IMPACT OF THE OVERLAP OF PUBLIC AND PRIVATE INITIATIVES ON THE PHILANTHROPY TAX REGIME IN FRANCE

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Introduction

In most European countries, philanthropy has seen rapid and conspicuous development over the past 20 years. This is notably visible in France, where donations from individuals subject to tax deductions increased by 70% between 2006 and 2016. Moreover, two-thirds of the foundations in France have been created since 2000.¹ This phenomenon, whereby private actors voluntarily collaborate with public authorities to serve the ‘common good,’² enables a synergy between vastly different cultures and different parts of society.

However, at the same time, some actors serving the public interest can be driven to include a degree of profit-making activities to complement their resources or to achieve their goals, depending on the challenges they face and according to the mechanisms described in this study.

The hybridisation of economic models among an ever-increasing number of actors is not unique to France and is well documented in international academic research.³ In practical terms, such hybridisation led to a profound upheaval in the major categories of reference in social and economic spheres. Consequently, the redistribution of roles between the public and private sectors blurred the traditional boundaries between commercial activities and activities that fall within the scope of public interest. This unavoidable evolution of economic models corresponds to regulations aiming to define clear boundaries between public and commercial interests.

The difficulties in distinguishing commercial and public-interest activities discussed in this chapter pertain to European competition regulations, which limited state subsidies in accordance with the *de minimis* rule.⁴ However, this problem is highly apparent in the French context because, after decades of restricting public-interest financing to the state and public authorities nearly 20 years ago, France decided to encourage private generosity by providing significant tax benefits.⁵ The rapid growth of philanthropy, or the transfer of proceeds from economic success to serve the common good, is a notable indicator of the redistribution of roles between the public and private sectors, increasing the number of interactions between actors with diverse interests and the complexity of the resulting models.

Using the French context, this chapter aims to describe this gradual increase in porosity between economic activities and public interest by reviewing the background of such developments and the problems they pose. It also outlines proposals for adapting the definition of public interest to specific economic activities to restore consistency between the law and the official guidelines by administrative authorities and avoid depriving organisations and actors of scarce funding while addressing some of the most acute problems facing today's society.

I Transformation of relationships between non-profit actors, the commercial world and the public sector

The deep transformation of the relationships between various actors supporting public interest and their economic models is rooted in the socio-historical context of the last quarter of the 20th century. The Glorious Thirties, the 1970s and the 1980s failed to remove poverty and exclusion mainly because of two factors of economic relegation. The first is the growing urbanisation and the desertion of some rural areas which created geographical pockets of poverty. The second is the consequence of unemployment induced by successive economic downturns after the oil crises became both a cause of economic hardship and social relegation.⁶ Consequently, job creation for long-term unemployed became a matter of public interest, with a special focus on the causes of poverty and relegation; that is, the vulnerabilities of territories and individuals.⁷ While this two-fold effect is prevalent even after 40 years, the challenge today is to establish clearly defined criteria to identify these vulnerabilities.

This socio-historical context, which is shifting the dividing line between the economic and social spheres, is simultaneously experiencing a radical reorganisation of public-interest financing. An increasing complexity is visible in two areas: a change in the ecosystem, with the multiplication and diversification of donors, and a change in their relationships with public funders, with the nature of the funding transforming from a subsidy into a form of service rendered for value.

A Developments in the public sector

1 Growing scarcity of public resources and the recourse to private funding

In the past 20 years, there has been an inexorable rise in the cost of some of the state's sovereign missions (e.g., education and healthcare, with the increased duration of compulsory schooling,⁸ the ageing of the population⁹ and the growing technology of healthcare). In this context, philanthropy has become a popular method of financing or supplementing the financing of certain initiatives.

Thus, in search of additional revenues, the French legislature frequently extended the list of bodies or the scope of actions that may benefit from philanthropic contributions to sectors which have been almost entirely financed by public money until now.¹⁰ This is notably the case for higher education, research, culture and heritage protection. Apart from direct legislative intervention, public bodies also created 'friends' associations¹¹ to raise funds while providing donors with tax benefits for voluntary contributions. The scarcity of resources thus encourages public bodies to compete with associations and foundations in the philanthropic fundraising 'market'.

2 Transformation of subsidies into a service subject to public procurement rules

Over the past 30 years, public actors have had to review the scope and methods of their actions under the combined effect of shrinking public resources and a decrease in public subsidies.

Initially, associations receiving regular subsidies were generally considered *de facto* representatives of the state or some other public entities responsible for public missions. However, this situation met increasing criticism because it was viewed as a kind of ‘debudgeting’. This connection between subsidised associations and the state is challenged for two main reasons.

- First, the purpose or scope of subsidies and the methods of assessing the achievements of such subsidies lack sufficient regulation.
- Second, the European Union (EU) rules regarding fair competition oblige public entities to select their suppliers and providers through a tender process. But if one of the bidders receives subsidies, this would be considered an infringement to fair competition rules. Therefore, entities receiving public subsidies should frequently be excluded from public tenders.

Thus, supervisory bodies also contributed to the rise in the suspicion of public subsidies granted to public-interest actors.

To comply with the EU's principles of fair competition, public authorities gradually dressed subsidies as a price paid in exchange for services within the framework of public tenders. However, private companies can also bid on these tenders. This approach is likely to attract both associations and new service providers from the commercial world. National surveys on associations indicate a major change in their resource structure between 2005 and 2011: a decrease in public funding from 34% to 25%, combined with an increase in public procurement from 17% to 24%.¹²

Therefore, public authorities treat associations as service providers, which has serious consequences for their economic and fiscal models. What was previously a matter of public interest is shifting towards a traditional commercial relationship, which now falls within the ambit of the legal and fiscal rules specific to such a relationship.

B Developments in the commercial sector

Parallel to the changes concerning public actors, the relationship between the commercial sector and public interest is also evolving.

