

TAXREP 13/00

GETTING BRITAIN GIVING

Memorandum submitted in March 2000 by the Tax Faculty of the Institute of Chartered Accountants in response to a consultation document issued in February 2000

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ANNEX

GETTING BRITAIN GIVING

1 We refer to the press release issued on 21 February 2000 and welcome the opportunity to comment.

General comments

Consultation proposals

2 In our response to the consultation exercise announced in the 1999 Budget (issued as TAXREP 24/99, a further copy of which is attached), we welcomed the Government's proposals to encourage charitable giving, but we were concerned that much more could be done to encourage charitable giving by all taxpayers.

3 Whilst the proposals outlined in this consultation exercise should help to go some way to encourage charitable giving, we think that much more needs to be done if all taxpayers are to be encouraged to give to charity. The proposals are little different to the existing Gift Aid rules, and we believe that a radical rethink is required to achieve the Government's objective.

Time allowed for response to consultation

4 Whilst we appreciate the short timescale before the Budget, issuing this substantial amount of documentation on 21 February and requesting responses by 10 March is much too short a period to allow for considered responses. In view of the importance of this consultation to the voluntary sector, we would have thought that a consultation period of at least a month and preferably longer would have been reasonable. The review process has also been hindered by the considerable number of files that had to be downloaded. We would have thought it much more sensible to consolidate most if not all of the files into one document, thereby easing the burden on those who had to review the draft documentation.

Specific comments

Deeds of covenant and trustees

5 It is proposed that new deeds of covenant will be phased out in favour of a revised Gift Aid scheme. However, not all taxpayers can make Gift Aid payments. Under the deed of covenant rules, trustees are able to make tax-efficient gifts out of taxable income. However this will not be possible under the Gift Aid rules, because gifts must be made by individuals. The rules should be amended so that when deeds of covenants are abolished, trustees can make charitable donations under the new Gift Aid rules.

Deeds of covenant v Gift Aid: benefits

- 6 The donor benefit rules set out in draft clause 1(5) will discourage smaller membership subscriptions being switched from a deed of covenant to Gift Aid. Under current rules, for example, a donor who gives £200 by way of a deed of covenant can receive a benefit of up to £50 (i.e. 25% of the subscription – see Inland Revenue press release dated 20 March 1990). Under these draft rules, however, the maximum allowable benefit imposed by clause 5B will be £25. In order to encourage a switch from deeds of covenant to the new Gift Aid rules, we suggest that the limit on benefits received should be set at a maximum of 25% of the subscription, subject to an overall maximum benefit (as set out in draft clause 5B(d)) of £250.

Gifts of shares and securities to charities etc

- 7 We would be grateful for confirmation that shares listed on a recognised stock exchange will include units in authorised unit trusts and other similar collective investment vehicles.

Guidance notes

Existing covenants

- 8 The guidance found in paragraphs 4.1 and 4.2 relating to the transitional period for existing covenants is confusing and should be made clearer. It needs to be made clear that:
- new deeds of covenant can still be made after 5 April 2000, but these will be dealt with under the new Gift Aid rules; and
 - payments made after 5 April 2000 under deeds of covenant effected on or before that date will still be subject to the old rules.

Signature

- 9 It appears that neither an oral nor an internet donation (see paragraph 4.13) require a signature in order to be effective. If this is so, why is it still necessary for faxed or posted donations to require a signature?

Record-keeping

- 10 Paragraph 4.35 of the guidance notes sets out suggested lengths of time for keeping records for charitable trusts. However, the guidance is confusing. Further, it deals only with charitable trusts and charitable companies (see paragraph 4.36) and does not cover unincorporated associations. We would suggest that the record-keeping requirements for the various types of charitable organisations be brought more closely into line.

Right to cancellation

- 11 If a donation is made orally, there is a right to cancel within 30 days after the donor has been sent a written record. This provision is inconsistent with the cancellation provisions for written/fax/internet donations and we would be grateful for clarification as to why this provision is considered necessary.

Donations by companies

- 12 We are concerned that the introduction of gross charitable donations by companies may lead to a reduction in the total amount of charitable total giving by companies. Charities will have to put more effort into persuading companies that because the gift is now paid gross rather than net of income tax, the company must give more to the charity if the charity is to receive the same amount as previously. We suspect that few charities will have the resources to undertake this work.

