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Charities Focus

Pension deficits – Doom for charities?

Another high profile charity, the Spirit of Enniskillen Trust, has gone into administration as a result of its increasing pension liabilities.

This has once again highlighted the risks charities face in relation to obligations in respect of their participation in defined benefit pension schemes. The problem is especially worrying for trustees of unincorporated charities, as was the case for the Enniskillen trustees, since the charity's liability is not limited and the trustees are therefore potentially liable for the whole of the debts of the charity, including the pensions debt.

The problem arises in multi-employer schemes, where several charities participate in one pension scheme. Under current pensions legislation, the liability of an employer to the scheme must be repaid in full when that employer leaves a scheme which is in deficit.

There will often not be sufficient assets in the charity to repay the debt it owes to the pension scheme. In the case of Enniskillen, the debt due to the pension scheme, which is run by the Pensions Trust, is some £250,000 – and the only asset of the charity is a property worth £100,000.

Because the scheme is a "last-man standing" scheme, the remaining employers in the scheme take on the debt of a departing employer that cannot pay off its deficit. This can be a further problem, potentially leaving the last employer in the scheme with debts disproportional to its own involvement in the scheme.

The current debt on employer legislation creates a dilemma for charities – they often cannot afford to leave the scheme due to the large debt that would become payable, and so the alternative is to remain in the scheme and continue to contribute, resulting in its liabilities continuing to increase.

The problem of dealing with deficits is made worse for charities as they do not have shareholders that could be called upon to contribute towards the deficit, nor will they necessarily have profits to utilise in this way.

The government has at least recognised the problem, with a recent announcement from Steve Webb, the pensions minister, suggesting that the government would carry out a study of "how the current processes relating to employer debt that cause difficulties for charities and others participating in multi-employer schemes could be improved."

Charities could take steps to limit their liability, perhaps by switching to a defined contribution scheme or implementing salary sacrifice which would save the employer costs on National Insurance Contributions, but for now at least it would appear that more charities will be facing the risk of having to close down as a result of spiralling pension deficits.

Please contact Craig Engleman if you would like to discuss this issue in further detail.

Craig Engleman

Consultation on new tax relief for social enterprises

The Government has launched a consultation on the design of a new tax relief for investment in social enterprise; called Social Investment Tax Relief (SITR). The Government proposals include limiting the relief to 'qualifying' social investment in community interest companies (CICs), community benefit societies and charities.

Social enterprises can take on a variety of legal structures and business models but the common aim is to combine business practices with social purposes, which seek to resolve social problems such as homelessness, crime and unemployment.

There are some tax relief schemes already available for trading companies, for example the Enterprise Investment Scheme (EIS) which encourages individuals to invest in small higher risk trading

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Also in this issue

New Gift Aid Small Donations Scheme (GASDS) for charities

On 6 April 2013 the Small Charitable Donations Act 2012 came into force, which created the Gift Aid Small Donations Scheme (GASDS). The GASDS allows eligible charities and Community Amateur Sports Clubs (CASCs) which already claim Gift Aid to receive Gift Aid style payments (known as top-up payments) on cash donations of £20 or less received after 6 April 2013. The scheme is aimed to benefit charities that receive frequent small donations in cash where they cannot obtain a Gift Aid declaration from the donor, for example through street collections or religious services.

In order to be eligible for the GASDS, a charity or CASC must satisfy the following eligibility criteria:

