

2009 Budget – implications for churches and charities

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1 Introduction

The Chancellor, Alastair Darling, delivered his second Budget Speech on 22 April amidst the most difficult economic situation that most of us will have seen in our lifetimes. The Finance Bill, which contains 126 Clauses and 61 Schedules and runs to 443 pages, was published on 30 April.

Many of the measures announced are intended to stimulate the economy. The package of measures is to be financed by unprecedented levels of Government borrowing. The success or otherwise of this strategy remains to be seen as it unfolds over the coming years. But several things seem sure: We cannot expect to see any meaningful tax reductions from this or future governments – they will need to curb expenditure and, as opportunity arises, increase the tax take wherever they can; Sterling, although possibly very slightly undervalued at present, is likely to remain under pressure for some considerable time.

In this context, more than ever, churches and Christian charities will need to:

- Address the needs of members and the wider community, to provide hope and to demonstrate God's love in action;
- Protect the livelihoods of overseas missionaries that they support, as the depressed value of Sterling heavily impacts the local currency value of that support.

At the same time, charity income is under pressure. That said, early indications are that income of churches is holding up well. It is those that have a degree of reliance on legacies or investment portfolios, or who are planning to, or having to, sell property that are suffering the most.

These factors alone present the church with considerable challenges. But we believe that it is also a time of great opportunity – a needy world beginning to ask deeper questions. As people lose jobs and the things that they take for granted, they start to ask what it is that really matters in life.

Stewardship has produced a range of resources to help. For example:

<http://www.stewardship.org.uk/recession.htm> - recession page with links to further resources

<http://www.stewardship.org.uk/documents/LifeBeyondDebtStatement.pdf>

<http://www.red2black.org.uk/> - resources to help address debt in your church and community

From the church's point of view, no specific measures that were announced in the Budget this year necessarily stand out in their own right. However, the announcements on substantial donors are of significance to the charity sector in general and the church sector in particular.

2 Gift Aid

2.1 Gift Aid Consultation

There will be some disappointment in the sector that the Budget did not contain any major announcements on Gift Aid reform, following on from the Treasury's Gift Aid Consultation several years back. The Treasury continues to dialogue with the charity sector on these matters but they have found, in some cases, conflicting views. Despite

this, they intend to make major announcements at the time of the Pre Budget Report later in the year.

2.2 Gift Aid relief for higher rate taxpayers

The Treasury and HMRC are presently conducting research into the question of whether higher rate taxpayers are motivated to give by the additional relief that is available to them personally as donors. We suspect that the prevailing view in The Treasury is that it does not. If this is indeed the conclusion of their research, they are likely to conclude that the higher rate relief should be switched to the charity. The outcome should be known by the time of the Pre Budget Report.

2.3 Reduced time limit for gift aid claims

Although not strictly a Budget measure, it is important to note that Finance Act 2008 provided for significant changes to time limits for tax assessments and claims across all of the major taxes. Claims for gift aid relief will be affected from **1 April 2010**. From that date, all gift aid claims must be made within four years (rather than the present period of (broadly) six years). Note that the time limit for gift aid transitional relief will remain at two years.

The immediate impact of the changed time limits will depend on whether your charity is an unincorporated trust or incorporated as a company (for example, a charitable company limited by guarantee). The time limit for unincorporated trusts is aligned to the tax year (to 5th April) whereas the limit for incorporated charities is aligned to their financial year (accounts year). The following tables illustrate the changes for trusts and for selected accounting periods for charitable companies.

Charitable Trusts:

Year of claim	Existing time limit ¹	New time limit ²	Change
Year ended 5 April 2004	31 January 2010	31 January 2010	Unchanged
Year ended 5 April 2005	31 January 2011	31 March 2010 ³	Reduced by 10 months
Year ended 5 April 2006	31 January 2012	5 April 2010	Reduced by 22 months
Year ended 5 April 2007	31 January 2013	5 April 2011	Reduced by 22 months
Year ended 5 April 2008	31 January 2014	5 April 2012	Reduced by 22 months
Year ended 5 April 2009	31 January 2015	5 April 2012	Reduced by 22 months

¹ That is, five years after 31 January following the tax year of claim.

² The rules change on **1 April 2010**.

³ From 1 April 2010, the time limit for this year would have changed to 5 April 2009. So, a claim made on 31 March 2010 is competent (under the old rules) but one made the next day will be out of date (under the new rules).

