In recent years there has been a global increase in the interest in philanthropy and international advisors are frequently asked for a simple answer to the question as to how one selects the country from which to operate philanthropic activities worldwide. This is a question to which a sophisticated advisor should seek to resist giving a simple answer. Philanthropy is the new tax planning and maximum tax efficiency is only achieved if the tax planning is approached with the openness to complexity that is required in traditional tax planning. Just as there are a variety of tax and operational reasons determining where and how entrepreneurs operate their business interests around the globe, similar reasoning will determine that their philanthropic endeavours be international rather than being located solely in a single jurisdiction of choice.

The reality is that philanthropy is driven by many motivations and it is overly simplistic to categorize it as a homogeneous altruistic motivation. It is often misleading to characterize some of the greatest transfers of wealth to philanthropic purposes to even being philanthropic – being the love of mankind. Sometimes, philanthropy is the only reasonable option left to an entrepreneur with a philosophy that precludes giving too much wealth to family and an ideology that is opposed to paying taxes, especially estate taxes. There are quite a few of my clients who fit the profile of Warren Buffet, unfortunately not with the magnitude of his wealth, who come to philanthropy as a last resort. While I do welcome his money into the sector, I want to add a cynical note of caution about a philosophy that says his children can only be trusted with a fairly small amount of money for their own use but can be entrusted with five billion dollars to interfere in the lives of others. As advisors, it is important for us to remember that misguided philanthropists has the potential to do harm as well as good. Philanthropy is not only the new tax planning of our time, if implemented as the great white man’s burden it can also be the new religious zealotry of our time.

Ideally, the best location for learning philanthropy is at home around the kitchen table with those who are philosophically committed to the public good rather than in professional offices with high priced tax lawyers who have no visceral understanding of its role in society. Prior to her death, I sat on the board of an international philanthropy with Bill Gates’ mother. One time she hosted a meeting at her home in Seattle and I had brought my 6 year old son with me from Vancouver whom she put down for a nap in Bill’s bedroom. Having this grandmotherly experience triggered an impassioned maternal discussion about her son whom she despaired would never produce grandchildren for her, let alone have the time or interest to become involved in the charitable community. I must confess that 25 years ago I did not
know who her son was and what he was in the process of becoming. However, I do know that at the kitchen table in the Gates home there was a profound commitment to charity that I am sure has a bearing on why Warren Buffet would turn so much of his philanthropic estate over to Bill and Melinda Gates. It is far more common for entrepreneurs who have no background in philanthropy to learn about its operation in the family office or from other professional advisors.

It is important to understand the individual entrepreneur’s background and motivation for involvement in philanthropy. If philanthropy is an entrepreneur’s mechanism for developing recognition and respect for having “made it” as being incredibly successful among his or her peers and in the hometown community and that hometown is Cleveland, Ohio, it is irrelevant to talk about the merits of doing sophisticated philanthropy out of Switzerland. If the driving motivation is to “return some wealth to the community” in which it was earned and the source of the wealth is the oilfields in Oklahoma, the entrepreneur will only be annoyed if you advise that the ultimate location for philanthropy is the Cayman Islands. Similar problems arise if the entrepreneur has no real interest in active philanthropy and wants to build a monument to his or her success without having the problems of ongoing involvement or work in determining how the money will be invested or spent. In those situations, entrepreneurs build the biggest hospital wing, or civic auditorium or university research facility either locally or in the most prestigious university with which they have a credible link.

Philanthropy is much more interesting and there is a greater role for the type of advisors in this room when it is intensely personal in its objectives rather than being about recognition or a location. These entrepreneurs will ultimately organize their charitable activities in places that interest them personally or are convenient to their lifestyle choices and will require their professional advisors to handle the technical legal challenges necessary to make this possible. If these entrepreneurs have banking relationships, as well as ski chalets in Switzerland, it is likely unwise to praise the flexibility of foundations in Panama. The level of comfort which philanthropists have with their international banking and home office structures is usually a more important factor in determining the location of their philanthropy base than a comparative analysis of technical laws governing philanthropy.

The reality is that the location of where philanthropy is based is frequently predetermined by where the wealth is made. The determination is based upon the tax mitigation efficiency of charitable deductions where the assets of the entrepreneurs are located because those taxes are the ones which can be reduced by philanthropic gifting. Almost all tax relief measures are domestic in that Canada does not want to subsidize the philanthropy of charitable work carried out in England. Canadian entrepreneurs can only obtain tax relief for donations to eligible charities recognized and authorized by the Canadian government. Consequently, for many Canadian philanthropists the discussion as to location stops in Canada.

When considering the tax issues involved in dispositions of wealth, it is important to distinguish *inter-vivos* taxes and *inter-vivos* giving from estate taxes and testamentary giving. Frequently, jurisdictions with high gift and estate taxes, such as the United States, have lower income taxes. There are also important distinctions in that while US donors can only obtain a deduction from income tax if they donate to a charity resident within the US, they can obtain deductions from estate and gift taxes if they
donate to non-resident charities. Consequently, U.S. donors can make the determination to pay U.S. income taxes on money and then give it to a charity set up offshore knowing that those income taxes are an acceptable cost for moving charitable funds into a legal environment where they can grow faster and be used more flexibly if there are no gift and estate taxes.

