursue the specific goals stated by the foundations' donors and codified in their charters¹ (Andrews, 1956). GMFs distribute their grants in several fields, from culture to research, from education to health. These grants support deserving charitable organisations and fund innovative policies. The grant-making activity is very relevant nowadays that the economic crisis has reduced the spending capacities of the public sector, and the governments are looking for new ways of funding services to the population at large.

While GMFs exist on both sides of the Atlantic, large differences occur in their diffusion. They are very common in the USA and their activity is so typical of the North American culture that they have been considered 'a unique American answer to the problem of excess wealth in a society with limited income redistribution' (Anheier & Toepler, 1999) and a strong aversion to public welfare policies (McDonald & Miller, 2010). According to the latest available statistics of the Internal Revenue Service² (IRS), the assets of American GMFs exceeded \$ 613 billion in 2010, out of the about \$ 2.9 trillion net assets held by the entire nonprofit sector.³ In the same year, they disbursed more than \$ 44 billion in charitable grants, funding many cultural, research and welfare activities and organisations. No comparable figures are available in Europe, where data are collected by a few states only.⁴ However, research conducted for the European Commission (CSI & Max Planck Institute, 2008) shows that GMFs are increasing their role in Europe too, and new institutions of this kind are coming into life every year.

Unsurprisingly, historical differences in the diffusion of GMFs have influenced their regulation. In most legal systems GMFs benefit of fiscal incentives or exemptions because of their activities in favour of society. At the same time, they are the target of specific regulations trying to guarantee that those incentives are well deserved. However, the development of legal and tax rules varies widely. In the USA, a sophisticated system of federal rules – developed in the late 1960s – applies to GMFs all over the country. On the contrary, many European countries are characterised by a much more incomplete regulatory framework, although in recent years a wide debate on the nature of foundations, as well as on their legal and tax treatment, has developed.⁵ For example, in the UK, in 2010, the government launched a public consultation on the possible introduction of a minimum compulsory level of grants for foundations,⁶ a rule similar to the Minimum Payout Requirement included in the American legislation since 1969. In Italy, in 2011, the government

¹ Examples of these organisations include the Wellcome Trust in the UK, the Volkswagen Stiftung in Germany, the Van Leer Stichting in the Netherlands, the Carlsbergfondet in Denmark, the Fondazione Cariplo in Italy, and the Bill & Melinda Gates, Rockefeller, Ford and Mott foundations in the USA.

² All data are available from the IRS website: <http://www.irs.gov/uac/Tax-Stats-2>.

³ We refer to the so called 'tax-exempt 501(c)3 organisations'.

⁴ For example, in 2009, Istat (the Italian statistical office) published a comprehensive survey of Italian foundations (Istat, 2009).

⁵ On the possible disadvantages of harmonized taxation and fiscal legislation in the EU, and what could be learned from the experience of the USA see, for example, Salvatore (2002).

⁶ In particular, in the Green Paper on giving (H.M. Government, 2010) one can read that 'some suggest that foundations should make a minimum payout annually, as is the case in some other countries, as this could result in extra income for charities. Others suggest that a requirement would not help charities in the long term, and could generate unintended consequences. We would like to explore this issue further and welcome views on foundation giving.' (H.M. Government,

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