Incorporated Charities:

Financial Year	Existing time limit ⁴	New time limit ⁵	Change
Year ended 30 April 2004	30 April 2010	31 March 2010 ⁶	Reduced by 1 month
Year ended 31 December 2004	31 December 2010	31 March 2010 ⁶	Reduced by 9 months
Year ended 31 March 2005	31 March 2011	31 March 2010 ⁶	Reduced by 1 year
Year ended 31 December 2005	31 December 2011	31 March 2010 ⁶	Reduced by 21 months
Year ended 31 December 2006	31 December 2012	31 Dec. 2010	Reduced by 1 year
Year ended 31 March 2009	31 March 2015	31 March 2013	Reduced by 2 years

Action Points

Make sure that your gift aid claims are brought up to date as soon as possible. Do you have taxpaying donors in past years that haven't given you a Gift Aid Declaration? Do you know why? Could it be that there is some further tax refunds waiting there for you? If your donors sign a Declaration now, you can claim tax for the last 6 years. But not for long!

If your standard Declaration wording already refers to the donor's gifts over the last 6 years, be prepared to change this (and any associated procedures) at the beginning of April 2010, so that it refers to 4 years.

2.4 Gift aid and non-domiciled individuals resident in the UK

This measure will affect relatively few individuals. Last year, the Government introduced a £30,000 flat rate charge on individuals who are not domiciled in the UK but live here. This £30,000 remittance basis charge can now be used to meet the requirement that a donor must have paid sufficient tax to cover their gift aid payments. This amendment is backdated to 6th April 2008.

3 Substantial Donors

Regular readers of our annual Budget Briefing Papers and e-mail bulletins will be aware of our campaign to obtain changes to the Substantial Donor legislation, first introduced in 2006. These rules were intended to counter abusive use of charity tax reliefs by a minority of major donors, who sought to use their position to 'control' a charity so as to receive undue personal benefit in return for their 'donation'.

Stewardship and other sector leaders have spent nearly two years working with HM Revenue and Customs, the Treasury and the Government to address the fact that perfectly innocent donations can be taxed. In these instances, the tax charge rests with the charity receiving the donations, which creates a major concern for the charity sector.

As well as taxing innocent transactions, the rules have proved to be completely unworkable, imposing unjustified compliance burdens on innocent churches and

⁴ That is, six years after the end of the accounting period.

⁵ The rules change on **1 April 2010**.

⁶ From 1 April 2010, the time limit for this year would have changed to a date prior to 1 April 2010. So, a claim made on 31 March 2010 is competent (under the old rules) but one made the next day will be out of date (under the new rules).

charities. In some cases, charities have had to turn donations away in order to protect themselves from charge.

The 2009 Budget has begun to address these shortcomings:

- A tax-avoidance motive test is to be introduced. This will mean that a charity will not be taxed unless there is an intention to abuse charity tax reliefs by making the donation.
- This is most welcome and is something that Stewardship has pressed for since the beginning of our campaign. Disappointingly, it will not be introduced until next year's Budget, meaning that we will have to wait until July or August 2010 before this becomes law. This is in order to allow HMRC and the Treasury to consult with us and others in the sector in formulating an *effective* motive test.
- For the moment, the rules stand as they were before the budget, with the exception of the following change:
- A 'substantial donor' is defined as one who makes tax effective donations (whether by gift aid or otherwise) of over £100,000 in any six year period. In fact, this means monitoring donations from a given donor or persons connected with them over a period of up to 13 years. The £100,000 threshold was increased to £150,000 from 23rd April 2009. The corresponding twelve month threshold remains at £25,000.

We will continue to work closely with Government, The Treasury and HMRC in ensuring that large innocent donations to charities don't fall foul of the legislation.

Action Points

Any church or charity that has donors who may fall within the substantial donor thresholds should, theoretically at least, take care not to enter into transactions with the substantial donor or any person connected with them that will lead to a tax charge on the charity. This includes, for example, the charity employing, or making a (charitable) gift to, the donor or a connected person, or to a charity of which the substantial donor and their connected persons are trustees. A full technical analysis is given in our Paper 'Gift Aid - The 'Substantial Donor' Legislation' available from the Briefing Papers Section of our website http://www.stewardship.org.uk/briefing_papers.htm

Since the Budget, HM Revenue and Customs have indicated that they will not use the Substantial Donor legislation to target charities unless there is tax avoidance behind the arrangements. We have asked the Government for a Ministerial Assurance to this effect and are hopeful that this will be forthcoming in the next few weeks. If this is received, charities will be able to adopt a softer approach, such as simply taking reasonable steps to satisfy themselves that they are not being used for tax avoidance purposes.