When jurisdiction shopping for philanthropy, it is useful to bear in mind that countries which provide the most generous tax benefits for donating usually have the most restrictive rules on investing assets and operating a charity. Consequently, an advisor should consider whether it is better to avoid being seduced by the initial tax benefits of the deduction for the gift and look to a jurisdiction that offers greater freedom to invest assets and accumulate capital in a charity. For example, the United States has generous tax incentives to donate but then taxes unrelated business income of charities, restricts the percentage of a company that a private foundation can hold indefinitely and has stringent payout requirements to charitable causes as well as an excise tax. If entrepreneurs have a long term perspective and want their charitable foundation to invest heavily in environmental business enterprises, they might better pay the taxes necessary to move the relevant portion of their wealth to a tax haven jurisdiction where the regulator will not worry about the investment policies and returns of the charitable foundation and will not prevent foundations from continuing to own 100% of for profit environmental corporations. Such corporations may not generate enough income in the initial years to support the payout or disbursement quota requirements that are imposed on charities in Canada and the United States.

The strategy which might be the most useful to advisors in this room is to use a domestic foundation to provide tax protection for the exit taxes of someone wanting to move offshore. It is possible to calculate the optimum tax efficiency of what percentage of an entrepreneur’s wealth should be given to a domestic foundation to reduce the tax payable and enable the entrepreneur to take the remainder of his or her wealth offshore. For example, if your client in Canada sells her business to Google in exchange for $100 million of Google shares, and then sells the Google shares, she would pay $22 million in tax and have $78 million to take offshore. However, if she donated $27 million of Google shares to a public foundation and sold the remaining shares, her tax would be reduced to $4 million and leave her with $69 million to take offshore as well as $27 million in a Canadian foundation available for philanthropy back in the community and country in which she made her fortune.

The problem with philanthropic planning for entrepreneurs with sophisticated tax advice is that all of the tax planning for their commercial and estate purposes will have been designed to place them in jurisdictions where the tax costs are minimal. Philanthropic tax planning requires a reverse analysis in which donations are the most tax efficient if they come from the jurisdictions with the highest tax cost. Consequently, there is a need to do some jurisdiction shopping based upon high tax rates and the allowable methods of moving philanthropic funds internationally. Most of our entrepreneur clients have assets in multiple jurisdictions. For example, when advising one of my Hongkong clients who wanted to donate to Oxford University, there was little advantage in donating from Hongkong income or tax haven assets because of the low tax rates. Instead we looked at assets in the US and Canada and chose to use Canadian assets because at that time the after-tax cost of the donation was only 46 cents on the
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dollar instead of 85 cents in Hongkong. The result was that the newspapers talked about a Hongkong donor giving to Oxford but the technical reality was that the donor was a Canadian corporation.

There are many barriers to truly international charitable giving. This is because the fiscal policies of every country try capture domestically as much of the philanthropic dollar as possible. While philanthropy may be the new tax planning, traditional philanthropic tax planning is being jettisoned by some of the most innovative entrepreneurial “new wealth” philanthropists. If potential philanthropists are primarily interested in promoting alternative energy and industrial development at lower environmental cost, the most effective way to do this in many developing countries is to forgo the benefits and restrictions of charity law and operate exclusively in the for-profit mode.

For example, last week I was in Beijing for my ninth meeting this year with the government officials in the Ministry of Civil Affairs drafting the proposed new law of charity in China. A charity client in Canada which works with disabled people asked me to use my connections to obtain charitable registration in China. My response was that they would be better to set up a for-profit company in China that manufactured wheelchairs and related devices to assist the handicapped. They would have no significant problem in incorporating and implementing their business plan whereas registering a charity is almost impossible until this new law is passed by the National People’s Congress next year. If they make a profit the corporation can reduce its taxable income and increase market share by giving wheelchairs to poor people. The corporation can even reduce taxable income by lobbying for better building codes that require access facilities for disabled people which it would never be allowed to do as a charity. It would also be economically sustainable without donations.

Using for-profit mechanisms attract less adverse scrutiny from governments and competitors hostile to the politics and “costs” of socially responsible business practices. While the developed industrial world has largely discounted the possibility of altruism driving the agenda of for-profit companies, in parts of the world, and even in Canada, it can be the most effective way for philanthropists to proceed. A well planned “negative social investment” that triggers tax losses to achieve a social purpose is just as tax efficient as a charitable donation deduction and has almost no regulatory baggage. Innovative planning options such as this is why in our office we use the term “benevolent organizations” to describe our clients because there are many ways beyond conventional charity structures to achieve philanthropic objectives.

