Charity Sector

Specialist Charity Accountants

Newsletter
Winter 2015

www.hawsons.co.uk

Introduction

The cold, wet weather and nights drawing in indicate winter is well on its way which means it's time for our Winter 2015 newsletter!

With the ongoing developments of the Kids Company case and the resulting additional pressures on effective financial management, the charity sector still faces a challenging future. There are many lessons to be learnt from the Kids Company closure and, once again, that is a key focus in our latest newsletter. We also look at the recent Autumn Statement and its impact on the sector, as well as the continuing complexities of gift aid payments made from a charity trading arm.

In this issue we look at:

- Autumn Statement charity review
- Non-financial trustee lessons from Kids Company
- Update on gift aid payments from charity trading arms to the parent charity
- Recent housing case highlights complicated charity VAT exemptions
- Are charities ready for auto enrolment?
- 43% of large charities fail to report correctly

We hope you enjoy this edition of our newsletter and, as always, please get in touch if you would like any further information.

Simon Bladen
Charity & Not-For-Profit Partner

E: slb@hawsons.co.uk
T: 0114 266 7141
LinkedIn: www.linkedin.com/in/simonbladen

Hawsons are specialist charity accountants

At Hawsons we recognise that not-for-profit organisations have very different requirements from other businesses and are currently exposed to a challenging economic climate. Our dedicated team fully understands the complex, ever-changing regulatory requirements of the charity and not-for-profit sector. Given the additional pressures on fundraising, complex tax regimes, internal risk exposure and stakeholder demands, it has never been more important to obtain specialist professional advice.

Our specialist team acts for a large number of charitable and not-for-profit organisations across each of our Sheffield, Doncaster and Northampton offices. For more information on our charity and not-for-profit expertise, including the services we offer and our experience, please visit: **www.hawsons.co.uk/charities**

HLB International

INVESTORS IN PEOPLE

Autumn Statement charity review

Last week, on 25 November, the Chancellor delivered his latest Autumn Statement. In a year which has already seen two Budgets and a General Election, and the possible anticipated focus on gift aid, it is with some trepidation that charities awaited this year's Autumn Statement In this article we summarise the key points arising from the Autumn Statement and focus specifically on what the changes may mean for the charity sector.

In summary (general):

- Tax credit cuts scrapped all together
- £12bn in targeted welfare savings to be delivered in full
- Small business rate relief to be extended for one more year
- NHS to receive £10bn more funding a year in real terms by 2020
- Basic state pension will rise by £3.35 to £119.30 a week
- New 3% surcharge on stamp duty for buy-to-let properties and second homes from April 2016
- Doubling of housing budget to £2bn a year
- Capital funding of transport projects to rise by 50%
- Increased devolution with 26 new or expanded Enterprise Zones announced
- Transport (37%), environment (15%) and energy (22%) departments all face funding cuts

In summary (charity specific):

- Extra £15m funding for women's support charities to come from 'tampon tax'
- Increase in places on the National Citizen Service
- No change to the Big Lottery Fund
- Budget freeze for the Charity Commission
- Partial exemption to close company loan rules
- £1.5 billion uplift to the Better Care Fund by 2019-20
- Large charity employers hit by apprenticeships levy
- Gift Aid Small Donation Scheme review to begin earlier than expected
- Business rates review delayed

Autumn Statement charity impact

Simon Bladen, Charity Partner at Hawsons, commented: "This was an Autumn Statement that delivered very little in the way of charities; it actually turned out to be a fairly uneventful affair. Much of the comment following the announcements, in the charity sector, will undoubtedly surround the Chancellor's controversial 'tampon tax', which will deliver annual funding of £15m to support women's charities."

"There were some welcome announcements though, including the expansion of the National Citizenship Service, the extension of the Better Care Fund and a continued commitment to the Big Lottery Fund. The Chancellor also confirmed that the Charity Commission's funding is to remain at its current level until 2020/21. That is still an effective funding cut in real terms, but it is not as severe as some in the sector had feared. Charities play a critical role in our society so any funding cut is unwelcome news. There was considerable anticipation for a stronger focus on gift aid, which didn't turn out to be the case. The Chancellor did however confirm that the Gift Aid Small Donations Scheme review would begin in December 2015, much earlier than expected. Although this initial review is likely to be only the first stage in a long review process, it is certainly a positive development for the smaller charity community."

"The exemption from Section 455 for loans to charities that use the funds for charitable purposes (e.g. where charity has a trading subsidiary) brings good news to the sector. This is a long overdue announcement and will provide welcome relief to charitable organisations that have been caught unawares by this tax."

This measure comes into effect immediately and will only be applied from 25 November 2015.

