

made simple guides

Made Simple guides are aimed at finance professionals working in charities. They cover technical areas such as risk assessment, accounting, tax and VAT treatments and aim to provide practical guidance to busy accountants in charities.

The content of guides is correct at the time of going to print, but inevitably legal changes, case law and new financial reporting standards will change. You are therefore advised to check any particular actions you plan to take with the appropriate authority before committing yourself. No responsibility is accepted by the authors for reliance placed on the content of this guide.

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Tax effective giving made simple

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sayer vincent

consultants and auditors

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CFDG (Charity Finance Directors' Group) is the professional body for finance directors within the sector, and has nearly 1,500 members. CFDG provides assistance to charities on a range of issues, such as accounting, taxation, audit and other finance-related functions. CFDG's mission is to deliver services that are valued by members and enable those with financial responsibility in the charity sector to develop and adopt best practice.

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Introduction

Various tax incentives are available to individuals and companies to encourage giving to charity. Gift aid has been covered in a separate made simple guide. This guide outlines the other key methods of making donations to charity tax effectively and incorporates the VAT implications of some of these forms of giving.

There are opportunities for both individuals and companies to structure their giving in such a way that it helps them to save tax and helps the charity to achieve its objectives. What many people do not realise is that the tax relief for giving away shares or property is very generous. Charities should therefore be encouraging this form of giving among their supporters and providing much better information on how it operates.

Even if you are a small charity and do not have an investment portfolio, you can sell the shares and get help to do that through ShareGift, a service set up to help charities. All charities can also access donated goods from businesses through In Kind Direct and there are various other intermediary services.

Some time spent researching what is available and providing guidance to the staff and volunteers in your organisation may be well rewarded.

1 Payroll giving

The payroll giving scheme enables employees (and pensioners paid through PAYE) to make regular donations to charity by having their donations deducted from their salary before calculation of their income tax liability. Employees can choose to give regular or variable amounts and can specify which charities benefit. As the donations are deducted from gross pay, higher rate taxpayers receive automatic higher rate tax relief and the recipient charity does not need to reclaim tax as with gift aid.

There are a number of agents authorised to operate payroll giving schemes. The employer must first contact an authorised agent to set up the scheme. The employer then deducts employees' donations from gross pay as part of the PAYE process and pays these over to the agent. The agent must distribute the donations to the employees' chosen charities within 60 days.

Agents' fees may be deducted from the payments to charity, charged to the employer or charged to the beneficiary charities. Any costs the employer incurs in running the scheme are allowable expenses for tax purposes.

2 Inheritance tax reliefs

Legacies are an important source of income for many charities. Lifetime and death transfers of property to a charity established in the UK are exempt from inheritance tax. Gifts to charity are deducted from the value of the estate before applying the nil band and calculating the inheritance tax due. There is no limit on how much can be gifted and as a result charitable gifts can be used to entirely eliminate any inheritance tax liability. Many people arrange their affairs so that a part of their wealth passes to charity rather than to the government.

One planning point for donors is that if they intend remembering a charity in their will, it may be better to make lifetime transfers of any assets that would be subject to inheritance tax and leave the tax saved to charity. However, donors are best advised to seek professional advice before setting up wills and lifetime transfers.

The will must name the beneficiary charity and if the charity has ceased to exist it used to be a problem. Now the Charity Commission has set up a register of mergers. Providing the merger or transfer is entered in the register of mergers, the successor charity is entitled to the legacy.

3 Gifts of shares and securities

Since April 2000 UK income tax payers and corporation tax payers can obtain tax relief if they give shares in quoted companies or unit trusts to a UK charity.

The amount of relief available to the donor is the market value of the disposal, plus any transfer costs, less any payment or benefit received from the charity. If a person connected to the donor receives any benefit as a result of the donation, this also reduces the tax relief available. The market value is determined at the date of transfer. The charity can ask the donor to dispose of the shares on its behalf, though it must be clear that the donor is doing so as agent of the charity. Income tax payers claim relief in their tax return or by notifying their tax office. Companies claim relief as a charge on income in their tax return. Donations are treated as 'no gain, no loss' disposals for capital gains tax purposes.

It is sometimes better for donors to sell investments and donate the proceeds under gift aid. For example, if the investments are standing at a loss, the donor may be better off using the loss and claiming higher rate relief on the gift aid payment. It worth checking the tax relief by both routes.

4 Gifts of land and buildings

From April 2002 UK land and buildings can also be gifted in the same way as qualifying shares and securities.

The donor must dispose of the whole of their interest in the property to qualify for the tax relief. If the property is held jointly or in common, all owners must gift the whole of their interest to the beneficiary charity at the same time.

