



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS
IN ENGLAND AND WALES

6 October 2008

Our ref: ICAEW Rep 117/08

Your ref:

Substantial Donor Consultation
HMRC Charities
Mail Station A
100 Parliament Street
London
SW1A 2BQ

Email: substantialdonors.consultation@hmrc.gsi.gov.uk

Dear Sirs

SUBSTANTIAL DONORS TO CHARITY

The Institute of Chartered Accountants in England and Wales (the Institute) is pleased to respond to your request for comments on the Consultation Document *Substantial donors to charity: A review of anti-avoidance legislation around large donors to charity*.

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours faithfully

Caron Bradshaw
Secretary to Charities Sub-Committee
Technical Strategy
T +44 (0)20 7920 8579
F +44 (0)20 7638 6009
E caron.bradshaw@icaew.com



THE INSTITUTE
OF CHARTERED
ACCOUNTANTS
IN ENGLAND AND WALES

ICAEW Representation

ICAEW REP 117/08

SUBSTANTIAL DONORS TO CHARITY

Memorandum of comment submitted in October 2008 by The Institute of Chartered Accountants in England and Wales, in response to the HMRC Consultation Document *Substantial Donors to Charity*, published in July 2008.

Contents	Paragraph
Introduction	1
Who we are	2 - 4
General points	5 - 10
Answers to specific questions in the consultation	11 - 20

INTRODUCTION

1. The Institute of Chartered Accountants in England and Wales (the Institute) welcomes the opportunity to comment on the Consultation Document *Substantial donors to charity* (the Consultation Document) published by the HM Revenue & Customs (HMRC).

WHO WE ARE

2. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 130,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.
3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
4. The ICAEW Charities Sub-Committee is responsible for co-coordinating the technical considerations of the charity sector with respect to Chartered Accountants working within or for charities. Its membership represents the interests of practitioners, their clients and Chartered Accountants employed in financial roles within charities.

GENERAL POINTS

5. The Institute supports HMRC's efforts to counter tax avoidance. However, HMRC appear unwilling or unable to explain what abuses they are trying to legislate against in their provisions for substantial donors. We suggest that, if the current legislation (even subject to the proposed amendments) does not close perceived loopholes, there is little point in having a law unfit for purpose, particularly where there is a myriad of unintended consequences for charities conducting bona fide transactions. Amending tax legislation by further legislation is always difficult so we urge the Government to withdraw the legislation altogether, and develop new provisions that are based on known abuses and are proportionate to the amount of tax evaded.
6. We have contributed to and endorse fully the submission of The Charity Tax Group (CTG) to HMRC on the Consultation Document. We agree with the CTG's overriding view that the changes proposed in the consultation do not go far enough to address the adverse consequences of the substantial donor legislation. The current provisions impose a significant administrative burden on charities in requiring them to identify substantial donors, connected persons and transactions which might fall within the legislation. We are unable to establish the size of the problem that HMRC considers to exist so it is difficult to assess whether the current legislation, amended as proposed, is likely to address the perceived abuses. On the contrary, we are concerned that the legislation has the potential to harm charities where it catches innocent transactions, and the need to monitor donations diverts charitable resources from their proper application of meeting charitable objectives. We also consider that the penalties when the legislation does apply are disproportionate, having the effect of taxing the total value of the amount paid by the charity, rather than any benefit received by the donor.

7. We therefore urge HMRC to consider changing the legislation to delete Section 506 A (3) so that only transactions which are at a value which disadvantages the charity are treated as non-charitable expenditure, and only to the extent to which the charity is disadvantaged. The legislation should also be amended so that only transactions which are carried out with a view to tax avoidance are penalised.
8. We recommend that there be a clearance procedure. This is standard where there is complex and/or wide-ranging anti-avoidance legislation, as taxpayers need certainty as to the tax treatment of particular transactions. A clearance procedure would enable charities to ascertain whether they could accept large donations, or engage in particular transactions. In our view, if transactions caught by the legislation were restricted to those involving tax avoidance (by a taxpayer), the number of transactions requiring clearance would be very small (probably much smaller than, say, the number of Section 776 clearances that are currently required for charities).
9. We deplore the effect of the current legislation, which is to penalise the charity and remove its exemptions where tax avoidance that falls within these rules does take place. The penalty should be imposed on the person who has received the tax relief on the donation in question.
10. We are concerned that the tax liability on the charity may be out of all proportion to the tax relief given to the donor. This is particularly harsh where payments by the charity are treated as non-charitable expenditure, even if they are on arm's length terms. We recommend that the penalty be based on the donation, and, further, that the penalties should be restricted to donations on which tax relief is claimed. It would then be possible for a donor not to make a claim if they did not wish to. This would apply where a donor did not wish the charity to be disadvantaged by transactions, where their own tax relief was small.

ANSWERS TO SPECIFIC QUESTIONS

Chapter 2: exempt transactions

Would the proposed arms length exemptions (for arms' length remuneration and arm's length grant funding) be welcomed by charities?

How many additional transactions do you envisage would be exempt under each of the proposed arm's length tests that are not currently exempt?

What is the value of the tax saving that you would expect to experience for each of the proposed arm's length tests? Do charities anticipate that there would be any other benefits or quantifiable savings?

Are there any issues or concerns as to how this will work in practice and the extent to which charities are able to demonstrate that remuneration and grant funding are paid at arm's length? What, if any, do you estimate the costs of providing this information to be?