The government has now released a policy document saying that the measure "exempts loans or advances made by close companies to trustees of charities for charitable purposes from the tax charge applied under the loans to participators rules."

Non-financial trustee lessons from Kids Company

The high-profile closure of Kids Company has seen the charity and the government come under intense scrutiny regarding funding, governance and financial management. Following its closure on 5 August 2015 there have been some serious allegations concerning the running of the charity. These allegations are currently subject to investigation and inquiries from a number of governing bodies.

Let's not get it wrong - the news that Kids Company has closed down is a devastating blow to everyone involved in the charity sector. Charities rely on public support by their very nature, so when cases such as this arise it can damage the sector, not just the individual charity. The media spotlight following the Kids Company case is putting even greater emphasis on ensuring effective financial management and fiscal planning within charities.

Non-financial lessons for trustees following Kids Company closure

In this article, we put finances to the side and focus on the non-financial lessons for trustees following the charity's closure. The failure of Kids Company is a very serious reminder to trustees that their role within the charity is anything but non-functional; they have the responsibility to safeguard the future of the organisation and ensure it continues to be capable to act for the public benefit.

Trustees cannot stay around long-term: The Guardian recently published an excellent article – good charity trustees are like gold dust, but they have a shelf life – which highlights that "it is also often forgotten that they (trustees) shouldn't become part of the furniture" within a charity. In any organisation, be it commercial or charitable, when the management board becomes 'part of the furniture' it is often difficult to champion change and challenge the status quo. But as the world changes, new strategies, priorities and operations must be looked at. For example, income diversification to include both traditional and non-traditional approaches is paramount.

A trustee board must have diversification of complementary skills: The second point is one that we have spoken about before, in our guide to trustee recruitment (available on our website). A board should have a broad range of skills (such as IT, legal, financial etc), but it should also be diverse in other areas too. To ensure that trustees speak up, challenge actions and raise concerns a charity board with varied skills, perspectives and backgrounds is usually advised. For example, beyond skill diversity boards may look to have a range of genders, sexualities and ages. Research suggests that more than half of trustees believe greater diversity on charity boards will improve effectiveness. It should be clarified, though, that board diversity isn't about 'ticking off' all types of diversity - the board should still relate to the charity's core activities.

Trustees must speak up and challenge the status quo: Linking with the two previous points, there should be regular, ongoing dialogue between board members and trustees should be encouraged to speak up and raise any concerns they may have. Financial warnings can sometimes go overlooked, as with Kids Company, but it is imperative that there are systems in place that enables trustees to take remedial action at the earliest available opportunity. Determining the role of a trustee is a very serious matter and there should be a balance between charity chief executive autonomy and trustee involvement.

Financial lessons for trustees following Kids Company closure

The financial viability and suitability of charities is undoubtedly a major worry in the sector. A recent report - CVO's Financial Sustainability Survey Report – predicts that the sector will face a £4.6bn shortfall in annual income by 2018/19, if it is to simply maintain its current spending power. Following the closure, we looked at the financial lessons for trustees following Kids Company closure.

That article has been very popular on our website: www.hawsons.co.uk/trustee-advice-kids-company

Seek professional advice

In light of the events of Kids Company it is essential to emphasise the importance of seeking professional advice if you have concerns. Whether legal or financial, it's out there and it's there to help - don't be afraid to use it. For more information please contact your local office specialist.

Update on payments of gift aid from charity trading arms to the parent charity

There is a lot happening with Gift Aid at the moment and it is important that charities keep on top of the issue. If you haven't already, please sign-up to receive our charity e-news and we will keep you updated with any ongoing developments.

Update to CC35: Trading arms cannot make gift aid donations from reserves to parent charities

It has long been the situation that companies that are wholly-owned trading subsidiaries of charities donate all taxable profits to the parent charity and claim charitable donation relief but, following a technical report issued by the ICAEW, this guidance is now being reviewed.

When the ICAEW technical report – TECH 16/14BL - was first released in November 2014 we commented that the new guidance had taken a lot of charitable groups by surprise and raised more questions than it answered. A year on from the initial publication and many charitable groups are still unsure where they stand with regard to payments of gift aid from charity trading arms to the parent charity.

TECH 16/14BL attempts to clarify this accounting position

TECH 16/14BL attempts to clarify the situation and the accounting implications when a trading subsidiary of a charity donates all of its taxable profits to the parent charity and claims charitable donations relief on this amount.

Under the Charity Commission's guidance note CC35 (which was withdrawn in October 2014) such payments were not considered as distributions. Following concerns raised over the guidance, however, the ICAEW set out to review CC35.

Given the significance of this guidance to charities, the ICAEW sought legal advice on the matter. Following that advice the ICAEW confirmed that the payments in question are, in contrast to the regulators guidance note CC35, distributions. This being the case, these distributions can only be paid out of distributable reserves and therefore any payments made in excess of profits available for distribution are unlawful.