The donor must first contact the charity to confirm it can accept the gift and obtain a certificate from the charity confirming the disposal. The certificate must:

- describe the property being gifted
- specify the date of transfer
- state that the charity has acquired the qualifying interest in land.

The donor can deduct from taxable income the market value of the property including valuation and disposal costs, less any payment or benefit received. The gift is also treated as a 'no gain, no loss' disposal for capital gains tax purposes and the charity is exempt from stamp duty land tax. The market value is at the date of disposal and it is advisable to obtain a professional valuation. Donors can seek confirmation of a valuation from the Valuation Office Agency.

As with shares and securities, it may sometimes be better for the donor to sell the property and gift aid the proceeds.

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Gifts of business assets

It is sometimes easier or preferable for businesses to give goods or assets to a charity. For example:

- business equipment, trading stock or manufactured goods
- temporary use of assets such as the free loan of equipment or free use of premises.

Income or corporation tax implications:

- Gifts of trading assets within the capital allowances regime are treated as disposals at nil value. This enables the business to claim full capital allowances on the donation.
- Gifts of trading stock and manufactured goods are treated as sales at nil value. The business can claim a deduction against its taxable profits for the cost of the donated goods but does not have to deem any income to have been received in respect of the gift
- If goods are donated from outside the EC they will be free of VAT on import and customs duties, though certain goods such as alcohol are excluded from this exemption.

Gifting business assets can sometimes have adverse VAT consequences for the donor. The basic VAT position is that where a business gives a business asset on which it recovered input VAT, this is a taxable supply by the business and it must account for output VAT on the value of the supply. For an outright gift the value is essentially the fair value of the gifted asset and for temporary use of an asset the value is determined by reference to the asset's depreciation over the period of use by the charity. However, there are a number of exemptions.

If goods are donated for sale, hire or export by a charity then the

supply by the donor is zero-rated. The sale, hire and export of donated goods are also zero-rated activities in the hands of the recipient charity and the VAT on purchases attributable to these activities is recoverable by the charity. If a gift of goods is made in the course of the donor's business activities and the cost of the gift is less than £50 there is no supply for VAT purposes and the donor does not have to account for output VAT on the gifted goods. This typically applies to gifts of small promotional items.

Where the value of the supply by the donor is small, HMRC officers will usually adopt a pragmatic approach and regard the supply as de minimis, so the donor can ignore any VAT implications. This would probably cover, for example, the free use of a vehicle or premises for a one off event or the donation of old stock or equipment for the charity's own use.

If the donor does account for output VAT on the gift the recipient charity can treat this as input VAT. The donor should give the charity a normal VAT invoice overprinted with the statement: 'Tax Certificate. No payment is necessary for these goods. Output tax has been accounted for on the supply.'

Giving staff time

Businesses sometimes second staff to a charity. If the business is effectively donating an employee's time, then it can continue to deduct the costs of employing the person as an allowable expense for tax.

For VAT purposes, if the charity pays for or contributes to the business's costs of secondment, then, even if this amounts to consideration for the supply of the seconded employee, it is by concession treated as a nil value supply by the seconding business. This is subject to the condition that the placement is not done by the seconding business for financial gain. A similar concession for the placement of disabled workers exists.

6 Gifts of private assets

The specific reliefs for qualifying shares and for property apply equally to gifts of assets held privately. Gifts of private assets to UK charities are treated as ‘no gain, no loss’ disposals for capital gains tax purposes. They are also exempt for inheritance tax purposes and if the gifts come from outside the EC, they are free from VAT on import and from customs duties.

Sales of ‘pre-eminent’ objects such as outstanding works of art, land and buildings to certain national museums and institutions under a private treaty arrangement may be exempt from inheritance tax, capital gains tax and VAT. The recipient body must be listed in schedule 3 to the Inheritance Tax Act 1984. Bodies which exist wholly or mainly for the purpose of preserving for the public benefit a collection of scientific, historic or artistic interest can be added to the list by Treasury Order. The arrangement is designed to encourage donors to sell to national institutions at below the normal market value. The treaty must require the vendor to share the tax saved with the institution, typically by agreeing a sale price that is less than the market value by 75% of the tax saved by the donor.

Detailed guidance on the scheme is available from the Museums, Libraries and Archives Council website and donors contemplating selling a pre-eminent object can consult the Council for advice on the public institutions most likely to be interested in acquiring it.

7 Substantial donor rules

The Finance Act 2006 introduced legislation designed to combat certain abuses of the tax reliefs for gifts to charity. The legislation deems certain transactions between a charity and its substantial donors to be non-charitable expenditure by the charity. As a result, the charity becomes liable for tax on an equivalent amount of income.