1 Progressive institutionalisation of corporate philanthropy

In France, the first foundation, Fondation de France, was created in 1990¹³ based on the American model. Twenty years after its emergence, a corporate foundation, the new ‘American uncle’ of the French non-corporate service sector, led to private donors supplementing and taking over state action. Private actors in the field welcomed this development, as they constitute an additional source of revenue. However, these actors are in an awkward position between profit and not profit. This is a characteristic of what we refer to as the hybridisation of their model.

Regarding the dividing line between commercial activities and activities for the ‘common good’, despite undertaking a public-interest mission lying beyond the scope of the company's corporate purpose, in the early 1990s, corporate giving was deductible from the company's

revenue, similar to its expenses. This provision, which is still applicable in most developed countries,¹⁴ helps to blend philanthropy into the company's business model. In France, this regime changed in 2003,¹⁵ following which philanthropic activities were incentivised through tax deductions rather than being deducted from the companies' taxable income. This development emphasises the benefits of public subsidies. It had consequences when the 'doctrine of causes', a historical framework defining the scope of tax shelters according to the charity's objectives and formed the cornerstone of philanthropy in France, was shaken up by European competition law, as discussed in the next section.

2 Corporate social responsibility and the introduction of an endogenous corporate mission of public interest

Article 116 of the Law of 15 May 2001 on 'the new economic regulations'¹⁶ proposed that companies listed on the stock exchange must include information regarding their corporate social responsibility (CSR) activities in their annual reports.

Thus, the associations gained new funding, accompanied by new constraints. Already providing services to the state, they now became service providers for CSR activities with similar consequences for the complexity of their economic and fiscal models (e.g., the obligation to implement specific analytical accounting, known as 'sectorisation', or even to create subsidiaries, among others).

The case of Simphon, examined further in the following, provides a telling example of the impact of the rise in CSR on the relationship between companies and public-interest operators. This social business offers free training in digital professions to low-income and marginalised people. Thus, companies trying to improve the diversity of their human resources, an important component of CSR reporting, no longer remain donors but have also become the clients of Simphon by sponsoring the remuneration of the trainers for those lacking solvency.

With the increasing demand for private intervention in social issues, CSR and sustainable development have become key arguments for companies to resist the scrutiny and short-term views of some of their shareholders; therefore, to improve their position in this challenge, some American companies found a solution that includes such social issues in their corporate purpose, with the B-corp (benefit corporation) status. Hiller's study describes the context of the development of this new model in the United States,¹⁷ while Reiser analysed its advantages and limitations.¹⁸ In France, this movement culminated in the *Plan d'action pour la croissance et la transformation des entreprises* [Action Plan for Corporate Growth and Transformation] Law enacted on 21 May 2019, which created mission-based companies. However, unlike in the United States,¹⁹ this new model does not have a legal status in France.

II 'Public interest market': A grey area

A Historical subjectivity in the concept of public interest

The concept of public interest, which is sometimes portrayed as universal and unchallengeable, is, conversely, truly subjective. This observation was not new. For instance, sociologist Chloé Gaboriaux analyses the recognition of the public utility of associations and foundations by the *Conseil d'Etat* (French Supreme Administrative Court) during the Third Republic (1870–1914). When the *Conseil d'Etat* was just renewed by the republicans and thus sought to establish its

legitimacy and the impartiality of its opinions, Gaboriaux nevertheless demonstrates the impact of the subjectivity of the members of the highest administrative court, their value systems and their personal relations.²⁰

Beyond personal positions and ideological convictions, the borders of public interest saw historical and geographical fluctuations, depending on the context. Notwithstanding some points of stability, such as solidarity and access to education and healthcare, some causes appear, while others disappear. However, in the long term, the scope of public interest increased significantly. For example, in France, access to culture, once accepted as a privilege of the powerful, was included as a public interest cause since the end of the 19th century,²¹ whereas the environment was included within its scope only in the past few decades.²²

Another example of this volatility of public utility in France can be found in the early 20th century idea of ‘municipal socialism’. This historical concept was analysed by the legal expert Katy Sibiril in an article on the notion of interest in French administrative law.²³ In this case, some local elected officials utilised public utility to justify their intervention to address the inadequacy of the private sector in meeting the requirements of trade, management of water or electricity and distribution services or public transport in rural areas. This interventionist stance was justified only because the local authorities deemed it necessary to satisfy universal needs. From this perspective, market competition, which has considerable significance today in the assessment of public interest, was not considered a relevant criterion.

While the present economic logic is returning to the concerns of public interest, unlike municipal socialism, it operates less as an aim but rather as a means of integrating citizens through work. Thus, the desire to promote integration by enabling people to find employment is clearly in the public interest and therefore within the scope of philanthropy.

B New distinction in economic markets between the public and private sectors

New private markets are now developing in sectors that were financed mainly by public authorities 50 years ago. An ageing and dependent population is a key example of this development. The ‘silver economy’ is now a regular economic market which is estimated at over 130 billion euros²⁴ and is regulated in France by a supply chain contract since 2013.

These changes led to a fundamental evolution in the concept of public interest. Today, the distinction is no longer determined by the sector of intervention and the purpose of activity by applying the ‘doctrine of causes’ but by other criteria such as the fragility or vulnerability of populations and territories. This new mechanism is probably more relevant, as it allows for a more specific consideration of the needs of the target population rather than predetermining eligible areas. However, defining its boundaries remains challenging.

C The social and welfare sectors as alternatives to the liberal capitalist model

In 2014, the French legislature recognised a specific field of the economy known as the *économie sociale et solidaire* [social and welfare economy (ESS)], composed of four types of organisations: mutual companies, cooperatives, associations and foundations²⁵.

The 2014 law also introduced *Entreprise Solidaire d’Utilité Sociale* [Welfare Company of Social Utility (ESUS)] accreditation for ESS companies serving the public interest or public utility that have democratic governance and reinvest most of their profits in the company. This

accreditation entitles the holder to specific resources, including welfare-based employee savings schemes and tax reductions.