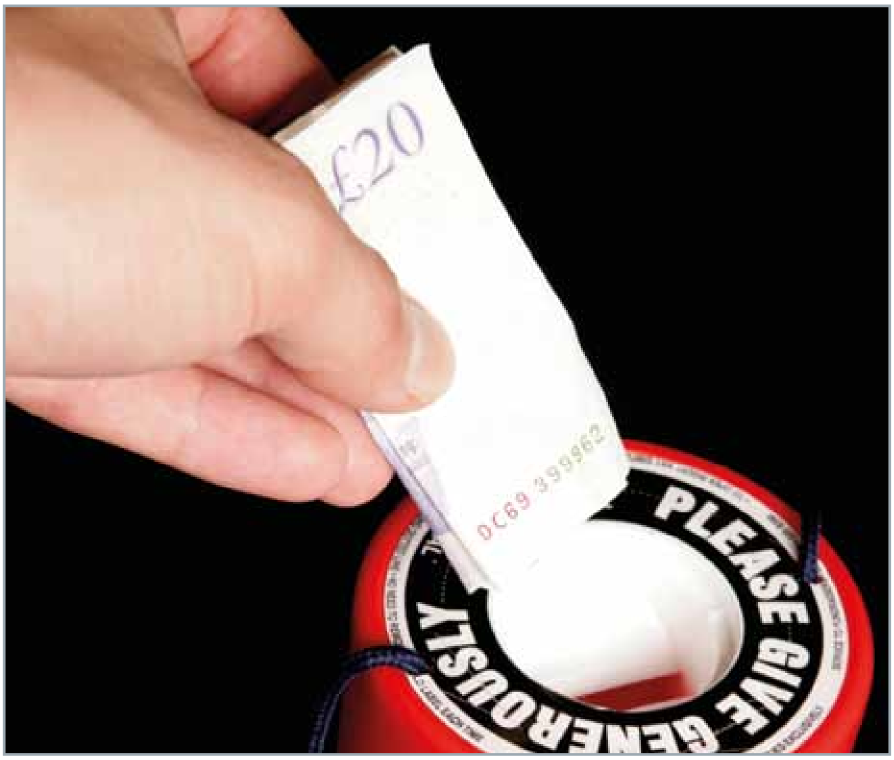
- the organisation must be recognised by HMRC as a charity or CASC for tax purposes;
- the organisation must have existed for two complete tax years (6 April – 5 April) prior to the tax year of the claim; and
- the organisation must have made a successful Gift Aid claim in two or more of the previous four tax years; and
- those Gift Aid claims must not be two tax years apart and there must not be two tax years between the last year of claim and the current year or claim; and
- the organisation must not have incurred a penalty in relation to a Gift Aid or GASDS claim either in the tax year of the claim or the previous tax year.

The eligibility criteria means that newly established charities will be unable to claim GASDS for at least two tax years following its recognition by HMRC as a charity for tax purposes, and will only be able to claim top-up payments once it has made successful Gift Aid claims in two tax years.

An eligible organisation can claim a top-up payment on £10 of small cash donations for every £1 of Gift Aid donations claimed, with a maximum claim on £5,000 of small cash donations per tax year. The top-up payment is calculated in the same way as Gift Aid and is based on the basic income tax rate for that tax year; therefore a charity can receive a top-up payment of £1,250 in each tax year for claims on small cash donations of £5,000.

However, where charities and CASCs are connected in any tax year any small cash donations received in that tax year will be pooled. HMRC states bodies will be connected if they:

- have the same or substantially similar purposes and activities; and
- are controlled by the same or connected persons.



Where bodies are connected they will share the maximum annual limit of £5,000 in small cash donations that can be claimed upon.

There is scope for charities (not CASCs) to increase top-up payments received where donations are collected by running charitable activities in a community building. A community building is a building that is not used for residential or business purposes, but charity shops are excluded. HMRC states the charitable activity must satisfy the following criteria:

- the activity must be one carried out as part of a charity delivering its charitable purposes; and
- the activity must be carried out by at least ten people, 6 times per tax year; and
- at least ten people attending each event must be beneficiaries of the charitable activity; and
- attendees must not be charged for entry to the building; and
- the activity must be available to the public or part of the public; and
- activities carried out for the primary purpose of fundraising are excluded; and
- donations must be collected in the building from the group during the charitable activities.

Where an activity satisfies the above criteria, a charity will be able to claim top-up payments on up to £5,000 of small cash donations collected while running the charitable activity in a community building, for every building that satisfies the criteria. The charity will also be able to claim top up payments on up to £5,000 of small cash donations that were collected elsewhere.