Are there any other likely costs? If so, what would the value of these costs be?

Are there any additional transactions between charities and their substantial donors that are not currently exempt but which Government should now consider exemptions for? What would be the associated cost and benefit implications to charities of exempting these?

11. The time allowed for responding to the Consultation Document was not long enough to enable us to assemble the information needed to reply in detail to each of these questions.

12. We support the recommendation made by the CTG that two further exemptions should be added to the current list of exempt transactions: one for remuneration paid to an employee on an arm's length basis and the other for financial assistance provided by the charity to the donor that takes the form of a charitable grant made in the course of one of the charity's primary charitable purposes;
13. We also support the CTG view that there are a number of other areas where the exemptions are too restrictive and innocent transactions are penalised. We agree with their recommendations that the exemptions must be extended to take out all innocent transactions and/or an avoidance/motive test should be introduced (see our paragraph 6 above). The alternative would be for a number of detailed changes to be made to individual sections, as set out in the CTG submission.

Chapter 3: De minimis limits

What proportion of charity donors make donations of less than £1,000 per charity, per year?

Would the proposed limit of 'ignored' donations to a charity of £1,000 help charities in reducing their administration costs around the substantial donor rules? If so, what do charities anticipate that the level of their savings will be? Is the proposed limit of £1,000 set appropriately? What would be the associated savings and costs to charities of an alternative limit?

14. We do not consider that 'ignoring' donations that did not exceed £1,000 would help charities to reduce their administrative costs around the substantial donor rules. Charities would have to maintain records of all small donations for many years in order to identify which donations fell below the £1,000 limit and to enable them to aggregate more than one donation by a single donor or donations by connected parties.
15. It is not clear for how long records would have to be maintained. Under the existing legislation there is a need to maintain records for 18 years (6 years before, 6 years after and the period of 6 years when the substantial donation was made). The changes proposed in the consultation document appear to have the effect of reducing the period to 12 years but this may not be the case. The fact that leading professionals in the field are not clear as to the intended length of the period is another indication of the problems with this legislation.

Chapter 4: Disregarding small benefits or payments

Would the proposed de minimis limit for small benefits or payments be welcomed by charities?

How many donors will this affect?

What would be the likely quantified savings to charities of introducing the proposed de minimis limit? Are there likely to be any other benefits or costs?

Is the proposed limit of £500 set appropriately? What would be the associated savings and costs to charities of an alternative de minimis limit for small payments and benefits?

16. Even if the principle of a de minimis limit were appropriate, the proposed limit is set too low to make any significant difference to charities. There is already an exemption in the legislation for benefits provided to gift aid donors which fall below the £500 gift aid benefit limit, so the proposal in the Consultation Document would only extend the exemption to donations that were not made under gift aid.

17. As we have stated in our paragraph 6 above, the legislation needs to be changed so that only transactions in favour of donors that are arranged with a view to tax avoidance, or that are at a value which disadvantages the charity, are treated as non-charitable expenditure and therefore penalised. Setting a de minimis limit does not correct what is wrong in principle and does little if anything to mitigate the risks of a tax liability arising on entirely innocent transactions that a charity may carry out with a substantial donor or connected person.

Chapter 5: Revised thresholds for substantial donors

Would the proposed revised thresholds for defining a substantial donor be welcomed by charities?

What are the current administration costs to charities of monitoring donations under the existing substantial donor definition (relievable gifts to a charity of at least £25,000 in a period of 12 months, or of at least £100,000 in a period of 6 years)?

Would the proposed revisions to the thresholds for defining a substantial donor (to relievable gifts to a charity of at least £50,000 in a period of 12 months, or of at least £125,000 in a period of 3 years) reduce administration costs for charities? If so, what is the value of the savings that charities expect?

Where charities have identified significant administration costs are these predominately from monitoring individuals? Do charities consider there to be any significant costs from monitoring corporate donors?

Are there alternative limits or measures that charities would prefer to see put in place for defining substantial donors? What would be the benefit and cost implications to charities of these alternatives?

18. We agree with CTG that it would be more sensible to define substantial donors according to the size of the recipient charities, i.e. that 'substantial' should be defined in relation to the income of the charity excluding the donation or donations, subject to a de minimis of £50,000 for charities of any size.
19. We welcome the suggested reduction of the period for monitoring relievable gifts from 6 years to 3 years, but we are concerned that the anti avoidance provisions would still operate to catch transactions that were made in the three year period before the donation. We therefore support the CTG recommendation that subsection 506A (2) (b) be deleted, so taking the six year period out of the legislation. If a three year period is to be included, on top of the automatic 5 year extension, we recommend that it should only operate from the date the donation is made, and that the period for casting back to previous transactions should be only 12 months for any donation. Furthermore, we recommend that a person should only become a substantial donor in relation to donations made after 22 March 2006.

Chapter 6: Date of proposed legislation taking effect

20. We agree with the proposal that the revised legislation should have effect in relation to transactions on or after 22 March 2006.

Email: caron.bradshaw@icaew.com

© The Institute of Chartered Accountants in England and Wales 2008

All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is reproduced accurately and not used in a misleading context;
- the source of the extract or document, and the copyright of The Institute of Chartered Accountants in England and Wales, is acknowledged; and
- the title of the document and the reference number (ICAEW Rep 117/08) are quoted.

Where third-party copyright material has been identified application for permission must be made to the copyright holder.

www.icaew.com