A substantial donor to a charity is anyone that provides ‘relievable gifts’ of £25,000 or more in a period of 12 months, or £100,000 or more in a period of six years. Other charities, connected housing associations or wholly owned trading subsidiaries cannot be substantial donors.

‘Relievable gifts’ are donations of cash or property that attract tax reliefs for gift aid, payroll giving, disposals of qualifying interests in shares, securities and land, ‘no gain, no loss’ gifts of chargeable assets, donations of trading stock and the capital allowance reliefs. Inheritance tax reliefs are not included so the receipt of a legacy exceeding £25,000 does not make the donor substantial.

If a donor is substantial in any 12 month or six-year period, then they are substantial in all of the charity’s ‘chargeable periods’ that overlap the 12 month or six-year period and for the following five chargeable periods. The chargeable period for a charitable company is its financial year and for a trust the tax year 6 April to the following 5 April. Donations made before the introduction of the legislation (22 March 2006) count when determining if a donor is substantial, but the legislation only applies to transactions that take place on or after 22 March 2006.

The rules apply to certain types of transaction between a charity and a substantial donor and persons connected to a substantial donor. However, there is a general exception for benefits provided to a donor below the gift aid donor benefit limits. The transactions caught and the specific exceptions are:

| <i>Type of substantial donor transaction caught</i> | <i>Exceptions</i> | |
|--|--|---|
| | <i>Supply from a charity to a substantial donor</i> | <i>Supply from a substantial donor to a charity</i> |
| The sale or letting of property | No exceptions | If the supply takes place in the course of a business carried on by the substantial donor and on arms length terms or better for the charity and is not part of a tax avoidance arrangement |
| The provision of services | If the services are primary purpose and on terms no more beneficial than those on which provided to others | |
| The exchange of property | Qualifying disposal at undervalue of shares, securities or land and 'no gain, no loss' capital disposals at undervalue | |
| The provision of financial assistance | No exceptions | If the terms are arms length or better for the charity and not part of a tax avoidance arrangement |
| Investment by a charity in a business of the substantial donor | The purchase of listed shares and securities | N/A |
| Payment of remuneration by a charity to a substantial donor | The remuneration is for services as a trustee which is approved by the Charity Commission etc | N/A |

The substantial donor rules are complex and may capture entirely innocent transactions between a charity and its substantial donors. The government has acknowledged these difficulties and on 15 July 2008 HMRC launched a consultation on proposals to reduce the impact of the substantial donor legislation on charities. The proposals are:

- Revised thresholds for qualifying as a substantial donor – the thresholds for relievable gifts would be £50,000 in 12 months or £125,000 in three years with a de minimis limit of £1,000 per annum, below which relievable gifts can be ignored when assessing if a donor is substantial
- Introduce further exemptions for 'arms length' remuneration and primary purpose grants provided to a substantial donor or connected person
- An annual de minimis limit of £500 below which all payments and benefits provided to a substantial donor can be ignored.

All proposals would, if implemented, be applied retrospectively from 22 March 2006.

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Conclusion

Charities that receive donations from individuals may be able to increase the value of those donations by structuring them tax efficiently. Gift aid is the best known tax relief and is a very effective route for increasing the value of cash donations from UK taxpayers. It can be administratively burdensome, but the benefits will usually outweigh the costs.

However, for businesses, other forms of giving may be more interesting to them and frequently companies are interested in a whole package to include corporate events and staff giving. Therefore, charity teams need to be aware of the whole range of tax reliefs and benefits available to companies and their owners.

In particular, dealing with major donors, you will need to be able to understand the donations and other help from their point of view. However, you may also need to explain the law to major donors if there is a potential breach of the substantial donor rules or some other aspect of tax.

Charities should never forget that donations may affect both the charity's and donor's VAT positions. The donor may have to account for output VAT on the gift and donations may restrict a charity's ability to recover VAT on purchases.

Donors to charities will expect the charity to know the rules and be able to explain them right at the beginning. So make sure your guidance and your staff know the rules so that you can make the most of the tax reliefs for giving.

Further information

A guide to tax incentives for corporate giving

Joint HM Treasury & Home Office publication
www.hmrc.gov.uk/charities/guide_tax_incentives.pdf

Guide to tax effective giving

Institute of Fundraising
www.tax-effective-giving.org.uk/index.html

Sharegift website

www.sharegift.org/

In Kind Direct

www.inkinddirect.org/

Valuation Office Agency

www.voa.gov.uk/

HMRC guidance on substantial donors

www.hmrc.gov.uk/charities/guidance-notes/annex2/annex_ii.htm#11

Museums Libraries and Archives Council website

www.mla.gov.uk/