A small cash donation is defined by HMRC as a single donation of up to £20 received in bank notes or coins only (in any currency); cheques, credit cards, text donations and bank transfers are excluded. HMRC states that membership fees are excluded, as are cash payments that result in a benefit or gift to the donor (unless the benefit or gift is of little value). Any donation that includes a Gift Aid declaration is excluded and all small cash donations must be collected and banked in the UK to qualify.

HMRC states that charities and CASCs must keep records of any small cash donations received in order to evidence a claim under the GASDS. Records should show:

- the amount of donations collected;
- the date the donations were collected;
- who collected the donations;
- whether any donations collected were over £20 (to ensure they are not included in the claim).

Where donations are collected in a community building records should also show:

- the address and postcode of the community building;
- a note of what the event was; and
- a note of the number of beneficiaries attending the event (approximately).

This is in addition to the usual Gift Aid records. HMRC also advises charities to have systems in place to ensure staff or volunteers do not include payments of over £20 as small cash donations. HMRC, however, does not give guidance as to what these systems should be.

In addition to the GASDS, from 22 April 2013, HMRC are introducing a new Charities Online service in order for charities to claim Gift Aid and top-up payments. Alternatively, charities using form ChR1 which will replace the current form R68.

Gerry Morrison

The importance of due diligence in the recruitment of trustees

It has recently been reported that Sir James Crosby has resigned from his role as a trustee of Cancer Research UK after a critical report on HBOS was published from the Parliamentary Commission on Banking Standards, in which the bank's two leading executives and its chairman, Lord Stevenson, were severely criticised.

Crosby confirmed that he was resigning because he wanted to put the interests of the charity before his own. This has wide implications for the charity sector, and in particular it demonstrates how charities (acting through their trustees) need to exercise their own discretion and judgement when it comes to the composition of the trustee board. It can be extremely damaging for a charity's reputation if it has the wrong people on its board and it is also imperative for charities to periodically review who is on their board to ensure that they have the right mix of skills and experience. A charity's reputation is a valuable asset and if damaged, can impact upon a charity's ability to fulfil its aims and successfully raise funds and finance.

In contrast to Sir James Crosby, mental health charity MQ has confirmed that Lord Stevenson is to retain his role as Chairman of the board.

It is advised that charities undertake proper due diligence when recruiting trustees. This can mean vetting potential trustees on the skills/expertise which they can bring to the board, and ensuring that the trustees are the right people for the job. It is also advised that when a new trustee is appointed to the board, the charity should ask them to sign a trustee declaration confirming they are fit to act in the capacity of a trustee and they are

not disqualified from acting. It is also advised that any necessary disclosure checks are carried out, and particularly by charities working with children and/or vulnerable adults.

If you are considering changing or reviewing your board of trustees, then Rollits can advise on the procedure to be taken in order to safeguard your charity.

Sarah Greendale

Consultation on new tax relief for social enterprises

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companies by giving income tax and capital gains tax relief. Seed Enterprise Investment Schemes (SEIS) provide the same reliefs but this scheme is designed to encourage individuals to invest in start-up trading companies.

The Government proposes that the SITR will firstly offer income tax relief on qualifying investments which will be calculated at a percentage of the amount of the qualifying investment made, and deducted from an individual's income tax liability. Secondly, the relief would be on capital gains tax, allowing the payment of such tax to be deferred where proceeds of a disposal are reinvested in a qualified social enterprise. It is proposed that CICs, community benefit societies and charities will be the only "qualifying" social enterprises.

There are other criteria in order to qualify for the SITR which include the following:

1. The investor cannot be connected to the qualifying social enterprise;

2. The investor must hold the investments for a minimum of five years;

3. The original investment must not qualify for tax relief under either the EIS or SEIS;

4. The original investment must not be secured against assets or subject to guarantee;

5. The holders of the investment must not have preferential rights to assets on winding-up compared to other holders of the same type of investment; and

6. Returns on investments should be payable at broadly commercial rates and on broadly commercial terms.

It is also proposed that there will be caps on the investments per investor per year, and a cap on the maximum investment per qualifying social enterprise over three years', such caps are to avoid the need to obtain European Commission approval.