Do charities need to take action?

Simon Bladen, Charity Partner at Hawsons, commented: "This guidance has challenged what has been the status quo for many years and, even a year on from its release, it has left many charities in limbo. The key point to understand from the withdrawal of guidance note CC35 is that any wholly-owned trading subsidiaries of charities that donate all taxable profits to the parent charity and to claim charitable donation relief will be in breach of company law under the Companies Act 2006. Charitable groups should consider whether donations from the charity's trading arms to the parent charity were given in a year in which they may have been in excess of distributable profits. If you are unsure of your position you should seek professional advice."

For more information please contact Simon on slb@hawsons.co.uk or 0114 266 7141 or your local office specialist.

Recent housing case highlights complicated charity VAT exemptions

VAT is a constant focus in the charity sector and presents a wide range of different challenges and issues for charitable organisations. The unique and valuable VAT reliefs that are available to charities are detailed and tightly defined, as a recent housing example has shown.

Charity faces 'unexpected' VAT bill of extra £1m

A London-based charity is facing an unexpected VAT bill of £1m, following a new development to provide "move-on flats" to homeless people. The charity had anticipated a VAT bill of £250,000, but this additional VAT – five times more than what was expected – has now put the future of the charity in jeopardy.

Reacting to the decision on the charity's website Keith Fernett, the charity's Chief Executive, commented: "HMRC's application of VAT in this case is devastating to our work and to the vulnerable people we support. We believe we're being unreasonably penalised for accurately describing our operations despite not changing what we do. We have worked incredibly hard to deliver a level of service with a reliance on donations and relatively little government funding. We hope HMRC will reverse its decision, and allow us to continue making a huge difference to people's lives. Otherwise our work is at risk, and local authority services will be put under greater pressure."

The full statement on the charity's website: http://caritasanchorhouse.org.uk/blog/2015/09/15/vat-threat/

Charity VAT is one of the more complicated areas of VAT

Paul Wormald, Charity Partner at Hawsons, commented: "Although charities do have a unique tax status and gain through a number of attractive tax and VAT reliefs, it is still a common myth that charities don't have to pay VAT at all. They do, and the rules around charity VAT exemptions are detailed and tightly defined. Charity VAT is actually one of the more complicated areas of VAT. This case is just another example of how minor changes can bring about big tax bills."

"One of the most important charity VAT exemptions, particular for those working in the housing sector, is undoubtedly on the construction of new buildings. A charity can have new buildings constructed at the VAT zero rate if they meet certain qualifying criteria. Usually this means that the building must be used for relevant charitable purposes…with no business activity being carried out; that also generally includes the charging of fees. In this case an adjustment in the charity's description of services from a 'homeless hostel' to 'residential and life skills' is what brought about the additional VAT charge."

"The charity is currently appealing the decision, which may well end up in court. The charity VAT payable on the construction of new buildings is particularly complex and this case is not the only example of a charity facing unexpected tax bills. There have been a number of tribunals regarding charity VAT exemptions and VAT on new charity buildings in recent years. Just last year HMRC lost in its appeal over Longridge - a charity providing water-based activities on the VAT zero rating for a new building. Before that, Quarriers and Jeansfield Swifts, two other charities, have both won their cases to overturn the additional VAT at tribunal."

"All of this creates ambiguity for charities and increases the cost of building new developments – even if the case is overturned at court – because of legal fees and postponements in development. Those other costs could account for £500,000 alone. That is vital funding that could be spent directly for the public benefit."

"I would advise any charity to seek professional tax advice on the construction of new buildings before starting projects. Your VAT affairs are likely to be complex and professional advice could be the difference between an unexpected tax bill or a smooth development."

For more information please contact Paul on pw@hawsons.co.uk or 01302 367 262 or your local office specialist.

Are charities really ready for auto enrolment?

The law on workplace pensions has changed and by 2017 every organisation in the UK, including charities, must automatically enrol their employees. The ability of pension providers to provide solutions is becoming a real issue of capacity and, if you do not start preparing early, the cost of auto enrolment (which is your legal obligation) will soon build up.

