charity tax group

OECD Pillar 2 – HM Treasury Consultation on Implementation

Response by the Charity Tax Group

4 April 2022

Introduction

1. The Charity Tax Group (CTG) has over 1000 members of all sizes representing all types of charitable activity in the United Kingdom, as well their professional advisers. The organisation was set up in 1982 to make representations to charity taxation and it has since become the leading voice for the UK charity sector on this issue.

2. CTG welcomed the opportunity to respond to the OECD consultation on Pillar 2 and would welcome further direct consultation with HM Treasury on the impact of its implementation for not-for-profit organisations in the UK. This will be very important to avoid unintended consequences as we have identified a potential issue for charities with UK trading subsidiaries which donate their taxable profits to the charity under the company Gift Aid Scheme.

3. CTG is not directly affected by this proposal, but our comments are informed by feedback from our members who believe that they are. We have liaised with UK partners including the British Universities Finance Directors Group (BUFDG) and Charity Law Association (CLA) and support the detailed representations that have been made on behalf of UK charities and universities.

Comments

4. CTG supports moves which tackle tax avoidance and abuse. However, we believe it is also important that measures to tackle avoidance are proportionate and do not have an adverse impact on not-for-profit organisations like charities.

5. Under the model rules, it is welcome that most UK charities should be considered an Excluded Entity under the Non-Profit Organisation exclusion. However, a charity's revenue is still included in determining whether the group it heads up breaches the €750m turnover threshold. To the extent that this threshold is breached, it then falls to be determined whether the charity's subsidiaries are taxable under Pillar 2.

6. The model rules include an exclusion for 95% owned subsidiaries of Excluded Entities providing they only perform activities which are "ancillary" to the activities of their parent Excluded Entity (i.e. the charity), under Article 1.5.2.(a)ii.

7. Under Section 191 of Corporation Tax Act 2010 ("CTA 2010"), a wholly owned UK trading subsidiary of a UK charity donating all of its taxable profits to the charity (under the company Gift Aid Scheme) will get a tax deduction equal to the amount of its profits, so that no Corporation Tax will be payable, irrespective of whether the activities of the subsidiary are ancillary to the activities of the charity.

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While all efforts are made by the Charity Tax Group to give assistance to its members, it is not qualified to give technical advice on fiscal matters and cannot therefore be liable in any way for any such advice given.

8. However, under the Global Anti-Base Erosion (GloBE) Rules, if a trading subsidiary does not carry out activities that are "ancillary" to the activities of its parent charity and it donates its taxable profits under gift aid, a Top-Up Tax may arise to the extent that the subsidiary's effective tax rate, in aggregate with other UK entities within the Multinational enterprise (MNE) group, falls below the 15% minimum rate.

> **Example**: A UK educational charity (part of an MNE group for the purposes of Pillar 2 but itself considered an Excluded Entity under the GloBE Rules), has a wholly owned UK trading subsidiary which performs activities which are not exclusively ancillary to the activities of the charity (e.g. it runs a shop which sells products other than educational products).
>
> The subsidiary earns taxable profits of £1m and donates the entire amount to the charity under the company Gift Aid Scheme.
>
> Under current UK tax rules, the subsidiary obtains a tax deduction equal to the amount of its profits, so that no UK Corporation Tax is due.
>
> However, under the GloBE Rules, the MNE group would apparently be considered to have GloBE Income of £1m and nil Covered Taxes (i.e. zero Effective Tax Rate), giving rise to Top-Up Tax of £150k.

9. We note that the OECD has also now published further commentary on this issue, however the ambiguity remains as to the precise interaction between the Pillar 2 rules and the existing UK rules on Gift Aid. There are many and varied interpretations of the concept of "ancillary" by UK charities and their advisers. Without further clarification charities risk being caught out or facing significant additional costs in seeking professional tax advice.

10. It is also important to note that some large charities may be denied Excluded Entity status solely because they have a small amount of income from the sale of goods or services that are unrelated to their charitable purposes. This is at odds with current UK charity tax policy which provides a limited exemption for small-scale trading by a charity without the needs to set up a trading subsidiary. To address this, the UK implementation of the model rules should ideally incorporate a *de minimis* threshold similar to the current limit under domestic law.

Conclusion

11. The top up tax could have a significant detrimental effect on the charity sector and does not appear to be consistent with the aims of the GloBE rules or indeed domestic policy and reliefs under Section 191 of CTA 2010. Therefore, we urge HMT to reconsider this proposal, with a view to ensuring that there are no adverse consequences for the university or charity sectors. While most charities will not currently meet the turnover threshold for eligibility, we are conscious that this could be lowered in the future and that this is an important point of principle to be resolved at the outset.

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12. Given the clear intention to take 'Excluded Entities' outside of this regime, HM Treasury could decide to exclude the revenue arising from any 'excluded entities' within the group from the calculation of the €750m consolidated revenue threshold. This would ensure that even with the debate around the status of trading subsidiaries as excluded entities, all UK charity groups should fall outside of the regime.

13. Alternatively, HM Treasury could consider one of the following measures to mitigate against a low effective tax rate arising due to a subsidiary donating its charitable profits to its parent charity under the company Gift Aid Scheme –

    a. The inclusion of Gift Aid payments by subsidiaries to their parent charity within the permitted adjustments to accounting profit in determining "GloBE Income"; or

    b. The inclusion of Gift Aid payments by subsidiaries to their parent charity, at the prevailing UK corporate tax rate, within the permitted adjustments in calculating "Covered taxes".

CTG
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