The ESUS accreditation aimed to urge private investors to encourage greater participation in corporate projects with social utility through tax incentives. Their investments have a purpose other than profit, enabling the creation of an environment for developing welfare-based enterprises. However, this accreditation led to a new form of hybridisation by bringing together associations, mutual companies, cooperatives and even traditional companies seeking to distinguish themselves from other commercial enterprises. Despite the intent to create a credible alternative to the global capitalist enterprise, this new mechanism further increased the complexity in defining a scope that is already fragmented and composite, as organisations eligible for accreditation (associations, mutual companies, cooperatives and foundations) have very different missions and operations.

The diagram (e.g., Stages 1, 2 and 3) shows three successive stages of the growing complexity of the relations and flows (donations or investments) between the actors in the French context: those traditionally working under general interest vs. private interests. In the middle, the grey area represents the ‘public interest market’, where private actors integrate some of their economic activities to serve the public interest.

Stage 1: Traditional actors on the spectrum from public to private interests

Figure 30.1 Stage 1: Traditional actors on the spectrum from public to private interests

Stage 2: Three-stage legislative evolution of the interactions between economic actors and the public-interest sphere

- 1990 law: creation of the corporate foundation marking the emergence and recognition of the private donor to supplement and take over state action
- 2001 law: introduction of CSR, an endogenous corporate mission for public interest
- 2014 Law on Social Economy: The legislature-recognised economic field, ESS, composed of four types of organisations: mutual companies, cooperatives, associations and foundations.

Figure 30.2 Stage 2: Three-stage legislative evolution of the interactions between economic actors and the public-interest sphere

Stage 3: New models and complex flows defining the grey area of the ‘public interest market’

- Private resources funding public interest
- New economic models (hybrid social enterprises, benefit corporations)
- Impact investment targeting hybrid models.

Figure 30.3 Stage 3: New models and complex flows defining the grey area of the ‘public interest market’

The proposals formulated in this chapter focus on shifting the limit of public interest to the dotted line in the middle to include hybrid social enterprises, according to the conditions described in the subsequent sections.

III History of the tax regulatory framework in France

A Set of rules and three definitions

This section interprets the eligibility criteria of the philanthropic shelter tax regime according to its regulatory context. For this, we delineate three relevant concepts and their associated rights arising from the *Conseil d'Etat* case law, tax legislation and the official guidelines of the tax authorities.

1 Public utility

This concept is part of the official guidelines of the administrative authorities, recognised by the case law of the *Conseil d'Etat*, upon the proposal of the Ministry of the Interior.²⁶ Public utility depends theoretically and explicitly upon the concept of public interest, as mentioned in Articles 200 and 238 of the French General Tax Code. Nevertheless, in practice, the *reconnue d'utilité publique* [recognition as being of public utility (RUP)], a body regulating public utilities, rarely casts doubt on whether an activity constitutes public interest.

2 Public interest

This second concept also follows the official guidelines of the administrative authorities,²⁷ in this case, tax authorities, which are under the Ministry of Finance.

- Donations to public interest, which form the basis of the philanthropy tax regime, are regulated by Article 200 of the General Tax Code. It entitles donors to a 66% reduction in income tax equal to the gift amount, subject to a ceiling of 20% of the taxable income. The reduction is applicable to donations and payments, including the express abandonment of income or proceeds made by taxpayers domiciled in France to organisations listed under Article 4 B.
- Article 238 *bis* of the General Tax Code adapts Article 200 to corporate giving by defining an almost identical scope. The reduction of up to 60% of the donation amount is applicable to income or corporation tax (and 40% reductions for donations over 2 million euros).
- In terms of the wealth tax, Article 885–0 V *bis* A of the General Tax Code relating to the *Impôt de Solidarité sur la Fortune* [Solidarity Tax on Wealth] reproduced in Article 978 for the *Impôt sur la Fortune Immobilière* (Real Estate Wealth Tax) defines a narrower scope which is different from Article 200 of the General Tax Code. In this case, the applicable reduction is 75% of the donation amount, with a ceiling of 50,000 euros.

3 Social utility

Law No. 2014–856, regarding the social and welfare economy, provides a precise definition of social utility. Under this law, enterprises (i.e., associations, foundations, cooperatives and mutual companies) whose objectives satisfy at least one of the following three conditions are recognised as being of ‘social utility’.

- Their aim is to support economically and socially vulnerable people or those with adverse personal circumstances or who need social or socio-medical support due to their health condition. Such persons may be employees, users, clients, members or beneficiaries of this enterprise.

- Their aim is to help prevent exclusion and inequality in healthcare, socio-economic and cultural matters to provide education to citizens, particularly through community centres, to protect and support social and territorial cohesion.
- They contribute towards sustainable development in its economic, social, environmental and participatory dimensions to support energy transition or international solidarity, provided that their activities are related to one of the aims mentioned in 1) and 2).

After public interest, social utility has its own doctrine of causes with no reference to public interest, the tax treatment or the fiscal framework of philanthropy.

The two fiscal frameworks do not fall within the ambit of the same set of rules. Nevertheless, while they overlap, they do not duplicate each other and have a fundamentally distinct set of provisions. The concept of social utility is split between the *Conseil d'Etat's* conception, which *de facto* presumes public interest, and the definition of the ESUS accreditation regulated by the ESS law, which differentiates itself from the official guidelines of the tax authorities. In practice, this split is particularly confusing for public-interest funders who must determine whether the organisation seeking involvement is eligible for philanthropic tax benefits. Nevertheless, in France, the distinction between for-profit and non-profit remains fundamentally determined by its tax law.

B Official guidelines of the administrative authorities and their limits

1 Introduction of the '4Ps' rule

In the mid-1990s, the administrative authorities' guidelines²⁸ originally intended to settle a tax investigation problem regarding the criteria for determining cases when associations and assimilated organisations should be subject to commercial taxes, namely corporation tax, value-added taxes (VAT) and territorial economic contributions. However, the concept of public interest was subsequently extended to regulate the scope of the philanthropy tax regime.

