# Charity Tax Group
# Budget Submission 2017

18 January 2017

The Charity Tax Group (CTG) has over 500 members of all sizes representing all types of charitable activity. It was set up in 1982 to make representations to Government on charity taxation and it has since become the leading voice for the sector on this issue.



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CTG welcomes the opportunity to make a Budget submission, which outlines a number of policy areas on which the Government could take action to improve the tax position of charities. We look forward to having the opportunity to discuss these issues further with the Financial Secretary to the Treasury and with officials, and to working with the Government to help create a simpler and fairer tax system for charities

## Tackling irrecoverable VAT

1. Charities continue to face structural distortions from the VAT system that result in irrecoverable VAT. We have estimated that the total annual cost of irrecoverable VAT to charities is at least £1.5bn a year. Many UK charities have taken over, or are willing to take over, the delivery of public services outsourced by governmental bodies, often because they are best placed to do so. However, the current system provides a disincentive to doing so because charities face large irrecoverable VAT bills unlike an equivalent public body.

2. While we would argue that a wider strategic review of the VAT system should be undertaken – particularly taking into account the increased freedom that Brexit is likely to give the UK Government – this will only give rise to results at some future date. CTG therefore urges the Government to introduce additional targeted refund schemes under the S33 VATA category. CTG is working with its VAT Expert Group and charities to develop a series of proposals to achieve substantive change and demonstrate the long-term value of such measures to both charities and the Government. Removal of the irrecoverable VAT burden would provide an important income boost for affected charities, decreasing their reliance on state funding and increasing their capacity to provide vital public services, resulting in a wider economic benefit for society.

***How the Government can help:***

- **By continuing to work with the sector to develop further s33 refund schemes.**
- **By working with the sector to identify opportunities for new reliefs for charities, reflecting the modernisation of charity operations and innovations not covered by the existing zero rates.**
- **By actively listening to the voice of the charity sector as part of Brexit negotiations, particularly in relation to the operation of the VAT system.**

## Insurance Premium Tax (IPT)

3. In the 2016 Autumn Statement, the Chancellor announced that, from June 2017, Insurance Premium Tax [IPT] would be increased from 10% to 12%. Since 2010, the rate of IPT will have more than doubled.

4. We recognise that IPT is a tax on insurers, but providers invariably pass on these costs and as charities do not benefit from an exemption they will be affected. IPT has a disproportionate impact on charities (especially those with substantial operational buildings - such as charities that provide activities in their buildings - and extensive transport and travel commitments) and we have serious concerns about rumours that IPT may eventually be increased to 20%, in line with VAT.

5. CTG has been running a survey to assess the cost of the proposal for the charity sector and initial results show that this 2% increase will cost in the region of £300,000 this year alone, with the total IPT cost of those charities surveyed now in excess of £1.7m a year. Our survey also demonstrates that the cost of an increase to IPT will weigh particularly heavily on some of the smallest charities – Village Halls, Community Associations and small church congregations, for example – as the insurance related to maintaining their buildings responsibly is a significant cost

***How the Government can help:***

- **By committing to a review of the current IPT burden faced by charities to assess whether a total or targeted exemption or a reduced rate would be achievable where the insurance is required to cover activities or premises that directly relate to a charity's objects.**

## Research and Development Credit (RDEC)

6. The Government has set an ambitious target for public and private expenditure on R&D to be 3% of GDP by 2025. In a highly competitive world, UK performance in R&D will depend on the Government supporting the sector's excellence in this area and helping to stimulate it further. The Research and Development Credit (RDEC) was introduced in 2013 but, since then, the legislation has been amended so that universities and charities are unable to claim it.