Charitable trading

- 13 We welcome the proposed relaxations and guidance on charitable trading. However, we suspect that ‘the reasonable expectation’ test set out in paragraphs 8.8 and 8.9 will lead to considerable problems for charities and possibly increased costs of compliance.

Model Gift Aid Declaration

- 14 The model form included as an appendix to the guidance notes should be reduced to a single side of A4 and should be designed so that taxpayers need only to ‘tick the box’ rather than have to delete statements that do not apply.
- 15 If you wish to discuss these points further, please let us know. We would also welcome feedback on the results of this consultation.

13 March 2000
14-5-97
FJH/AM

REVIEW OF CHARITY TAXATION

1 We refer to the above consultation document issued on 9 March 1999.

GENERAL COMMENTS

- 2 We have no particular expertise on the overriding question of how people could be encouraged to give more to charity, and we suspect that many of the more detailed questions are best answered by the charities themselves on the basis of their own experience. Most of our comments are directed towards the questions on administrative simplification. Nevertheless, as chartered accountants we have a public interest role in addition to advising both charities and donors. Therefore, where appropriate, we have considered the wider issues that arise.
- 3 We have set out our comments on the document below. For clarity, our comments on the 'Points for consideration' are set out in *italics*. Our major concern is that the Consultation document does not address properly the fundamental problem, namely that the UK tax system provides tax relief only for the minority of gifts made to charity, and much more could be done to encourage charitable giving by all taxpayers.

CHAPTER 1 INTRODUCTION

Government's relationship with charities

- 4 The Consultation Document states that the amount of tax relief that the Government provides to charities is currently estimated at £2 billion each year. However, we understand that there are real concerns expressed by charities that the trend in Government policy for some time has been to reduce the amount of this support. Specifically, we understand that charities have found their income levels reduced in the following ways:
- the amount of irrecoverable VAT that they pay has risen progressively to some £500 million;
 - the decision to abolish repayments of tax credits on dividends will reduce their investment income by a further £400 million over time; and
 - their share of the proceeds of the National Lottery has been reduced.
- 5 All these changes have occurred at a time when charities appear to be being encouraged to take responsibility for services that were previously delivered by local and central Government. Further, the burden of employment costs is steadily rising. In the longer term, charities also face a threat in the form of EC proposals to reduce or abolish VAT

exemptions and reduced rates as part of the programme to create a definitive system of VAT throughout the EU. Moreover, existing zero rate derogations depend wholly upon the maintenance of the veto. How long will this survive against the proposal for a lower reduced rate for social purposes?

- 6 Not only has Government reduced the resources that would otherwise be available to the sector through the tax system, it has also introduced the National Lottery. The Lottery is an alternative attraction to charitable giving. It is a way for individuals to give part of their disposable income that they might have otherwise given to charity. We consider this further in paragraphs 9 and 10 below.
- 7 Against this background, it seems to us that unless charitable giving can be further encouraged, charities will not be able to meet their existing programmes let alone any additional responsibilities. We are very concerned at this development.
- 8 Charities are also important employers in their own right, particularly amongst the disadvantaged. On average 66p out of every £1 in state aid provided to charities is spent on employment, some of which will be returned by way of taxes. This proportion is unlikely to change radically, because charity work can usually only be effective where it is delivered on a personal basis.

Trends in giving to charity

- 9 The Consultation Document makes no mention of the influence of Government action on attitudes to private giving. We find this surprising, as we would have thought that the introduction of the National Lottery might have had a profound effect on private giving. While the Lottery has not necessarily reduced the total resources of the charity sector, it will have led to a redistribution of income within the sector in favour of Government controlled activities.
- 10 Further, it must have reduced the individual giving levels of lottery players, and we suspect that this is especially true among those on lower incomes and also the young, at whom many of these proposed incentives are aimed. We would have thought that a comprehensive review of this nature should have addressed the impact of this fundamental change. There must be a real risk that the mere offering of further tax incentives for charitable giving may not be enough, given the possible fundamental shift in attitudes to charitable giving as a result of the Lottery.

The Consultation Document

- 11 The document states that over 3,000 responses were received in the first stage of the review. We suspect that a great deal of valuable work has been carried out both by those preparing the responses and the civil servants responsible for analysing the ideas and suggestions. It would be helpful to the many who commented if any factual analysis that may have been prepared were published. We appreciate that under the Code of Practice

on consultations, such an analysis may be provided on request, but we suspect that few charities are aware of this procedure.