The boundary between taxed and non-taxable activities was previously based on the 'doctrine of causes' and depended upon the aim of the organisation's activities: pursuing a philanthropic goal and conducting a for-profit economic activity. From a tax perspective, this teleological approach was a source of great insecurity as inspectors were obligated to question the tax status of non-profit organisations upon finding that their management used similar methods or activities that placed the organisation in competition with private enterprises. Thus, the doctrine of causes was unsuitable for determining the scope of commercial taxes, despite its coherence with the statutory definition of the scope of donations eligible for the philanthropic tax benefits provided by Articles 200 and 238 *bis* of the General Tax Code. The objective or cause of the organisation prevails while establishing the scope of non-profitability, determining fiscal liability and delineating the right to benefit from the philanthropy tax regime. The presumption of eligibility for the philanthropy tax regime is, therefore, almost systematic when the funds received by the organisations fall within the ambit of this doctrine.

However, Articles 200 and 238 of the General Tax Code do not define the concept of public interest. They refer to the official guidelines of the tax authorities, which have three conditions to be satisfied beyond the cause doctrine:

- disinterested management,
- widespread beneficiaries that are not limited to a small circle of people, and
- non-profitability.

From the outset, the semantic conflation of profitability with economic activity blurs the reasoning of eligibility for philanthropic tax benefits.

When the guidelines were introduced, the public-interest sector had a limited scope of activities requiring donations. Therefore, non-profitability was analysed solely in terms of the volume of economic activity. As far as their economic activities were not preponderant, organisations would not be liable for commercial taxes and would remain eligible for philanthropic benefits.

However, by the late 1990s, the EU imposed new rules in line with the policies of competition law.²⁹ The non-profit sector was affected by the state subsidies received, especially those received indirectly through philanthropic tax incentives. France was particularly affected because, since 1995, such incentives took the form of a tax reduction rather than a simple deduction from the taxable base. A law enacted in 2003³⁰ significantly increased tax reductions. However, this measure also led to the suspicion of French non-profit organisations benefiting from the philanthropic regime.

Therefore, the analysis of non-profitability is not limited to the preponderance of economic activity. The French tax administration devised a '4Ps' grid, which is better suited to verify whether an association with commercial activities competes unfairly with other businesses.³¹ This inquiry focuses on the following aspects:

- **Product:** Does the 'product' offered cater to a need that is either not catered to or inadequately catered to by the market? In other words, the product offered should not be available in any market where it can be procured under similar terms, which is tantamount to ensuring that there is no risk of competition with businesses in the commercial sector.
- **Public:** Do the target beneficiaries ('public') suffer from any difficulties (unemployment, disability, age etc.) that make them worthy of philanthropic interest and justify the grant of special benefits?

The beneficiaries in this case refer to direct 'clients' or recipients of the activity and not those for whom the activity could be a source of employment.

- **Prices:** If the product is not gratuitous, are the prices significantly below the market prices (beyond the effect of tax exemptions), such that they facilitate access to similar services for people in difficulty?
- **Publicity:** Advertising ('publicity') or, more broadly, marketing and sales methods that lead to the presumption of competition, may only be used to appeal to the public's generosity while considering the type of target beneficiaries the organisation serves. The purchase of advertising inserts, sale of a catalogue on newsstands or participation in trade shows may call into question the non-commercial nature of the organisation's approach. However, in the age of digital communication and social media, this criterion is losing relevance.

The non-profit nature of the organisation should be assessed by all four criteria and not just based on one criterion. Furthermore, the presence of competition must be assessed '*in concreto*', implying that a product or service would not be considered competitive if it has no competitors within a radius of several dozen kilometres. However, this concern has been undermined by the fact that, in the case of VAT, the EU Court of Justice subsequently retained the importance of competitive potential rather than the presence of actual competition.³²

As European law applies to circumstances of hybridisation of for-profit and non-profit markets, reasoning based on unfair competition prevails over the doctrine of causes.

This new dominant paradigm to assess the scope of public interest has several limitations, as seen in the case of Montessori schools. Although the law states that private education is a matter of public interest, in 2013 and 2014, the local authorities of the tax administration considered one Montessori school in the form of an association ineligible for philanthropy. This was because this school had three other Montessori schools operating as limited liability companies (and therefore subject to commercial taxes) within a radius of less than 30 km. Thus, these schools fell within the same ‘geographical area of attractiveness’³³ defined under the tax code.

The liberal approach characterising Europe favours private companies’ interventions in public-interest issues. Despite public service constraints, European tax laws prefer to apply the normal rules of competition, even if it means allowing private companies to assume any public service obligations while scrupulously preventing it from becoming a means of distorting market competition. This approach exemplifies the regulation on the ‘Services of General Economic Interest (SGEI)’.

2 Public interest and the exclusion of profit-making activities: A nonlinear movement

The official guidelines issued by the tax authorities favoured the 4Ps rule in certain cases. For instance, these guidelines resolutely protect the disability sector against scrutiny over unfair competition. The administrative authorities accept that *Etablissements et services d’aide par le travail* [establishments and assistance services through employment] would not fall within the scope of competition³⁴ distortion because the additional costs incurred by disabled workers significantly exceed the advantages of the tax benefits. Moreover, disabled workers are considered beneficiaries or the ‘public’ of the 4Ps and not clients to whom the products or services are sold.

In other cases, the doctrine of causes prevailed. France was an early campaigner in Europe to exclude the cultural sector from a competitive analysis. Recently, this exception includes the audio-visual and press sectors.