4 Personal allowances and tax rates

Whilst comment to changes in personal allowances is strictly beyond the scope of this Briefing Paper, we feel that it is worth mentioning a couple of changes that may impact either on the amount that an individual can make in gift aid donations or on their tax position as an overseas Christian worker.

4.1 Commonwealth citizens

Individuals who are neither British or EEA citizens nor tax resident in the UK normally have no entitlement to claim UK personal allowances. In limited circumstances, some

non-resident individuals, including overseas missionaries who have a property in the UK which is rented out, may benefit from UK personal allowances.

Where a person qualifies for personal allowances **solely** by being a Commonwealth citizen, HM Revenue & Customs have been advised that this is not compliant with the Human Rights Act. Legislation will, therefore, be introduced to withdraw this entitlement where it and any other income tax reliefs arise solely by virtue of being a Commonwealth citizen. Individuals affected are likely to be those from the Caribbean, or from islands in the Pacific or Indian oceans. They may however still be able to benefit through other means, for example Double Taxation Treaties.

4.2 Those earning over £100,000 per annum

From 6th April 2010, individuals with a taxable income of over £150,000 will be taxed at a new 'additional rate' of 50% (rather than 40%) and there will be no entitlement to the basic personal allowance. Dividends received by these individuals will be taxed at 42.5%.

From the same date, individuals with an 'adjusted net income' (ANI) of over £100,000 will have their entitlement to basic personal allowance reduced by £1 for every £2 that ANI is over £100,000. Adjusted Net Income is broadly taxable income less trading losses (if any) and the gross equivalent of pension contributions and gift aid payments. Using the 2009/10 levels, the personal allowance will be fully withdrawn once ANI exceeds £112,950. So, gift aid payments that reduce ANI from above £112,950 to below this figure will not only attract the usual tax relief but will mitigate against the reduction in personal allowance.

4.3 Gift aid – Up to 60% relief for 'additional rate' taxpayers

For the moment, the law provides that gift aid relief will be available to 'additional rate' taxpayers in much the same way as for higher rate taxpayers. In other words, the grossed up value of a gift aid payment will give the donor personal relief equal to the difference between the additional rate and the basic rate of tax.

Assuming that the 2009/10 tax rate thresholds apply, the following scenarios illustrate the Budget changes:

Example 1

Joe has taxable income of £160,000 and no deductions to arrive at 'adjusted net income' other than any gift aid donations that he may have made.

(a) If Joe makes no gift aid donations, he receives no personal allowance and pays tax of £57,520:

	£
Calculated as:	
£10,000 at 50%	5,000
£112,600 at 40%	45,040
£37,400 at 20%	<u>7,480</u>
	<u>57,520</u>

(b) If he makes gift aid donations of £8,000 net, his position becomes:

	£
Total income	160,000
Less: Gross value of gift aid donations (£8,000 grossed at basic rate of 20%)	<u>(10,000)</u>
Adjusted net income	<u>150,000</u>

He now pays tax only at 20% and 40%, reducing his total tax charge by £3,000 to £54,520. His gift aid donation of £8,000 has personally cost him £5,000 net whilst benefitting the charity by and further £2,000 basic rate relief⁷ on top of his £8,000 donation – **total tax relief of 50%**:

	£
£0 at 50%	0
£112,600 at 40%	45,040
£47,400 ⁸ at 20%	<u>9,480</u>
	<u>54,520</u>

Example 2

(b) Josephine has taxable income of £112,950. Out of this, she makes gift aid payments to charity of £10,360 (net), the grossed up equivalent of which is £12,950. The gift aid payments reduce her 'adjusted net income' from £112,950 to £100,000 completely restoring her entitlement to personal allowances:

	£
Total income	112,950
Less: Gross value of gift aid donations (£10,360 grossed at basic rate of 20%)	<u>(12,950)</u>
Adjusted net income	<u>100,000</u>

Now, she pays tax only at 20% and 40% and receives a full personal allowance. Her tax saving is therefore:

	£
Gift aid tax relief at 40% less 20% on £12,950 (gross)	2,590
Tax relief of 40% on restored personal allowance of £6,475	<u>2,590</u>
	<u>5,180</u>

So, Josephine's net gift of £10,360 has cost her only £5,180, whilst the charity she has supported has received an additional £2,590¹ in gift aid tax refunds. This represents **total tax relief of 60%** (charity benefits by £12,950 at a cost to the donor of £5,180).