CHAPTER 2 SUPPORTING GIVING BY INDIVIDUALS

General comments

- 12 Many people are undoubtedly confused by the fact that there are currently four tax-favoured ways of giving for individuals. It would therefore be sensible to merge Gift Aid and Millennium Gift Aid, as proposed in paragraph 2.14 of the consultation document. However, beyond that there may only be limited scope for reducing the actual number of schemes, since each serves a particular purpose.
- 13 It appears that the Government intends to leave the current provisions on Deeds of Covenant unchanged. We expect that charities themselves will be reluctant to forego the assured income stream which comes from the Deed of Covenant route. It is important that the option to use covenants should remain in place for the benefit of those charities (notably religious charities) that derive a significant part of their income in this form. If the Government is contemplating that covenanted giving will be abolished at a future date, it should provide for a transitional period for donors and charities to adjust their giving and fund-raising practices.
- 14 The approach should therefore be to simplify as far as possible the administrative requirements. Many individuals undoubtedly find the Deed of Covenant scheme daunting, not just because of the long-term commitment but also because of the formality of the documentation. Since relief is now allowed under Gift Aid for single payments there is no overwhelming need from the Revenue's perspective to retain the rule that a covenant must be legally enforceable. The removal of that rule would also make it unnecessary for the covenant to be formally signed and witnessed as a deed. Evidently the charities still see a need for a scheme which requires long-term committed giving. However, since they would have been unlikely in any case to enforce a Deed of Covenant against a defaulting donor, it should be possible to achieve the same result through a system of non-binding undertakings which would require much less formality.

Improving Deeds of Covenant and Gift Aid

Paragraph 2.16

- 15 There seems no particular reason in principle why a gift needs to be a minimum amount before it can qualify for Gift Aid. However, it may make sense to set a limit, so as to avoid the administrative expense of processing very small claims.
- 16 **Points for consideration**
- (i) *If the tax system is to be effective in broadening the donor base to include in particular the young and the lower paid, it would appear desirable to reduce the minimum limit for Gift Aid to £100, the same limit as for Millennium Gift Aid.*

- (ii) *Even so, there may be a case for reducing the limit further, say down to £50 or even lower. Ultimately, however, it must be for the charities to express a view as to what would be the smallest amount for which they would think it worthwhile to process a tax claim.*

Recent changes in income tax rates have made it more difficult for charities to explain to donors how tax-effective giving works, particularly if the donor is paying tax at the 10 per cent or 20 per cent rates. There is also the related issue which, surprisingly, the document does not mention but which is a real practical problem, namely the taxpayer who has insufficient income chargeable at the basic rate to cover his charitable donations. Such a taxpayer is obliged to account to the Revenue for part of the tax deducted at source. This has potentially been a problem since the introduction of the 20 per cent lower rate, and undoubtedly many small liabilities must have been overlooked. However, charities cannot assure donors that the Revenue will not try to collect tax from them if they do not have sufficient income taxable at the basic rate to cover the gift, thus discouraging the donor from making a gift. The introduction of the 10 per cent starting rate will increase the problem.

We think that this problem now needs to be addressed. One solution is to allow basic rate income tax relief for all donors, in effect by waiving the right to seek a payment of the excess tax withheld.

We have highlighted this point previously, notably in our representations on the 1999 Finance Bill (paragraph 26, TAXREP 9/99), but we have met with little success. Such a move would simplify the affairs of a group of taxpayers who are generous to charities despite having only modest incomes, and the total amount of tax at stake cannot be large.

Other options for improving Gift Aid

Paragraph 2.17

- 17 The Document suggests that the certification requirements for Gift Aid might be simplified. This strikes us as a sensible suggestion.

Paragraph 2.19

- 18 We are inclined to agree with the conclusion not to take this idea forward. This suggestion would require charities to reappraise their donor marketing strategies and overhaul their existing donor literature: a substantial investment of resources for a return that is at best uncertain.

Paragraph 2.20

- 19 We do not see any good reason for extending the relief only to UK diplomats and people in the armed forces serving overseas. If the relief is to be extended, it should be made available to all non-UK residents with sufficient UK source income; it is an anomaly that

such donors can currently obtain UK tax relief only if the gift takes the form of a covenant.