Conversely, some early examples of the rejection of the doctrine of causes due to evidence of competition include a decision by the tax authorities based on an old case of the *Conseil d’Etat* relating to the Association de médecine du travail du département de la Mayenne.³⁵ In this case, it was held that any activity aimed at providing services to businesses is necessarily ‘profit-making’. Accordingly, administrative instructions state that for an activity to remain of public interest, its main purpose must not consist of applying resources to enable enterprises to conduct or delegate tasks to third parties that are either compulsory or useful to their main activity. In other words, to determine its tax regime, an organisation conducting non-profit operations may assume a non-profit role solely to satisfy tax eligibility based on the identity of the beneficiaries and the services it provides.

3 Weaknesses of the hybrid model

- Supremacy of guidelines over tax law.
- After the introduction of the ‘4Ps’ analysis grid, rather than revising the law or putting the doctrine of causes into perspective, France chose to allow two different types of reasoning to coexist. This led to the paradoxical application of the current tax law guidelines in France.
- Distorted link between commercial taxes and ineligibility for philanthropic tax benefits.
- Ideally, the shift from a purpose-based definition of non-profitability to that based on an absence of competition with businesses should have ended the connection between the

payment of commercial taxes by non-profit organisations and their ineligibility for philanthropic tax benefits. However, the tax authorities did not foresee the consequences of this evolution and continued to restrict the eligibility of non-profit organisations engaged in profit-making activities to enjoy philanthropic tax benefits. In some respects, this amounts to considering that the mere fact of conducting an activity for payment implies that it is no longer of public interest.

- Stopgap proposal of the sectorisation of profit-making activities with ‘preponderance’ of the non-profit-making activity.

The sectorisation of profit-making activities could enable organisations to retain philanthropic tax benefits without creating a separate legal person, provided that the donation amount is not utilised for profit-making activity and does not act as a subsidy that could distort competition. However, sectorisation is only suitable for organisations that can clearly distinguish and isolate an economic activity that is not preponderant from other activities.

Several conditions must be satisfied to be allowed to sectorise an economic activity:

- **Separation of commercial activities from non-profit-making activities:** An organisation’s activities must correspond to services of a different nature, which does not exclude an element of complementarity as far as the two activities are effectively separated.
- **Principle behind sectorisation:** According to the 16 February 1999³⁶ instruction, sectorisation must be based on a ‘principle of a physical separation or individualisation of the relevant activities in relation to the association’s main activity, notably with respect to the place of production, human and material resources and investments’. However, the tax instruction of 18 December 2006³⁷ specifically curtailed this requirement and allowed associations to apply the same resource simultaneously if they could justify it based on the association’s purpose (e.g., achieving social diversity). In such cases, the separation of activities may be limited to the accounting aspect by separating the expenses and incomes from various activities or for various kinds of beneficiaries.
- **Preponderance of non-profit-making activities:** An association must not be guided by commercial activities, while its non-profit-making activities must remain materially preponderant. This distinction must be assessed to reflect the true weight of the association’s non-profit activity, such as by measuring the ratio of commercial income to an association’s overall financial resources (operating income, subsidies, subscriptions, donations, etc.), without a set percentage of margin of appreciation set by tax authorities. However, the example published in the 1998 tax instruction indicated a ratio of 75% of resources from the non-profit sector to 25% of commercial income. However, additional criteria may be considered, such as the magnitude of voluntary work and the number of staff and resources devoted to profit and non-profit-making activities, respectively. This preponderance was assessed based on a multi-annual average.
- **Isolating income and expenditure of exempt activities vs. taxable profit-making activities:** Cost accounting should enable the isolation of income and expenditure relating to the sectors of exempt activities and taxable profit-making activities, where each sector must bear its incumbent costs. This requires the allocation of operating resources to either the profit or non-profit sector. In the case of assets for common use, a distribution mechanism must be devised.

The application of sectorisation is particularly complicated for small organisations that are often underequipped to deal with legal issues. Therefore, it does not resolve the requirements of

organisations whose purpose depends on a predominant economic activity or whose economic activity would be considered extremely similar to the other activities.

The Simplon case: an emblematic hybrid

The Simplon project, a socially conscious welfare enterprise, was co-founded by Frédéric Bardeau in 2013. It leverages digital technology to promote the inclusion of disadvantaged or vulnerable groups (migrants, older adults, people with disabilities) while supporting the digital transformation of organisations. Simplon.co is a network of socially aware and inclusive factories that offer its clients free training in digital technical professions, both in France and abroad.

Through its 109 factories worldwide, Simplon has already trained more than 11,476 people, 78% of whom are job seekers, with a positive outcome rate of 67%³⁸ after training.

The project is widely recognised for providing free training to insolvent persons on a large scale. The majority of the project's budget now comes from public funds. However, to remain economically feasible, the Simplon project was forced to create three organisations in the course of its development:

- An ESUS-approved **simplified limited liability** company, a commercial body positioned in a market consisting of companies seeking to improve their recruitment diversity in the age of CSR and that of the state, local authorities (regions) and the Employment Agency. This entity brings together ESS investors and receives public subsidies and issues invoices in its capacity as a training organisation for third-party funders (trainees are not liable for payment).
- **An endowment fund**, with the capacity to collect donations and issue receipts for receiving tax deductions. The endowment fund supports activities that are complementary to training such as social support, French lessons for refugees, mobility assistance, housing assistance and drop-out prevention scholarships.
- **An association** that receives grants from donors that cannot be channelled through the ESUS-approved SAS or the endowment fund and that which assist a part of the support activities, excluding training and occupational integration.

According to Frédéric Bardeau, 'this forced hybridisation of our model is the source of many complications in the management of the project, particularly in terms of governance and human resources'. In a 2019 report by the Court of Auditors that addressed this emblematic case,³⁹ the state expressed its regret regarding the Simplon Foundation directly subsidising free and inclusive activities conducted by the ESUS-approved SAS as an umbrella foundation but without proposing a solution nor questioning the impact of Simplon's actions.

IV Proposed changes and methods

The proposals in this chapter have a three-fold objective: (i) to modernise the concept of public interest to adapt it to new circumstances (as in other periods of its history), (ii) to make administrative authorities' official guidelines comply with the law and (iii) to urgently simplify the work of public-interest operators and protect their access to essential resources to fulfil their missions.