The most dramatic example of this thinking is Google which has elected to run its billion dollar “charity” as a for-profit division of the company. It will have almost no restrictions as to how it can carry on its activities and any advocacy it may want to do. As the experience of the micro-credit movement for which Yunus and the Grameen Bank in Bangladesh which were awarded this year’s Nobel Peace Prize has shown, enterprise and businesses are the most efficient and sustainable mechanism for charity. We all watch the philanthropy of Bill and Melinda Gates and see the hundreds of millions of dollars they are spending on charitable endeavours such as developing medicines and vaccines in Africa for black water fever, malaria and AIDS etc. I wish that their friend Warren Buffet would take an equal amount of money and pursue exactly the same objectives through a for-profit vehicle. Expenditure on research for medical vaccines is a deductible expense so the tax efficiency is there. It would be interesting to see
whether having these medical breakthroughs in a for-profit entity owned by a benevolent proprietor, or an offshore charitable trust, would actually benefit mankind more because it will be easier and likely more efficient for a for-profit company to take the intellectual property into the market place than it will be for a foundation which has so many restrictions on its ability to act in a commercial way.

There is likely a generational issue in how philanthropists approach these questions. If dealing with older philanthropists or inherited money there is usually a greater comfort level with traditional charity structures. However, the younger generation and especially extremely wealthy entrepreneurs in their 40’s who are first generation money, frequently hold the view that the only philanthropy that is effective is itself entrepreneurial. This is because they want the enterprise to become sustainable and prefer the view that the only true philanthropy is to provide someone with meaningful employment. It is frequently easier to “give” internationally by reducing the taxable income of for-profit corporations operated for altruistic purposes by providing additional education opportunities, daycare and medical benefits to employees pursuing a socially beneficial purpose rather than by operating under laws governing charities. If one adopts this view, then selecting the best location for philanthropy is a question of determining where you want the beneficiaries of your entrepreneurial activity to be located.

As indicated previously, if you have tax paid money and want to operate your philanthropy internationally, I believe that it is best to use substantially the same selection of location process that you would in for-profit jurisdiction shopping. It will be important to consider issues such as tax rates if you are going to carry on philanthropy through for-profit activities. You will also want to pay attention to questions such as whether there are multi-generational constraints on ownership such as the rule against perpetuities. I would strongly encourage you to consider a jurisdiction outside the traditional constraints of the common law restrictions that a charity be constituted for and carry on its activities on an exclusively charitable basis. This is because innovative cutting edge charitable endeavours will include purposes and methodologies which are not exclusively charitable. For example, you do not want to face a prohibition on funding children’s sports programs because sport per se is not charitable under the traditional law of charity. I know that the new Charities Act in England was given Royal Assent the day before yesterday and that it does include the promotion of amateur sport as a charitable purpose. However, in jurisdictions like Canada sport is still not charitable. Consequently, I would recommend a jurisdiction like the Cayman Islands which allows non-charitable purpose trusts so it is unnecessary to stay on top of all the nuances of the law of charity in different jurisdictions as being preferable to a jurisdiction, or vehicle, that will require exclusively charitable purposes.

One of the problems with charitable trusts is that many lawyers who only deal with charities when considering estate planning issues are not familiar with the exacting, and often arcane, word formulas required to meet the common law test of charity. Another advantage of a jurisdiction such as the Cayman’s is that it allows the trustees to have access to reputable courts to resolve questions of law when trustees need directions. There is comfort in the fact that the possibility exists of an appeal to the Privy Council in London.

If one is to operate internationally under the law of charity the optimum structure is to choose a jurisdiction that allows charities to incorporate and allows directors to be chosen outside the
membership. In Canada, for example, a charity would incorporate federally or in a jurisdiction like British Columbia rather than Ontario because Ontario makes it a legal requirement that directors be or become members. The advantage of separating out members is that ultimately members have control in the same way that shareholders do in a for profit corporation. However, when addressing jurisdiction issues the tax authorities almost always restrict their analysis to the nationality or residence of the directors. Consequently, you can have all your members being residents of Hongkong and elect directors all of whom are residents of Canada but none of whom are members. In this scenario, if the Canadian directors begin to act too far outside the intentions of the philanthropist, he or she as a member can remove all the directors without even inviting them to the meeting at which the deed is done. I have just come from London where I have created a charity with English directors but the members are exclusively Canadian so the Canadians will never lose control of the charity even though they cannot disavow any actions taken by the English directors while they were in office.

Unfortunately, in today’s world any international funding of charitable activities must be done in compliance with anti-terrorism laws. It is also necessary to be mindful of the “best practices” guidelines that various countries have adopted due to the focus of the Financial Action Task Force of the OECD on charities funding terrorism. It is problematic to determine how active a process of due diligence is required. The more control that the donor has over the funds from the time of donation until the final expenditure of those funds the greater the comfort of the regulatory authorities. Unfortunately, by the same measure, the greater control the donor has over the ultimate expenditure, the greater the donor’s responsibility should any funds find their way into the hands of “terrorists”. I must end on this unhappy note that the regulatory authorities increasingly view charities as the primary conduit for funding international terrorism. The United States Treasury Department issued a “final” version of the draft best practices voluntary guidelines on September 30. The OECD has similar guidelines and England is about to issue new guidance on terrorism and charities. These countries then informally add the most restrictive provisions of the regulations of the other countries to the standards to which they seek to hold charities accountable. Increasingly, sophisticated international philanthropy will require more compliance advice with regard to money laundering regulations than tax advice in setting up the structure.