20 *Points for consideration*

- (iii) *Making a gift over the Internet is more likely to appeal to younger taxpayers and be less attractive to, say, pensioners. However, the popularity of the Internet is likely to increase with all generations over the next few years. Making gifts by telephone is likely to be popular with all ages, and will mirror the Revenue's plans to encourage taxpayers to settle their tax bills over the telephone. It should enable telethon fund-raisers to offer tax-effective giving to their whole audience. The ideas appear worth exploring, provided that claims do not need to be paper based and that any lower limit is set at a modest level. If all taxpayers are to encouraged to make donations, the level must be much lower than £100.*
- (iv) *It is difficult to know whether reminding taxpayers about Gift Aid with their tax returns would stimulate further giving, but it seems to be a low-cost option which must be worth trying. We understand that Hungary recently introduced a similar scheme with good results. However, if the reminder appears only on tax returns, its appeal will be limited to only those who receive a tax return, which broadly will be higher rate taxpayers. To reach other taxpayers, a reminder needs to be added to other standard documents that they are likely to read, such as pension statements or P60 forms.*
- (v) *We are less convinced about the idea of allowing a one-year carry-back of Gift Aid relief, although it has some attractions. If it follows the usual self-assessment pattern of a relief calculated at the tax rate for year one but allowed as a deduction from tax payable for year two, we suspect that it would be over-complicated, and of very limited incentive effect. If it is given as a true carry-back it could probably only be fitted into self-assessment by being claimed in the year one return (which appears to be what the document implies), but that would operate capriciously according to when the gift is made during the year, and could even operate as a perverse incentive to delay filing the return. However, this conflicts with the point already made above: taxpayers might feel aggrieved if they were reminded (as in point (iv)) that they could make a tax effective gift, only to find that they cannot claim the tax relief on the form for the year in question. We suspect that many taxpayers would claim relief in error. A possible compromise might be to allow claims up to 30 September following the end of the income tax year, ie. the deadline for submission of the return if a taxpayer wishes the Revenue to calculate the tax.*

A US-style relief for giving

- 21 The UK system is much more restrictive in allowing tax relief for charitable donations. Currently, only about 20% of charitable donations qualify for tax relief, whereas in the US we understand that it is much higher, perhaps 90% or more. The reason for this difference is that the US system is much more flexible and appeals to all taxpayers.

- 22 In effect, a US taxpayer can obtain tax relief by itemising all payments made to charity on his tax return. The taxpayer will need to keep the receipts in the event that his tax return is audited. Thus, tax relief will be obtained by the taxpayer for all charitable donations, subject to limits, and no tax relief can be reclaimed by the charity. An additional attraction of the US system is that the category of gifts that can qualify for tax relief is broad, for example gifts in kind can qualify, with the major exception that no relief is available for the value of any voluntary work supplied.
- 23 The UK tax system for charitable giving is not only complicated but, with the exception of payroll giving, it only really encourages tax-effective giving by, broadly, higher rate taxpayers who are able to make substantial donations. Put another way, the UK tax system discriminates against tax-effective giving by the less well-off. In our view, this is the crux of the problem and, unless this is addressed, any further measures to encourage charitable giving will have only limited success.
- 24 For example, very few taxpayers will have the resources to make a single gift of £250 under Gift Aid. Even a gift of £100 under Millennium Gift Aid is still beyond the resources of most taxpayers. The majority of taxpayers are likely to make donations of modest amounts, say £10 to £20 and at most £50, to a number of charities throughout the year. This is by far the most common method of charitable giving.
- 25 If the tax system is to be used to encourage further charitable giving, this type of giving must be encouraged. Therefore, the tax reliefs must be extended to provide relief for all charitable donations, of whatever amount, made by all taxpayers.
- 26 The two particular problems with importing the US system to the UK are that:
- i) because charities would not be able to reclaim any tax relief, they would see their income reduced if they were not be able to persuade taxpayers to make ‘gross’ gifts; and
 - ii) under the UK tax system, the majority of taxpayers are under PAYE and do not receive a tax return, thus providing no ready means to reclaim the tax relief.
- 27 The first of these could be overcome in part by offering the US-style relief as an alternative to the current schemes. It is of course possible that some taxpayers might switch from, say, Gift Aid to the US-style relief without increasing their donation to the ‘gross’ amount. However, if the new scheme also encouraged new charitable giving, an increased level of donations may offset the possible loss of such income.
- 28 We appreciate that the second problem is more difficult to address, as taxpayers who wish to claim tax relief will need to be sent tax returns or an annual coding adjustment will be needed.