A Constraints

The regulation and application of public interest face two types of constraints.

The first constraint is the predominance of the objective of public interest in conducting an activity. This primarily involves ensuring that the pursuit of gain ('profit') does not determine the activities of the relevant organisation. Tax authorities already mostly consider this constraint by requiring disinterested management, executive remuneration and the democratic functioning of the organisation. While some adaptations might seem appropriate, the present rules for non-corporate bodies do not require any significant modifications.

The second constraint is the rules pertaining to competition and state subsidies. Measures to prevent unfair competition due to philanthropic tax benefits are not unique to Europe. From a global perspective, it is also one of the recommendations of the 2020 OECD report on taxation on philanthropy (recommendation 6.6.2).⁴⁰ As discussed earlier, the guidelines of the French Tax administration give paramount importance to the numerous and stringent constraints of European law.

However, the general opinion supports upgrading the doctrine of causes upheld by Articles 200 and 238 *bis* of the General Tax Code, accounting for the constantly evolving list of subjects eligible for philanthropy, which corresponds not only to the structural changes in society but also to economic cycles. Consequently, the assistance provided to a small business after a natural disaster or in a severely underdeveloped region would not be analysed in the same way as under 'normal' circumstances in a developed country.

- Analysis of competition: A complex undertaking

The analysis of competition is a complex process. Competition may arise directly because of the actions of the organisation seeking benefits from the philanthropy tax regime if its services overlap with those provided by commercial enterprises. However, indirect competition occurs when the benefits enjoyed by the organisation are transferred, notably in the form of lower prices, to businesses to conduct activities to meet their aims.

Tax authorities' comments redefining the condition of non-profit organisations regarding 'commercial taxes' already attempted to define competition. They emphasised that competition can be effective in certain geographical areas and not in others and is limited to certain categories of products or services while being assessed based on their target clients.

However, these efforts were partly undermined by the European courts' adoption of a stricter approach, particularly regarding VAT. In 2017, the Court of Justice focused on the potential rather than the effective nature of competition regarding this tax.⁴¹ This allowed non-profit organisations to compete with each other or with companies, despite operating in different geographical areas. Similarly, it obliged the tax authorities to adopt a more restrictive approach to VAT exemption on services provided by an entity, especially created by non-profit organisations, for their own needs (Article 261 B of the General Tax Code). This is a real concern for these associations.

The lesson to be drawn from these regulations is that rather than using the theoretical analysis of competition to define the tax treatment of transactions, it would be better to try to use the exceptions or derogations provided in the sixth VAT Directive, particularly Article 13. By relying too much on the commentaries of the FTA, taxpayers, including non-profit organisations, cannot be sure that such commentaries could not be challenged by the EU Commission or by the ECJ.

- *De minimis* subsidies⁴²

The European regulation regarding subsidies compatible with the internal market provides some criteria for restricting and relaxing subsidies. The latter is applicable for *de minimis* subsidies that may be granted to small enterprises or for amounts that are considered too insignificant to distort competition.

These regulations enabled the introduction of an amendment on support offered to small businesses (cf. Article 238 *bis* (4) of the General Tax Code regarding the grant of financial subsidies to or equity investments in SMEs). This provision was adapted to the European regulation on state subsidies compatible with the internal market, which required prior approval from the European Commission.

Article 17 of Commission Regulation (EU) No. 65/2014 of 17 June 2014, mentioned in Article 238 *bis* (4) of the General Tax Code, concerns organisations accredited for paying certain financial subsidies or providing non-financial support services, such as advice to SMEs. This reference provides a framework for utilising financial subsidies by targeting new investments or acquiring assets from organisations. Financial subsidies must not be remunerated, whereas the assessment of their value should treat support services as donations in kind.

The conditions for accreditation notably require the relevant organisations to be managed in a disinterested manner, the subsidies to satisfy the criteria for *de minimis* aid and the amount paid each year to an enterprise to not exceed 20% of the organisation's resources. This example illustrates the complexity of the system and the hierarchy of EU rules over national regulations.

Moreover, it seems clear that the benefits of the provisions favouring philanthropy and the nature of organisations' non-profit activities are obsolete. Therefore, it warrants a revision of this connection along with the overly global and systematic approach of the tax authorities towards organisations that complement the activities of profit-making enterprises, particularly *associations intermédiaires* [intermediary associations], *entreprises d'insertion* [job seekers' support organisations or the ESUS].

- Organisations' use of legal forms other than associations

The provisions of Articles 200 and 238 *bis* of the General Tax Code could be applied to companies, even in the cultural or research sectors. Organisations operating in various sectors, including those supporting integration through employment, housing and dependent support, constitute different forms, such as cooperative companies or even traditional corporations. However, legal statutes should not justify, by themselves, exclusion from the scope of the philanthropy tax regime.

Accordingly, a parallel could be drawn with Article 107 of the Treaty of Lisbon, which determines the areas of subsidies considered compatible with the internal market, as listed in the following.

- Promoting economic development of regions with an abnormally low standard of living or serious under-employment.
- Facilitating the development of certain economic activities or regions without altering trade conditions to be contrary to public interest.

However, the preference for a corporate form rather than an association should not be used to circumvent non-profit constraints, such as in terms of remuneration. If allowed to conduct an activity in public interest, companies must pay special attention to their governance and resource use, particularly regarding the devolution of assets in the event of cessation of activity.

The problem of executive remuneration or the risk of a diversion of philanthropic funding due to a privileged relationship between organisations and the beneficiaries of their actions must be scrutinised. However, this should apply to all organisations, regardless of their legal form.

B Proposals

The following proposals aim to arrive at a better definition of the scope of public interest in the context of Articles 200 and 238 *bis* of the French General Tax Code and the official guidelines of the administrative authorities. However, these proposals do not seek to extend the scope of the benefits provided by other legislation, nor do they deviate from the principles laid down by European law.