7. The Government has stated that the rationale for withdrawing the relief is that charities and universities were never the intended recipients of RDEC and that, in the case of universities, equivalent funding is already provided through HEFCE. However, non-university research charities receive no such funding and the reintroduction of RDEC for them would provide a major stimulus to R&D in medical research in the UK thereby helping to meet the Government's stated objectives. Our understanding is that HMRC has been resisting existing RDEC claims made by many charities. This

runs the risk of sending out conflicting signals on the Government's intention to boost spending on R&D. A commitment by the Government that charities should be treated as being as eligible as a university for the relief would be helpful both to stimulate further investment in R&D and unlock RDEC that has already been claimed. We believe that there are other imaginative tax measures that the Government could introduce to stimulate the funding of bio-medical research by charities and CTG would be pleased to discuss these with Ministers and officials.

***How the Government can help:***

- **By supporting claims made by research charities for any qualifying expenditure they incurred prior to 1 August 2015.**
- **By reinstating RDEC as a relief for non-university charities.**
- **By engaging in a dialogue with charities as to how bio-medical research could be further stimulated by charities through targeted tax reliefs.**

## Employer-provided Living Accommodation

8. CTG met HMRC officials in early 2016 to discuss the Office for Tax Simplification's proposals to review existing exemptions relating to Employer-provided Living Accommodation. We highlighted the significant value of the current exemption for charities, in particular for churches, hospitals, higher education establishments and heritage buildings. For these types of charities, accommodation is provided for the better performance of the duties of those employees whom the charity accommodates – an obvious example is parish clergy in the Church of England and the Church of Scotland, who are normally obliged by church law to reside in the parsonage house. In the vast majority of cases, it is these exemptions that make the provision of a reasonable standard of living possible. We understand that that a further consultation on this issue will be announced in the Budget and we urge the Government to maintain this important exemption, which is so important for certain charities.

***How the Government can help:***

- **By committing to protecting this exemption as part of the consultation on Employer-provided Living Accommodation.**

## Apprenticeship Levy

9. CTG supports the Government's drive to improve productivity by increasing the number of apprentices in the workplace but we have serious concerns about the extent to which the Apprenticeship Levy, in its current form, can be utilised for training the charity workforce. Many charities do not currently employ apprentices and, in some cases, doing so on a sufficient scale to utilise the levy fully would be neither realistic nor appropriate.

10. On the other hand, volunteers are the lifeblood of the charity sector and, in many charities, they outnumber paid staff by a considerable margin. Volunteers provide a very effective and productive workforce and, without them, many charities would find it difficult to operate as effectively as they do. However, they are not by definition 'employees'; and, given their importance to the sector, we would argue that it makes sense to extend the levy contributions made by charities to supporting accredited volunteer training and associated expenses. This would be an effective way of using this funding and would meet the intention that the levy should increase the skills of our workforce. In particular, resources could be focused towards encouraging younger people to get involved in volunteering, thereby playing a role in the up-skilling of the country's younger workforce, which will allow them to bring additional relevant skills to any paid employment. We would be happy to give examples of how activities carried out by volunteers can be applied in an employed role.

***How the Government can help:***

- **By permitting charities to assign to other charities any unused Levy credits at a higher level than the 10% currently under consideration. This move would ensure that more funding is retained for charitable use.**

- **By allowing Levy funds to be used to pay for accredited volunteer training and associated expenses.**

## Transfer of profits

11. CTG wholeheartedly supports Government efforts to stop charities being used as vehicles for fraud and tax avoidance, but has stressed the need for proportionate and targeted legislation that will not inadvertently catch innocent donors or charities.

12. We welcomed the Government's decision to introduce a charity exemption from the Diverted Profits Tax following CTG representations that charities would be inadvertently caught by the legislation. We believe that a similar exemption is necessary to avoid charities being unintentionally caught by

the legislation on transfer of corporate profits in s1305A in Chapter 1, Part 20 of Corporation Tax Act 2009, as introduced by the Finance Act 2014.

13. We have welcomed Ministerial assurances that the legislation will not apply if a company pays all its profits to charities through Gift Aid unless avoidance is present, and also the confirmation that it is not avoidance if taxpayers use statutory relief for charities in the way intended by Parliament. We also welcomed the written assurances, given in the technical guidance note (see example 6) published in March 2014, that charitable subsidiaries would not be caught. However, based on our experiences, we believe that such assurances should be enshrined in legislation and we urge the inclusion of a charity exemption in the next Finance Bill. This proposal would result in no additional cost to the Exchequer.