Thousands of charities are approaching their staging date

As an employer you are responsible for enrolling all eligible employees into your scheme (and contributing to it). There are thousands of charities approaching their staging date, as the below table (a rough estimate) shows:

Staging date	Number of employees	Number of charities
Already passed	500+	215
Already passed	350-499	121
Already passed	250-349	209
Already passed	160-249	400
Already passed	30-159	3238
1st June 2015 to 1st April 2017	<30	22,000

Do not underestimate auto enrolment duties

Over 80% of charities will be approaching their staging date and will automatically enrol between now and April 2017. However, despite the national media coverage and breath of information available the concerns remain over whether or not charities are prepared, as Nigel Smith, Director of Hawsons Wealth Management, explains:

“I think some charities are underestimating how complex auto enrolment is and how much work is involved. There are a number of tasks you must complete before your staging date and we advise charities to start preparing nine months - ideally twelve - before this date. Some charities that already have workplace pensions in place might assume that their existing scheme will meet minimum criteria, but this is not always the case. In fact, in the majority of cases it does not. The ability of pension providers to provide solutions is also becoming a real issue of capacity and if charities continue to delay their auto enrolment preparations they will likely be charged a more expensive service fee. Adding this cost to the potential fines charities could receive, at a minimum of £400, and the costs of auto enrolment can soon add up for those that wait.”

For more details and advice please come to one of our free auto enrolment workshops: www.hawsons.co.uk/workshops

43% of large charities fail to report correctly

A new report from the Charity Commission (published on 19 August 2015) found that a large number of charities are under-reporting charitable expenditure and failing to submit accurate records in both their annual accounts and annual reports.

The report, which examined 188 charities which met certain criteria and had annual accounts which suggested that expenditure on charitable activities was less than 10% of their income, found that charities were making basic errors in annual reporting.

The report highlighted that:

- 57% were able to provide reasonable explanations for the low expenditure against income for the year in question.
- 43% had made errors in their annual returns or their trustees’ annual report and accounts for the year in question.

Michelle Russell, Director of Investigations, Monitoring and Enforcement at the Charity Commission, said: “…we are concerned that so many charities are making basic errors in their annual reporting. Aside from being a regulatory concern and undermining public trust in charities and the information they provide about their work and finances, it is likely to impact on how they are perceived by donors and potential supporters."

Richard Burkimsher, Charity Partner at Hawsons, said: “I would echo those comments made by Michelle; charities must ensure they are financially transparent, particularly in light of the ongoing Kids Company case. Trustees have ultimate responsibility to report on the charity’s finances and activities correctly. The regulator has also now confirmed it will step-up its work to promote guidance in these areas through various awareness campaigns. This is of course welcome news.”

Charity Health Check

How healthy is your charity?

If you answer no to any of the below questions, we would really like to meet you and share with you how Hawsons may be able to help you. We offer all new clients a free initial, no-obligation consultation, at a time to suit you. Whether we are appointed as auditors/advisers, or helping with a one-off exercise, we look forward to meeting you.

Questions

	YES
Do you feel that your charity has sufficient funds to undertake all of its aims?	
Have the trustees outlined a policy for reserves setting out the amount the charity needs to hold in funds?	
Have you reviewed the new charity SORP and understand how your charity's accounts may be affected?	
Do the charity's accounts present the best image to funders and the public at large?	
Are you making full use of the SORP exemptions to make the charity's published accounts easier to follow?	
Have you undertaken a VAT health check in the last 12 months?	
Does the charity have incoming resources that may be VATable?	
Are you confident that your charity is not undertaking trading activities?	
Are you aware of the tax laws relating to charities and are confident that the charity is complying with them?	
Do you find dealing with the charity's payroll and making HMRC returns a straightforward process?	
Do the charity's trustees know about their responsibilities and level of personal risk?	
Has the charity considered the potential benefits of incorporation?	
Have you reviewed the structure of the charity recently to check that it's still appropriate for the activities that it undertakes?	
Are you comfortable that the charity has control over all of its incoming resources and expenditure?	
Can the charity demonstrate how funds have been applied to its aims with relative ease at any given point in time?	
Does the charity have a funding plan for the next 12-24 months?	

Did you answer no to any of these questions?

Winter 2015

Registered to carry on audit work in the UK and Ireland and regulated for a range of investment business activities by the Institute of Chartered Accountants in England and Wales.

Sheffield
0114 266 7141

Pegasus House, 463a Glossop Road, Sheffield, S10 2QD

Doncaster
01302 367 262

5 Sidings Court, White Rose Way, Doncaster, DN4 5NU

Northampton
01604 645 600

Jubilee House, 32 Duncan Close, Moulton Park, Northampton, NN3 6WL

HLB International

INVESTORS IN PEOPLE

Your local specialist:

Sheffield

Simon Bladen
Partner
0114 266 7141
slb@hawsons.co.uk

Doncaster

Paul Wormald
Partner
01302 367 262
pw@hawsons.co.uk
@PAW_Hawsons

Northampton

Richard Burkimsher
Partner
01604 645 600
richardburkimsher@hawsons.com

Find out more about how Hawsons can help your charity.

Please call your local office or visit:

www.hawsons.co.uk/charities

Register to receive this edition quarterly:

www.hawsons.co.uk/newsletter