5 Employment Tax

5.1 National Insurance Changes not mentioned in the Budget

These changes were announced in the Pre-Budget Report last November:

- The Upper Earnings Limit is increased to £43,875 from 6 April 2009 to align with the higher rate tax threshold (after taking account of the basic personal allowance). This will add approximately £420 to the annual contributions payable by employees with income at the new threshold.

⁷ Transitional relief of around 3% of the net donation is also available to the charity for until 5 April 2011.

⁸ The legislation provides that the donor's basic rate tax threshold is extended by an amount equal to the grossed up value of the gift aid donation made. The effect of this is that he receives personal tax relief equal to his top rate of tax (50%) less the basic rate of tax (20%).

- From 6 April 2011, the primary National Insurance Contribution threshold will be broadly aligned with the tax threshold.
- From 6 April 2011, the main employers' rate of National Insurance will increase from 12.8% to 13.3% and the employee rate will be increased from 11.0% to 11.5%.

It is curious that these measures were not mentioned in the Budget!

Action Points

Charities with employees need to incorporate these changes into their budgeting and forward forecasting plans. From April 2011, National Insurance Contributions will increase to a rate of about 25% (Employees: 11.5% plus Employers: 13.3%).

6 Value Added Tax (VAT)

6.1 Change in standard rate

As expected, the standard rate of VAT will return to 17.5% with effect from 1 January 2010. The good news is that the Government have not sought to increase the rate to a higher level as some commentators thought would be a real possibility, given the Governments plans for major increases in public borrowing.

Anti-avoidance rules are to be put in place to prevent artificial advancement of transactions to take advantage of the 15% rate, for example, by prepaying for goods or services that will not be made until 2010. The rules will apply from 25 November 2009 and will result in a supplementary VAT charge of 2.5 per cent.

The supplementary VAT charge will apply when the purchaser is unable to recover all of the VAT incurred and one of the following conditions applies:

- the supplier and purchaser are connected
- the supplier helps fund the pre-payment
- an invoice is issued for the pre-payment and payment of that invoice is not required for at least six months.

A supplementary VAT charge will also apply where any prepayment is made in excess of £100,000 for supplies made in 2010, unless it can be shown to be in accordance with normal commercial practice. This supplementary charge applies for any prepayments made with effect from **31 March 2009**.

Action Points

Most charities and virtually all churches are unable to recover VAT incurred on purchases of goods and services in full. As such, they should be aware of these provisions so that there is no unexpected supplementary VAT charge passed onto them by suppliers.

Any church of charity undertaking building work, for which a large prepayment has been asked, should take account of the new rules introduced with effect from 31 March.

6.2 Registration threshold

From 1 May 2009, the VAT registration threshold is increased to £68,000.

The new registration threshold will apply if:

- at the end of any month, the value of “taxable supplies” made in the past 12 months or less has exceeded £68,000; or
- at any time there are reasonable grounds for believing that the value of “taxable supplies” to be made in the next 30 days alone will exceed £68,000.

If, at the end of any month, a person’s taxable turnover in the past 12 months or less exceeds £68,000, but the authorities are satisfied that it will not exceed £66,000 in the next 12 months, registration will not be required.

From the same date, the deregistration threshold increased to £66,000.

Action Point

Most charities do not have taxable turnover because they do not make taxable supplies. For example, donation income is generally outside of the scope of VAT and service provision can be ‘non-business’. If in doubt, professional advice should be taken, as failure to register for VAT at the right time can give rise to significant penalties.

6.3 Refund of VAT incurred in other EU countries

A new electronic VAT Refund procedure is being introduced across the EU from 1 January 2010. This replaces the current system. From that date, VAT registered charities, established in the UK, that incur VAT in other EU countries will submit claims for refunds of overseas VAT electronically to HM Revenue & Customs rather than to the Member State where the VAT was incurred.