29 Points for consideration

- (vi) *It is doubtful whether it is possible to reproduce in the UK the amount raised in the US just by adopting the US rules. Ignoring the differences in cultural attitudes to giving, it is not just the procedure for giving in the US but also the relief for gifts in kind as well as cash that accounts for the amounts raised from individuals. The US experience also suggests that certain sectors (e.g. religion) would benefit more than others under this system.*
- (vii) *On balance there does not appear to be a downside in trying the US method, provided that it is offered as an additional option rather than replacing an existing method. We would be happy to consider proposals in this area further in due course.*

Payroll giving

30 In principle, the proposal to raise the limit on gifts that can be made under this scheme from £1,200 to £6,000 appears sensible, and we do not object to the proposed lifting of the limit entirely. However, given the limited take-up under the scheme as it stands, we think it is reasonable to query whether even so there will be many taxpayers who will take advantage of the scheme.

31 Points for consideration

- (viii) *This is most likely to appeal to larger employers and higher earners. We are unclear as to what additional compliance rules would be required to counter the alleged risk of abuse, and would be grateful for clarification. However we cannot comment on whether the increased limit would be worthwhile if 'new compliance rules' have to be introduced, when we have no idea what those rules might be.*
- (ix) *In principle this appears a reasonable proposal. Both charities and employers are likely to consider this from a resource viewpoint, particularly a small charity or a small employer who will tend to want to minimise the amount of administrative work involved. It will therefore be important to take into account the views of charities regarding this proposal.*
- (x) *Effective marketing of payroll giving requires co-operation between employers and charities. It will also be important to involve (i) payroll agencies, as this function is increasingly being outsourced, (ii) umbrella organisations to reach smaller charities and employers, and (iii) pension funds to reach pensioners in occupational schemes. Ideally, all parties would be involved in a joint campaign from the outset.*
- (xi) *This suggestion is an interesting proposal. The transitional supplement is more likely to appeal to charities and donors than to employers, as it will involve some administrative effort by employers.*

We think that payroll giving would be encouraged further if payroll contributions were exempted from employers' and employees' Class One National Insurance Contributions. Such payments could then be treated in the same way as, for example, employee pension contributions. Thus, the payroll giving contribution would be deducted from gross salary before calculating National Insurance Contributions. This should help to reduce the administration as it would simplify the payroll calculations. This is particularly important if small employers are to be attracted to the scheme.

One-off small donations through street collections, telethons, etc

Paragraphs 2.39 & 2.40

- 32 Of course many (particularly religious) charities organise regular fund-raising appeals that include the use of 'envelope giving' to collect small cash gifts. These often raise funds from lower paid donors, and are usually structured as a Deed of Covenant.
- 33 If a US-style tax relief for charitable contributions was introduced, as discussed above, this should enable taxpayers to claim tax relief for one-off small donations made outside the Deed of Covenant route.

Gifts of assets

Paragraph 2.42

- 34 We refer to the comments made above concerning the possible introduction of US-style tax reliefs, which allow for gifts in kind by individuals. We note that the Document rejects this idea because of 'real difficulties in arriving at objective valuations'. We would point out that it is not always that difficult to arrive at an objective valuation. For example, if a taxpayer made a gift to a charity of quoted shares, the market value of the shares will be straightforward to calculate. In this case, we see no reason to deny tax relief.
- 35 We agree that in other cases, for example, a gift of private company shares, the determination of market value is more difficult. However, the valuation of assets for tax purposes has always been an important part of the tax system, and the techniques and procedures which need to be adopted are well known and understood.
- 36 We understand that tax relief for gifts in kind is one of the features of the US system that has proved to be a success. The fact that there may sometimes be problems of valuation and that anti-abuse measures may be required are not convincing reasons to reject entirely any form of relief for gifts in kind by individuals.
- 37 In our view, tax relief should not be limited to gifts of trading stock and equipment by businesses. We would welcome an extension of tax relief for gifts in kind so as to include gifts made by individuals.