The Government's consultation closes on 6 September this year and the Government aims to publish draft legislation for consultation in the autumn, with a view to introducing such legislation in the Finance Bill 2014.

Sarah Greendale

Business rates relief: Charities beware

The Charity Commission has issued a warning to charities taking advantage of business rates relief following the case of *Public Safety Charitable Trust v Milton Keynes Council* [2013]. This is due to a growing number of tenancy agreements entered into between landlords and charities were the property is only partly used or left empty.

Ordinarily business properties attract business rates. However, Section 43 (6) Local Government Finance Act 1988 provides that business rates relief shall be available for charities or charity trustees in respect of a property where that property is 'wholly or mainly used for charitable purposes'. The relief is split into two parts: a mandatory relief of 80% of the business rate for the relevant property and a discretionary relief of 20%. Whether the discretionary relief is available will depend on the relevant local authority.

In the case of *Public Safety Charitable Trust ("PSCT") v Milton Keynes Council*, the PSCT entered into a large number of tenancy agreements of business properties but only used a small area of each property for furthering their charitable purposes. The remainder of each property was left empty. A number of local authorities refused to give the PSCT business rates relief on the basis that they were not using the properties wholly or mainly for charitable purposes. There was no doubt as to whether the PSCT used the properties for charitable purposes; but the question arose as to the extent a property must be used for charitable purposes for the relief to apply.

The courts looked at the definition of 'wholly or mainly used for charitable purposes' and Parliament's intentions when drafting the legislation. The courts held the definition not only includes the purpose which the property is used for but also the extent or amount of the actual use. This means charities cannot just use a property wholly and mainly for charitable purposes for the relief to apply; they must use a large extent of that property for charitable purposes. This case does not, however, offer any guidance on the exact extent or amount a property must be used in order for business rates relief to apply.

This case followed the previous decision of *Kenya Aid Programme v Sheffield City Council* [2013]. Kenya Aid used 50% of two properties for charitable purposes, but the court held this was not wholly and mainly for charitable purposes. Kenya Aid was made to pay over £1.6 million to the local authority in backdated business rates as a result of this decision.

The Charity Commission has warned charities that they may be liable to pay full business rates if they do not use the full extent of a property for charitable purposes and leave parts of a property unused. The Charity Commission has also warned charity trustees that they may be personally liable if they do not carefully consider a tenancy agreement and consequently full business rates become chargeable.

The Charity Commission has advised charity trustees to comply with the following steps before they enter into a tenancy agreement:

- Be sure that the tenancy agreement is for the exclusive benefit of the charity, will further the charity's purposes and is in its best interest;
- Ensure the property is genuinely required and is fit for purpose;
- Consider the potential liability of the charity to pay outstanding rates if the local authority disputes use of the premises and refuses rates relief;
- Very carefully safeguard the charity's independence and ensure the charity is not being abused for the benefit of a commercial company;
- Take suitable professional advice, including legal advice, before entering into a tenancy agreement

Charities must think carefully before entering into a tenancy agreement where they do not plan to use a large extent of a property for charitable purposes or were they believe a landlord may be trying to avoid paying business rates, especially as there is no guidance in either of the above cases as to the exact extent a property must be used for business property relief to apply. Failure to consider a tenancy agreement carefully may result in a charity having to repay full business rates to a local authority for their entire period of occupation of a property, which could potentially amount to a large sum. Charity Trustees may also find themselves personally liable if any loss which results to the charity is as a result of their breach of duty. We can provide specific advice to charities which may be concerned about their own arrangements.

Gerry Morrison

Information

If you have any queries on any issues raised in this newsletter, or any education matters in general please contact Gerry Morrison on (01904) 625790 or email gerry.morrison@rollits.com

The law is stated as at 10 July 2013.

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