From this standpoint, we outline the following proposals for redefining the scope of public interest:

1 Three cumulative conditions to be presumed by public interest actions

We propose a three-stage approach to overcome the difficulties of assessing public interest. Moreover, in addition to the organisations mentioned previously, organisations that satisfy the following cumulative conditions should be eligible for the philanthropic regime:

- Disinterested governance

The first eligibility condition is to ensure that the organisation's governance is disinterested.

As discussed, Articles 200 and 238 of the General Tax Code already apply to certain companies. However, an increasing number of actors in public interest tend to opt for a commercial status to benefit from institutional investments, which, in the current context, deprives them of the potential for philanthropy that could aid their missions.

Following the progress made by associations and foundations, other social and welfare organisations (SSEs) should also diversify their resources as far as possible to guarantee disinterested governance.

- Purpose of the project

Once the first condition is satisfied, the next step is to analyse the purpose of the project. If the conditions relating to the purpose of the project are not satisfied, then the project will not be eligible.

We propose that the terms 'family', 'social' and 'humanitarian' in Articles 200 and 238 *bis* of the General Tax Code be interpreted based on the relevant tax instruction. To clarify the scope of these terms, such instruction could draw inspiration from the terms used to define the scope of ESUS accreditation (vulnerable people, prevention of exclusion, maintaining and strengthening territorial cohesion, the preservation and development of social cohesion, etc.). Alternatively, they could also refer to the definitions proposed by organisations representing the philanthropy sector as part of the working group set up in 2013 on the territoriality of donations led by Gilles Bachelier.⁴³ These proposals are inspired by the definitions of social and medico-social action provided in Articles L116–1 and L312–1 of the Code of Social Welfare and Families.⁴⁴

Additionally, the conditions listed in III B 1 should apply not only to project operators but also to those who support them by providing advice and/or funding, provided they operate under public interest and from the non-profit sphere.

Furthermore, advocacy, when distinguished from the promotion of particular interests, should be considered a means of conducting actions related to a public interest cause and should therefore benefit from the rights attached thereto, provided that the cause served is eligible for philanthropic benefits. Some prominent and effective examples of public interest actions include Greenpeace's work to protect the environment or the fight against AIDS.

- Non-competitive nature of the project

The third issue is determining whether the nature of the project is non-competitive. This requires considering the three criteria (product, public and price) currently used by the tax authorities. The activity must offer a product or service that meets specific social needs.

- For products or services that are currently unavailable in the territory under consideration, a time-based criterion should be introduced to support activities in their starting phase. For instance, some activities that are useful in terms of public interest may be unprofitable before finding a suitable economic model.
- If the first condition is not satisfied, then the product or service must be offered at a price that is accessible to people in vulnerable circumstances.
- If the first two conditions are not satisfied, then the product or service should be provided to a group that does not currently have access to it (e.g., job seekers' support organisations helping people obtain employment).

2 Invert and clarify the conditions for implementing sectorisation

Rather than limiting economic activities, philanthropic resources should be sectorised to indicate the charges that they may legitimately cover. This mechanism would help to justify the additional costs incurred by a public-interest organisation when acting for people in difficulty or in deprived areas, thereby promoting transparency while avoiding any suggestion of unfair competition.

Nevertheless, the limitations of sectorisation listed earlier remain relevant and require further review. The conditions under which philanthropic funds can be traced should be specified. For example, regarding job integration initiatives, there is continuity between activities that are part of a competitive sector and those that are not. The same beneficiary may require both professional and social support, one of which may not fall under philanthropy. Thus, the funds intended for each of these activities may, in part, be common, yet administrative authorities are reluctant to address such situations. Therefore, a regulatory framework for the sectionalisation of activities should also consider such situations.

3 Amending the statutory provisions of the general tax code relating to philanthropy

As provisions on philanthropy are not limited to the official guidelines of the administrative authorities, the statutory provisions of the General Tax Code relating to philanthropy may require an amendment.

Given the risk of interference with EU law, some aspects of the contemplated amendments must be subject to prior notification to the European Commission. This precaution should be taken to forcing organisations that may have already received donations to reimburse the funds received in the event of a dispute. Dealing with such risk is all the more important to avoid donors' tax benefits from being challenged.

Frequently updating these regulations would be cumbersome because of the nature of the notification procedure. Therefore, the content and scope of the regulatory mechanism should be clarified before they are notified to the European Commission. This would require a detailed consultation and documentation outside legislative text, which could also serve as a basis for the administrative authority's comments on the proposed mechanisms. Such a process would also provide an opportunity to address two concerns: the challenge of anticipating answers to potential questions asked by the European Commission and the challenge of clarifying the rights and obligations of the organisations concerned.

Conclusion

The analysis of public and commercial interests overlaps with the economic and social spheres. Additionally, the increasing complexity of the relationships between public, private commercial and private non-profit actors highlights two main ideas:

- Public interest is and will necessarily remain a partially subjective concept, whose scope cannot be set in stone and whose interpretation would vary with time and space. Therefore, it is important to adapt its scope to societal evolution and train administrative authorities to interpret the same while understanding the true constraints and motivation of the actors in the field.
- The idea that the preponderance of profitable economic activities within an organisation should inevitably imply its for-profit motives, and therefore its incompatibility with public interest is largely erroneous.

Although this chapter focused on the French context, it is clear that methods to improve the untenable situation faced by several public-interest operators must be explored at both the national and European levels. To start, subsequent efforts should focus on identifying and analysing these issues in various national contexts to identify similar issues and converging action policies.