CHAPTER 3 SUPPORTING GIVING BY COMPANIES AND OTHER BUSINESSES

Deeds of Covenant and Gift Aid

Paragraph 3.7

- 38 The particular avoidance schemes which led to the introduction of the requirement for corporate donors to withhold basic rate income tax from their donations involved arrangements for donors to control the use of the money instead of applying it to charitable purposes. The withholding requirement has proved to be a particular obstacle for companies willing to donate blocked funds (bank accounts subject to foreign government exchange control laws); because tax cannot be withheld out of blocked funds the donor has to find additional cash to pay the withholding tax. In these cases, it is absolutely clear that control of the use of the money lies with the foreign Government not the donor, so that there is no scope for abuse. This is supported by evidence from the US, where the law was changed specifically, and successfully, to encourage donations of blocked funds. UK law should be amended to allow 'gross' donations of blocked funds.

Gifts in kind

Paragraph 3.13

- 39 The comments above in relation to gifts in kind by individuals apply equally here. It is difficult to see why the Government should be willing to concede relief for business gifts in the case of certain categories of assets but not for others. The risk of abuse is again cited as a reason for granting no relief, yet it is difficult to believe that the tax systems in other countries can cope but apparently the UK cannot.

CHAPTER 4 SUPPORTING CHARITY BUSINESSES - DIRECT TAX

General comments

- 40 For charity businesses the main issue is again one of administrative simplification.
- 41 The reasons why charities frequently use a subsidiary to trade are not primarily because of UK tax law. They are because UK charity laws do not allow a charity to:
- (i) trade directly unless the trade is incidental to the charity's objects; and
 - (ii) risk its assets in a trading venture.
- 42 The Document notes that charities can in practice always avoid paying tax on any business income, by means of the subsidiary company route. However, it rejects the proposal to save them the trouble of doing this by giving them a more extensive

exemption for their own trading income. The reason given for this is that, as noted above, charity law places limits on a charity's ability to carry on trading activities, and the tax system for charities has to reflect this.

- 43 For the reasons mentioned above, larger charities will invariably be required to trade through a separate subsidiary. For smaller charities, the position may be somewhat different. The boundary between what may be regarded as one-off fundraising and what may be trading is not always easy to decide. Since charity law imposes its own restrictions, there appears to be no reason why any trading income should not be exempt from tax: the charity law restriction will ensure that any tax exemption for trading income cannot be abused. An extended tax exemption should be of most help to smaller charities with small amounts of trading income.
- 44 The other major consideration is whether or not an exemption from tax for trading income allows charities to compete unfairly with small commercial businesses. As a charity can in any event enjoy an exemption from tax for trading income if it adopts the subsidiary company route, the widening of the tax exemption to include trading income is unlikely to exacerbate this potential problem. We do not think that this issue should be used as a reason to preclude charities from enjoying an unrestricted tax exemption on trading income.
- 45 A tax-exempt charity will be at an advantage as compared with a taxable business if both were aiming to make the same post-tax profit, but that is not the case. The charity may indeed have the advantage if, in a particular case, it does not feel the need to maximise profits (e.g. because the trading activity is related to its charitable objects – in which case if the charity trades itself it may avail itself of the specific exemption available to charities) or that it can cut its margins to the detriment of competition, but these are separate problems from the issue of taxability.
- 46 We are not convinced that charities (or their subsidiaries) which trade are normally in direct competition to non-charitable traders. One notable exception is in the selling of Christmas cards. However, the success of charity cards owes more to charities encouraging people to support charities at Christmas time by buying cards. Their success is not due to competing on price.
- 47 Clearly a balance needs to be struck. We think the current balance is about right and, by and large, is acceptable to non-charitable traders.
- 48 For the reasons already mentioned, many charities will always need to trade through a separate subsidiary company. For these companies, we welcome the proposal to calculate Gift Aid payments retrospectively, as described in paragraph 4.17.

Improving the direct tax system for charity businesses

Paragraph 4.12

49 A significant compliance matter not addressed in the Consultation Document is the new requirement introduced by Corporation Tax Self Assessment (CTSA) to complete form CT 600E. Conventional charity accounts do not produce the analysis necessary to complete the form; in particular it appears that additional work is needed to apportion reported costs to fit the boxes on the form. Given that charities qualify for exemption from tax it is not clear why all charities should have to provide this extra information. If they are expected to complete this, then it is important to ensure that disclosure under CTSA is consistent with that required under the charity accounting standards.

