

House of Commons Treasury Committee Inquiry into Tax after Coronavirus

Joint response to the Call for Evidence by the Charity Tax Group, Charity Finance Group, National Council for Voluntary Organisations and Chartered Institute of Fundraising

8 September 2020

Summary

1. As a result of COVID-19, traditional income sources for the charity sector have come under increased strain, while demand for services has increased. Charities benefit from important and valuable tax reliefs (estimated at £3.79bn in 2018/19) and it is important that any reforms to the tax system after Coronavirus, do not have any inadvertent adverse financial impacts on charities. Charities already face a cumulative burden of taxation, both in terms of tax payable (particularly irrecoverable VAT and employment taxes) and the administrative burden associated with compliance – both of which are higher than generally perceived by the public.
2. This joint response to the Inquiry, from sector experts on tax and finance issues, outlines a number of core principles that should underpin any reform of taxation going forward. As a minimum, existing charity tax reliefs should be protected and tax compliance and administration simplified. We highlight the importance of protecting valuable existing business rates and VAT reliefs, future-proofing tax systems and legislation and call for improved collaboration and dialogue between HMRC and the charity sector. The charity sector also makes a specific call for a Gift Aid Emergency Relief package to help ensure charities have sufficient funds to play a leading role in the COVID-19 recovery.

Impact of COVID-19 on the charity sector

3. The charity sector, like the rest of the economy, faces a financial crisis as a result of the pandemic. Huge falls in income, increased levels of demand for services, needing to do more to respond to COVID-19 and care for the most at-risk and marginalised individuals and communities has created a perfect storm. Recent research by *Pro Bono Economics* has found that UK charities are facing a £10.1bn funding gap over the next six months with incomes expected to drop by £6.7bn while demand for support rises by the equivalent of £3.4bn. The initial £750m charity support package (which was primarily intended to support organisations on the frontline response to COVID-19) and other Government support schemes, have helped some charities, but the gap between support provided and need is vast and likely to increase.

Principles that should underpin reform of taxation of charities

4. Improvements and simplifications to the tax system are an important way that the Government can support the charity sector to recover from COVID-19 and to maximise the effectiveness of public funding and private philanthropy. Consultation between the Government and the charity sector on future tax policy is therefore crucially important.
5. The charity sector is not homogenous and the way that taxation and associated reliefs affect different types of charity depends on their size, activities and structure. There may not always be a one-size-fits all solution – more often there is not. The recent Independent [Charity Tax Commission report](#) outlined three pillars that should underpin the design of charity tax reliefs:
 - i. To support functional activity undertaken in pursuit of a particular social good or public benefit. The principles governing charity tax reliefs should also reflect the distinctive value of the independence of charities and individuals' decisions to support good causes.
 - ii. To support individual donations to, participation in and support of charitable activity.
 - iii. To support charities to increase efficiency and effectiveness and to innovate and collaborate.
6. In difficult economic times in the aftermath of COVID-19, there will inevitably be pressure on the Government to review existing tax reliefs. It is sometimes assumed that tax reliefs received by charities are simply Government expenditure that could simply be redistributed. However, there is a strong and long-standing rationale for many tax reliefs and it is important that in reform of the tax system key principles are not undermined e.g. the principle underpinning donor reliefs is that individuals should not pay tax on income given away to support charities delivering public benefit. Charity reliefs from VAT, rates, corporation tax and other taxes follow similar principles that money that is used to generate public benefit should not be subject to tax. It is also important to remember that, as not-for-profit organisations, charities do not benefit directly from all tax policies to support businesses and stimulate the economy, such as corporation tax reductions, so sector-specific solutions are often required.
7. While it is right that the value and appropriateness of tax reliefs is considered when reviewing the future of tax policy, it would be helpful for the Government to review the scope and value of taxes actually paid by charities and whether this is appropriate. For example, at least £2bn was paid in business rates and irrecoverable VAT last year, significantly more than is commonly perceived to be the case. In addition, for Gift Aid evidence from HMRC research suggests that the total amount of tax relief claimed is £380m lower than the number of donations on which tax relief was eligible. The reality is that if many of the existing tax reliefs were not in place the cost to the sector and the wider community and economy would be higher as charities would have fewer resources to deliver their vital work, placing additional burden on public services.
8. The charity sector is supportive of Government efforts to stop organisations 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, or result in disproportionate compliance costs. [Research](#) has highlighted the significant costs and complexities for charities in complying with tax legislation, yet successive Governments have been slow to address the problem. 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. In addition, small charities, often run by volunteers, can find tax legislation and guidance very difficult to comprehend, let alone follow.