Notes

- 1 Fondation de France (2019). Panorama national des générosités [National panorama of donations]. And Fondation de France (2018). Enquête nationale fondations et fonds de dotation [National survey of foundations and endowment funds].
- 2 The term 'common good', which indicates a general, philosophical concept, will be used in quotation marks to clearly distinguish it from the concepts of public interest, public utility and social utility, each of which refers to specific legal and/or fiscal concepts.
- 3 Livia Ventura (University of Geneva) provided an excellent overview of the development of hybrid models internationally (L. Ventura [2019]. The social enterprise development and the birth of hybrid entities. A comparative law perspective. *Expert Focus*, 3, 170–174). Heather Sertial also analyzed the development of hybrid models in the United States and their limits and challenges (H. Sertial [2012]. Hybrid entities: Distributing profits with a purpose. *Fordham Journal of Corporate & Financial Law*, 17, 261).
- 4 In EU Law, this principle of regulating state subsidies of economic operators takes its name from the Latin legal maxim *De minimis non curat praetor* (the chief does not bother with the details).

- 5 Law n° 2003–709 of August 1, 2003, on philanthropy, associations and foundations, introduced reductions on corporate tax (60% of the amount of the gift) and income tax (66%).
- 6 E. Malinvaud (1986). Les causes de la montée du chômage en France [The causes of the rise of unemployment in France]. *Revue française d'économie*, 1(1), 50–83.
- 7 P. Rosanvallon (1981). *La crise de l'Etat-providence* [The crisis of the welfare state]. Seuil, Paris.
- 8 Law n° 2019–791 of July 26, 2019 regarding 'a school of trust' increased the duration of compulsory schooling for 16–18-year-old children. Moreover, the age of entry for primary school was reduced from six years to three years.
- 9 People aged 65 and above constitute 20.5% of the population in 2020. Their share has increased by 4.7% in the past 20 years. (M. Martin & E. Rignols (2020). Tableaux de l'économie française. *Collection Insee Références Édition*, 24–25.)
- 10 F. Charhon (2016). *Vive la philanthropie!* Cherche Midi, Paris.
- 11 Created in 1871, Les amies et amis de la commune de Paris was the first friends' association in France.
- 12 V. Tchernonog & L. Prouteau (2019). *Le paysage associatif français: mesures et évolutions* [An overview of French associations – measures and developments]. Dalloz Juris Associations, Paris.
- 13 Law No. 90–559 of July 4, 1990, on the formation of corporate foundations and amendment to the provisions of Law No. 87–571 of July 23, 1987, on the development of philanthropy.
- 14 See OECD (2020). *Taxation and philanthropy*, OECD tax policy studies, n° 27. OCDE Editions, Paris, p. 96 and following.
- 15 Law n° 2003–709 of August 1, 2003 (article 40).
- 16 Law n° 2001–420 of May 15, 2001 on new economic regulations.
- 17 J. S. Hiller (2013). The benefit corporation and corporate social responsibility. *Journal of Business Ethics*, 118(2), 287–301.
- 18 D. B. Reiser (2011). Benefit corporations – a sustainable form of organization. *Wake Forest Law Review*, 46, 591.
- 19 In the United States, the B-corp legal status is not recognised at the federal level; however, 37 states have adopted this status in their legislation.
- 20 C. Gaboriaux (2017). Une construction sociale de l'utilité publique [A social construction of public utility. Associations and foundations before the Conseil d'Etat (1870–1914)]. *Genèses*, 4, 57–79.
- 21 M.–C. Gonet-Delacroix (1992). *Art et Etat sous la IIIème République* [Art and state under the Third republic]. Editions de la Sorbonne, Paris.
- 22 Law n° 76–629 of July 10, 1976 on the protection of nature.
- 23 K. Sibiril (2012). *La notion d'intérêt en droit administratif français* [The notion of interest in French administrative law]. University of Brest, France.
- 24 Ministère de l'économie des finances et de la relance. (2017). Qu'est-ce que la silver économie ou économie des seniors? [What is the silver economy?]. Retrieved from: <https://www.economie.gouv.fr/entreprises/silver-economie-definition>.
- 25 Law No. 201–856 of July 31, 2014 on the social and welfare economy.
- 26 Law of July 1, 1901 on the association contract (article 10).
- 27 Article 11 of the law August 11, 1954, which introduced a tax benefit for gifts to 'oeuvres ou organismes d'intérêt general' in France.
- 28 Instruction 4 (1998), 170 of September 15, H-5–98.
- 29 ECJ judgment of 1970 France c/Commission (61969CJ0047). Subsequently, on December 10, 1998, the European Commission published a notice on the application of the state aid rules relating to direct business taxation (98/C 384/03).
- 30 Law n° 2003–709 of August 1, 2003.
- 31 The 4P rule is defined in *Bulletin Officiel des Finances Publiques* [Official Bulletin of Public Finances] BOI BOI-IS-CHAMP-10–50–20–20120912.
- 32 ECJ (19/01/2017) aff C 344/15. National Roads Authority.
- 33 Tax rescript refusal by letters of October 1, 2013, and March 24, 2014, received by the Association Ecole Maria Montessori from the local authorities of the tax administration of Essonne.
- 34 BOI No. 61 of 9 June 2008.
- 35 Conseil d'État (November 6, 1995). Association de médecine du travail du département de la Mayenne
- 36 Instruction 4 (1999), 33 of February 16, H-1–99 'Concerning the Tax Regime Applicable to Non-profit Organisations'.
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- 39 Cour des comptes (2019). *Fondation Agir Contre l'Exclusion: Exercices 2013 à 2017*. Rapport, pp. 58–59. Paris.
- 40 OECD (2020). *Taxation and philanthropy, OECD tax policy studies*, n° 27. OCDE Editions, Paris.
- 41 CJEU (19 January 2017). National Roads Authority.
- 42 *De minimis* subsidies are small state subsidies granted to businesses. For amounts below EUR 200,000 per company over a three-year period, the relevant EU countries are not obliged to notify the European Commission.
- 43 G. Bachelier (2013). *Les règles de territorialité du régime fiscal du mécénat* [The rules of territoriality in the French philanthropy fiscal regime]. Rapport au ministre de l'économie et des finances, Paris.
- 44 Code de l'action sociale et des familles [Code of Social Welfare and Families] (1956, last updated on April 5, 2021).

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