50 *Points for consideration*

(xii) *We refer to our general comments made above. Ideally, charities would be free to undertake most forms of fund-raising in the name of the charity. As matters stand, the Charity Commission is generally willing to accept occasional fundraising events organised by the charity itself, which is broadly consistent with the Revenue's application of ESC C4. It appears reasonable to exempt any trading income from tax, as in any event if a charity intends to trade substantially it would still have to use a subsidiary. Moreover, whatever position the Charity Commission takes on this question, its view is limited to charities in England and Wales. The position of the authorities in Scotland and Northern Ireland also needs to be clarified.*

(xiii) *There is a good case for using the VAT threshold as a limit for a direct tax exemption. However, it is often not clear to what extent grants are treated as taxable income. We therefore suggest that grants should be omitted from counting towards this limit.*

Making things easier for charities with subsidiary companies

51 *Points for consideration*

(xiv) *Carrying back Gift Aid would certainly reduce compliance costs. But to assist charity subsidiaries to build up working capital this needs to be coupled with a more flexible method of obtaining approval to reinvest funds in the subsidiary. The current wording of the statute could be changed to allow the Revenue to issue binding advance rulings on both initial and subsequent investments in charity subsidiaries for specified purposes and periods of time. Ideally, this procedure should be co-ordinated with those of the Charity Commission to maximise the benefit to charities.*

CHAPTER 5

SUPPORTING CHARITY BUSINESSES AND ACTIVITIES - VAT AND BUSINESS RATE RELIEF

- 52 We support any moves that would align the rules for both direct and indirect tax, provided that the moves are designed to reduce administration and complexity and not the other way around.

Keeping VAT rules and reliefs up-to-date

53 *Points for consideration*

- (xv) *To reduce compliance costs for charities, the most effective step would be to co-ordinate guidance from local VAT offices on difficult and emerging issues. Possibly, the most significant single source of difficulty is the VAT status of grants, on which almost all charities rely at some stage of their existence. Given that the vast majority of grants originate from the EU, central and local government, it should be possible for Customs to develop a framework for gathering the necessary information and providing clear and consistent guidance on which grants are taxable and in what circumstances.*

Reforming the VAT and direct tax treatment of fund-raising events

54 *Points for consideration*

- (xvi) *Some charities want their events to be exempt and others want them to be taxable. Charities should have the option to tax, rather than having one rule for all. The difficulty, of course, is that the Sixth Directive does not allow the charity to waive its exemption. Only by making itself taxable is there a way of reclaiming input tax. There are ways that this problem can be mitigated, for example it may be possible for an exempt charity to achieve taxable status by the use of a subsidiary company to organise an event which would be exempt if organised by a charity, but this is not a straightforward solution.*

Ideally the Government should lead a lobby in Brussels to change EU directives in favour of charity friendly measures, and specifically to amend the Sixth Directive to allow charities the option to tax. If it is not possible to amend the Sixth Directive, then the existing rules should be re-examined to identify whether they can be made more flexible.

(xvii/

- xviii) *There are problems with competitions involving an element of skill (currently standard rated regardless of the level of skill required). Charities have difficulty recognising that a problem exists both when the competition is the fundraising event and when it is just one event within a larger series.*

Membership benefits

55 *Points for consideration*

- (xix) *If charities provide membership benefits, their charitable status may be prejudiced. In practice, of course, some 'nominal' benefits may be provided, such as newsletters/journals, followed by small gifts (pens, badges etc) but the dividing line as to what is acceptable and what is not is far from clear. In view of this uncertainty, many charities do not provide any benefits, although it may assist*

them in their work if they did so. It would be helpful to have a clear set of rules as to what is de minimis and what is not.