Other related changes:

- Claims will be able to be submitted up to nine months from the end of the calendar year in which the VAT was incurred, rather than the present six months
- Tax authorities will have four months, rather than six months, to make repayments, unless further information is requested, in which case the deadline extends up to a maximum of eight months
- the Member State of Refund will pay interest in cases where the charity meets all its obligations, but deadlines are not met by the tax authorities
- all EU Member States will be required to afford a right of appeal against non-payment in accordance with the procedures of the Member State of Refund.

Action Point:

Any charities affected by this change should make sure that they are aware of the new arrangements, which should provide great benefit in simplifying an otherwise time consuming and cumbersome process.

7 Tax Management

7.1 Penalty regime for late filing and late payment of tax

PAYE penalties

The Finance Bill 2009 reforms the law on penalties for late filing of tax returns and late payment of tax across the major taxes. The most significant of these reforms for charities are the penalties that will apply for late payment of ‘in year’ PAYE (the monthly or quarterly PAYE payments made by employers which are due by the 19th of the month following the payment of the related wages or salaries).

Implementation requires changes to HMRC's computer systems and is to be staged over a number of years. However, PAYE penalties will be the first to be implemented, from April 2010. These will be structured as follows:

- the amount of the penalty will depend on the number of defaults in any 12 month period. The first time the taxpayer defaults, they will not receive a penalty;
- a second late payment and any subsequent failures in the default period will attract a penalty of 2 per cent of the tax unpaid rising to 5 per cent of tax unpaid;
- further penalties of 5 per cent of any amounts of tax still unpaid at 6 and 12 months

The penalty can therefore reach 15% of the tax due.

Late payment penalties will not be charged during an agreed time to pay arrangement with HMRC unless the taxpayer defaults or misuses the arrangement.

Action Points

In a time of recession and where cash flow is under pressure, churches and charities should make sure that priority is given to putting sufficient funds aside each month to settle later PAYE liabilities on time.

For some, this will mean putting in suitably robust administrative procedures to ensure that payments due are diarised and calculated in good time, that cheques signatories are available at the right time etc. to avoid incurring unnecessary default notices and penalties.

Stewardship's payroll service (http://www.stewardship.org.uk/payroll_bureau.htm) is another way of gaining piece of mind for your payroll compliance.

8 Sundry

8.1 Hardship Loan Fund

Following the announcement in February of a £42.5m Action Plan, the Budget announced a new £16m hardship fund (known as the Targeted Support Fund) which opened on 29th April. This is a one year programme focused on the fifty areas of England that are most at risk of increased deprivation during the recession. Local services in those areas, with an annual income of £30,000 to £250,000, are eligible to apply for grants of between £10,000 and £40,000. The fund is targeted at third sector organisations providing front line services that have been hit by the recession, either through an increased demand for their services or because of cash flow difficulties.

Grants are to be given for recession focused services under one of the following themes:

- Information, advice and guidance (housing, financial, debt, legal advice and support)
- Employment and employability (training and skills development related to finding employment)
- Health and wellbeing (mental health, lifestyle, relationship breakdown, counselling, domestic violence and substance abuse).
- Further information and application details can be found at:

http://www.cabinetoffice.gov.uk/third_sector/news/news_stories/090429_targeted.aspx

Action Point

Churches or charities working in these fields should follow the above link to establish eligibility.

8.2 Social Investment Bank

The Office of the Third Sector is to consult over the summer on the design and functions of a new Social Investment Wholesale Bank. The aim is to increase the supply of investment in the third sector and strengthen demand for finance.

Action Point

Watch this space!

8.3 Common Investment Funds (CIF's) and Common Deposit Funds (CDF's)

The Government will consult shortly in conjunction with the Charity Commission on ways to bring these funds more fully under the FSA's regulation, whilst preserving their existing tax reliefs. This is a topic which has been under discussion for some years. No doubt the recent instability in financial markets has brought it to the top of the agenda again.

This is more an issue for those who run CIF's and CDF's, in as far as regulation by the FSA is inevitably going to lead to an increased cost of administering these funds at the expense of the charity investor. The key issue for the Government and regulators is to achieve a right balance between regulatory cost and the benefits of protection to the investing charities.

Action Point

Investors in these funds should keep an open mind on the impact of regulation should it come and whether or not there will be any material adverse impact for them.