The importance of protecting and improving tax reliefs for charities

9. As outlined above, tax reliefs are hugely important to charities and were worth at least £3.2bn in 2018-19. The long-term protection and improvement of tax reliefs that charities are able to access is therefore essential to the future financial stability of the charity sector.
10. While there is a cost to these tax reliefs, this is a small investment compared to the socio-economic benefits that charities provide, generating employment, investing in research, reducing reliance on state services. For example, charities provide a means through which around 19.4 million people formally volunteer, estimated to be worth £23.9bn in the most recently available data. The sector contributed in total an estimated £18.2bn to the UK economy in 2017/18, equivalent to almost 1% of total GDP. In addition, research charities spent more than £4bn on research in 2017/18¹.
11. It is important that any taxation reform proposals do not leave charities worse off. In England, the Government has launched a Fundamental Review of Business Rates, which includes a review of all reliefs. Given that the largest of these reliefs is Charitable Rate Relief (worth £1.93 billion in 2018-19 in England), it is important that broader reform of business rates and property taxation do not disadvantage charities or lead to additional administrative complexities. Policymakers in Scotland and Wales have taken steps to review charity rates relief or restrict its application, but it is our strong view that eligibility for tax reliefs should be based on agreed charity law definitions of eligible bodies and not operate as an instrument to support or exclude charities seen as more or less deserving of relief.
12. Reform of VAT is also a major priority for the charity sector. As charities often provide services that are either exempt from VAT or outside the scope of the VAT system, they are unable to recover the VAT that they pay on the purchases incurred to help their beneficiaries. They are, in effect, treated as the final consumer, even when they are not. The UK standard VAT rate of 20% compounds the cost to charities at a time when their services are more in demand than ever. A forthcoming research study by the Charity Tax Group will highlight the importance of existing VAT reliefs and exemptions for the charity sector. However, the research will also provide strong evidence that VAT continues to place a significant burden on UK charities, despite existing reliefs. It thus reinforces the rationale for significant structural reform to reduce the level of irrecoverable VAT facing charities. A fundamental

¹ <https://data.ncvo.org.uk/>

review of VAT should be at the forefront of the Government's policy agenda for the charity sector. Any attempts to broaden the VAT base or remove reduced VAT rates should take into account what the unintended consequences for charities might be.

13. Investment and forward planning is also required to ensure that there is a tax system fit-for-purpose for the future. The administration and application of Gift Aid is based on an increasingly outdated paper-based system that is inflexible in adapting to new payment mechanisms and digital technology. Greater automation and interaction with HMRC tax records could achieve the twin objectives of reducing the tax gap and maximising the value of eligible Gift Aid claimed. There has already been positive engagement between the sector and HMRC's innovation team on this "future of Gift Aid" project and resources should continue to be allocated to this initiative.
14. In addition, tax legislation and guidance failing to keep up with commercial and technological developments is a recurring problem. Recent examples include the need for extensive campaigns to address the VAT treatment of digital advertising and e-publications. Often, when HMRC has identified a need to update guidance, there has been insufficient resources available to undertake this work. It is important that tax reliefs, designed by Parliament to reduce the tax burden, are not eroded by inaction.

The importance of philanthropy and individual giving to the COVID-19 recovery

15. While Government support for the sector will be crucially important, the importance of philanthropy in a post-COVID-19 world cannot be underestimated. For that reason, it is important that the tax system supports and facilitates giving and does not provide an obstacle to it. It sends a clear message that philanthropy and personal engagement matters. Where lawful tax relief mechanisms are available (and openly promoted by the Government), these should be promoted to maximise private philanthropy. Although donors receive tax relief on their giving they need to give away a significant amount more than they receive in relief.
16. To support the COVID-19 recovery, a coalition of leading voices in the UK charity sector have called on the Government to temporarily increase the level of Gift Aid that can be claimed on donations. Raising Gift Aid from one-quarter to one-third on donations, on a temporary basis, could secure an extra £450m for charities and benefit over 70,000 charities, as they return to fundraising activity and re-open charity shops. The initial response received from the Treasury indicates that they do not believe it would be appropriate to make changes to Gift Aid at this time, but, importantly, no insurmountable technical obstacles have been identified, and there is precedent for such a change with the introduction of Gift Aid Transitional Relief in 2008. The proposal has received significant support from charities and we would urge the Treasury Committee to support calls for this important temporary relief package, which would increase the value of individual giving and potentially incentivise an increased number of donations.

Improving consultation with the charity sector on tax policy and tax reform

17. The impact on charities should be considered in any future changes to the tax system and HMRC and HM Treasury should increase the opportunities for engagement with the sector. The HMRC Charity Tax Forum provides a useful platform for discussion, but it is often reactive and focused on reporting, rather than providing a space for substantive discussions about the future of charity taxation. Pro-active discussions should be taking place sooner rather than later to plan ahead for the COVID-19 recovery.
18. The recent COVID-19 crisis has highlighted the need for improved liaison between HM Treasury and HMRC and other departments (including DCMS, BEIS and MHCLG) on financial support and tax relief measures for charities. It would be helpful if there was a clear mechanism that could be activated in times of emergency so there are clear channels for representations by sector bodies and individual charities. A better understanding of the impact of taxation on charities would help to avoid all too common situations where charities miss out on reliefs or are subjected to tax rules not designed to impact on them.

About us

The Charity Tax Group (CTG) has over 800 members of all sizes representing all types of charitable activity. The organisation 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.

The Charity Finance Group (CFG) inspires a financially confident, dynamic and trustworthy charity sector. It does this by championing best practice, nurturing leadership and influencing policy makers. Over 1,400 UK charities turn to CFG to develop their finance management knowledge and skills. Collectively, these charities manage £22bn of funds – a third of the charity sector's income.

The National Council for Voluntary Organisations (NCVO) is the largest representative body for charities and voluntary organisations in England. NCVO has over 15,000 members ranging from large 'household name' charities to small community organisations. NCVO is also the national body for volunteering in England.

The Chartered Institute of Fundraising (IoF) is the professional membership body for UK fundraising. Its mission is to support fundraisers through leadership, representation and education, and it champions and promotes fundraising as a career choice. It has over 600 organisational members who bring in more than £10 billion in income, and over 6,000 individual members.