- (xx) *The comments above concerning fund-raising events are also relevant to membership benefits - exemption will not be beneficial to all charities and many will prefer a flexible approach that allows them to tax subscriptions if it is to their advantage.*

Charity advertising

56 Points for consideration

(xxi) *We do not see why the form of the advertising should affect the entitlement to the relief.*

(xxii) *Logically, you should ask the advertising industry how best to define advertising. If the Government is unhappy with this, the law should at least enable new forms of advertising to be added by secondary legislation without requiring Parliament to change the law.*

(xxiii) *For smaller charities we suspect that this varies considerably according to their staff requirements, and when they organise a fund-raising initiative.*

(xxiv) *We suspect that Internet advertising will increase substantially over the next few years, given the rise in subscription free Internet Service Providers.*

VAT De-registration

Paragraph 5.29

57 In the case of the transfer of a charity subsidiary's business back to the parent charity, there is a case for exempting the transfer from the deregistration clawback to the extent that the assets continue to be used by the charity for business activities.

58 *Points for consideration*

(xxv) *The rule would be more straightforward to understand and apply if it was calculated by reference to the value of the goods. We think that the limit should be by reference to a readily identifiable total value. We suggest a figure of £5,000, which is equal to a limit of £875. The £5,000 figure should then be highlighted in any explanatory material rather than the VAT amount.*

Charity businesses and Business rate

59 *Points for consideration*

(xxvi) *The existing guidance on what constitutes 'wholly or mainly concerned' need to be more widely publicised and consistently applied across the country.*

(xxvii) *The current tests seem relatively simple. If local authorities are having difficulty applying them, this suggests that more complex tests would not be welcome.*

CHAPTER 6

SIMPLIFYING THE TAX SYSTEM FOR CHARITIES

Improving the service

60 *Points for consideration*

(xxviii) *It would be helpful if tax officers had a better understanding of charity work and charity law. In our experience, perhaps because of its involvement in the charity registration process, the Inland Revenue has a better understanding of charity law than Customs and Excise. Nevertheless, this tends to focus on what is charitable rather than what charities can do in their own names and when they have to use a separate company. There is a case for a programme to second officers from the Revenue and Customs to work in charities for short periods.*

(xxix) *Apart from producing joint publications, there needs to be a regular liaison between the two departments on charity issues via designated staff. Such staff should have responsibility for providing co-ordinated guidance on difficult and emerging tax issues. It would be helpful if Customs followed the example set by the Inland Revenue's FICO office by setting up a department with specific responsibility for the charity sector and which has the capacity to deal directly with charity queries. It is not clear whether the proposed helpline service will go this far. Charities need to be able to obtain specific rulings on difficult and emerging issues; the benefit of the helpline will be diluted unless the helpline has the authority and resources to do this.*

Charity workers

61 *Points for consideration*

(xxx) *If a de minimis approach is acceptable in other areas raised in the consultation document, it must be worth considering extending it to cover the reimbursement of expenses incurred by volunteers. Many people are willing to give their time to help a charity, but they may not have sufficient income not to claim for out-of-pocket expenses. Where a charity makes a genuine attempt to pay reasonable expenses to volunteers which are properly supported, there should be no question that such payments might be subject to income tax and PAYE. We think it must also be possible to fix an amount which can be assumed to be paid without any element of profit to the volunteer, an example being the allowable rates for volunteer drivers.*

It would also be helpful if there was greater co-ordination with the social security department regarding payments to volunteers that can be made without adverse consequences. Many people who are entitled to benefits through disability or

unemployment can make a useful contribution to society as charity volunteers without necessarily being sufficiently skilled to have an immediate prospect of gaining full-time employment. Benefit rules that assume that volunteering for charitable work is evidence of employability, thus reducing benefit entitlement, will limit the scope for the socially excluded to play a full part in society.

CONCLUSIONS

62 We believe that it is vital that the UK tax rules should be such as to encourage charities to thrive, as this will benefit society as a whole.

63 We believe that the Government should take further steps, along the lines set out in this Consultation Document, to encourage charitable giving and reduce the burdens on charities.

64 However, as mentioned in paragraph 3, we think that the Consultation does not address properly the fundamental problem; namely that the UK tax system provides tax relief only for the minority of gifts made to charity, and much more could be done to encourage charitable giving by all taxpayers.

65 We think that the UK should learn from the US-style approach to tax relief for charitable giving. The US system adopts a much more flexible approach to tax relief for charitable giving and, unlike the UK system, provides tax relief for the majority of charitable gifts. As a result, the US system appears much more successful in encouraging charitable giving.

65 We should be happy to provide any further information on the points raised in this representation.