***How the Government can help:***

- **By introducing in the next Finance Bill an exemption for charitable companies from the legislation on the transfer of corporate profits.**

## Making Tax Digital

14. CTG commends efforts to improve digital record keeping, through the Making Tax Digital agenda, and we welcome the Government's commitment to consulting on exemptions for charities and Community Amateur Sports Clubs (CASCs).

15. Many larger charities with sophisticated support systems and infrastructure are already familiar with online operations and would not face major issues in moving to online record keeping. However, as we outlined in our response to the consultation, for those charities with limited resources or a lack of digital expertise, it is preferable that the processes remain optional so that they manage the transition at a time suitable to them. Note should be taken of the fact that most charity income is covered by a relevant tax exemption or falls within the small-scale trading relief.

16. In the long-term we believe that Making Tax Digital can help to simplify the Gift Aid system, given the increased powers HMRC will have to identify whether donors have paid enough tax to cover a Gift Aid declaration or are eligible for higher rate relief.

***How the Government can help:***

- **By introducing an exemption from digital record keeping for charities, while providing resources and support for those charities that wish to opt in**

## Administrative burden of tax issues

17. CTG published a Charity Tax Map which highlights the wide range of taxes affecting charities. Importantly it also highlighted the high compliance cost burden related to charity taxation. It also demonstrated the significant variation between charities in their tax and compliance costs which depended on the charities' particular activities (rather than just the scale of activities) and the time involved in obtaining particular tax reliefs. This is a cause for concern since it suggests that some charities are having to devote a disproportionately high level of their resources to compliance: resources which might be better devoted directly to their charitable activities.

18. Charities often face large administrative costs (both in terms of time and financial resources) when they are required to introduce new reporting requirements or maintain detailed record-keeping structures to comply with the requirements of the tax system. This is particularly true when charities are required to invest in new IT infrastructure, training and professional advice, the cost of which can sometimes undermine the benefit (where relevant) of the tax relief/scheme in question. Recent examples of this are the Apprenticeship Levy, Common Reporting Standard, filing of charity subsidiary trading accounts and, for the largest charities, the requirement to publish an annual tax strategy.

***How the Government can help:***

- **By committing to a review of the administrative burden of tax policies on charities and more detailed consideration of associated costs when compiling Impact Assessments.**

- **By providing, where possible, free tax reporting tools for charities.**

## VAT Grouping and the Cost Sharing Exemption

19. HMRC's review of the rules relating to VAT Groups and the Cost Sharing Exemption, in the wake of relevant CJEU decisions, needs to ensure that charities are not inadvertently discriminated against. If it is accepted that a non-corporate body may group register with other closely related entities, this will present an opportunity for unincorporated charities to form a VAT group with their trading subsidiaries. However, unless it is agreed that the trustees of the unincorporated charity will not be held jointly and severally liable in respect of their *personal* assets (such as their own house), the change will provide no assistance to the sector. We are strongly against any system which compulsorily group-registers related entities. We believe that more work is needed on how to determine a close enough financial link to allow group registration to occur. We are against any rule

which would remove the current ability of a charity to group register with a company over which it exercises Companies Act control.

20. We are keen to ensure that the potential opportunity to reform the Cost Sharing Exemption is taken up and that the current, highly impractical, approach is reformed. This measure could remove considerable obstacles to co-operative working between charities. We would be happy to reinforce views already expressed to HMRC on this topic. However, we do not think that the Cost Sharing Exemption should be regarded as being any kind of substitute for an ability to form a VAT group registration, and we see the two issues as being unrelated to each other.

***How the Government can help:***

- **By committing to a review of the rules relating to VAT Groups and the Cost Sharing Exemption in respect of charities.**

**CTG**
**January 2016**