Submission to HM Government for Budget, June 2010

Published: May 2010

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1 INTRODUCTION

This Paper sets out **five key submissions** to HM Government, in respect of the forthcoming Budget covering tax measures affecting the charity sector. As the Official Briefing Note accompanying the Queen's Speech observed:

"Social enterprise, charities and co-operatives can play a valuable role in the running of public services. They reach and engage communities, understand need and pioneer new approaches, which have a social, environmental and economic impact. There is scope for this role to be increased significantly.

With increased pressure on public services, the need to improve outcomes and to reduce national debt, there is a need for radical reform of public services. Social enterprises, charities and co-operatives are one means by which to address these challenges."

It is in this context that Stewardship makes this Budget Submission.

As a charity ourselves, we are a significant gift aid user. We currently receive over £50 million a year in gross gift aid donations. But, more importantly, we are also a representative umbrella body for the Christian charitable sector. We provide a range of professional services and support to Christian churches and charities, including advice and training on new and existing law and regulation. Our mission purpose is to share knowledge and encourage good practice in law and finance. The staff team include qualified accountants, a chartered tax adviser and a lawyer, as well as other professionals.

The author of this Paper has been a member of various HMRC and HM Treasury Consultation Groups, most notably serving as a representative member of the Treasury's Gift Aid Forum, and the HMRC Substantial Donor Working Group.

Recognising that this first Coalition Budget is an emergency Budget, we have limited our Representations to those matters that are:

- already well advanced within Sector, HM Treasury and HMRC thinking, or
- of key concern, as a result of Manifesto pledges of either of the Coalition partners, or
- a perceived threat to the effective delivery of public services by charitable organisations.

2 BUDGET REPRESENTATIONS

2.1 Substantial Donor legislation (Finance Act 2006, s54)

In July 2007, we set out in representations to HMRC and HM Treasury considerable concerns that we had in relation to the operation of the substantial donor legislation contained in Section 54 Finance Act 2006. We considered that the costs and uncertainties brought about by this legislation to law abiding charities and their donors was wholly inappropriate. Since then, much has been achieved, most notably the publication, in July 2008, of an HMRC Public Consultation to review this anti-avoidance legislation, and the subsequent establishment of a working party consisting of members of HMRC Charities Policy and Anti-Avoidance Group staff working together with key charity sector representatives, including Stewardship, to frame replacement legislation (which has the working title of the 'Donor Value Extraction Rules').

We are grateful for HMRC's willingness to engage with the charity sector over the last few years and now urge the new Government to complete the process by enacting the replacement laws in their first Budget in 2010, whilst repealing the poorly targeted rules of Finance Act 2006.

There are clear advantages in early action:

- HMRC want the new workable legislation, rather than the existing legislation which is not fit for purpose;
- The charity sector, and major donors, who have been represented on the HMRC Working Group, wholly support the new legislation which will avoid the inappropriate costs associated with compliance with poor legislation.
- The new Government will be able to demonstrate decisive action in the public interest in an area that is non-controversial.
- The new Government will achieve credit for remedying a defect that the previous administration failed to do, even though the matter was first raised with them in 2007.
- The new rules already have the support of the last administration, meaning that agreement in the relevant Finance Bill Standing Committee should be a straightforward matter.

Stewardship requests HM Government to:

- **Authorise HMRC to re-engage with the Sector Working Group towards agreeing the final points of the draft replacement legislation in good time for the output to be included in the Finance (No. 2) Bill.**
- **Include amending legislation in Finance (No. 2) Bill 2010 to repeal the existing Substantial Donor Rules and introduce the new Donor Value Extraction Rules.**

2.2 Gift aid: composite rate proposal

HMRC and HM Treasury sponsored research, published on 15 December 2009, suggested that there may be benefits to the Charity Sector in abolishing gift aid relief at the higher rate of tax and replacing it with a composite rate for all gift aid donations. The Liberal Democrat pre-election Manifesto adopted the introduction of a composite rate as Party policy and referred, somewhat bizarrely, to higher rate relief as 'tax avoidance'.

Debate within the Charity Sector has cast serious doubt over the benefit of any composite rate scheme. Sampling constraints within the research undertaken means that there is no reliable evidence to predict the behaviour of major donors, should a composite rate be introduced. The research itself indicated that there would be 'winners' and 'losers' within the sector, but the identity and extent of 'wins' and 'losses' could not be reliably determined.

Stewardship therefore invited a selection of our larger donors (who had either given a one off donation to us of at least £10,000 or who regularly give us at least £500 per month) to take part in an anonymous online survey. 155 donors responded with the following headline results:

Proportion who claim the higher rate relief

- 98.0% claim the higher rate relief on their gift aid donations
- 1.3% said that they didn't know how to claim
- 0.7% said that they did not claim as their gifts were made under payroll giving

Asked if the amount that they give is affected by the tax relief received:

- 74.6% said the amount they give is influenced by the fact that the *charity* receives tax relief
- 83.2% said the amount they give is influenced by the fact that *they themselves* receive tax relief

If composite rate relief were introduced in place of higher rate relief:

- 66.0% said that they would *reduce* their giving
- 32.6% said that they would give the same *net* amount
- 1.4% said that they would *increase* their giving

Of those that would reduce their giving if a composite rate were introduced in place of higher rate relief:

- 60.9% said that they would reduce their giving by an amount that would broadly compensate them for the loss of higher rate relief
- 31.5% said that they would reduce their giving by an amount that is less than the lost higher rate relief
- 7.6% said that they would actually reduce their giving by an amount that is more than the lost higher rate relief

A number of our donors were not aware of the proposals until we invited them to participate in the survey and called us or e-mailed in response, to express their alarm and generally talk around the issues arising.

These results were submitted to HM Treasury's Gift Aid Forum.

Our survey provides strong evidence (supported by arts and educational sector charities in particular) that introduction of a composite rate relief in place of higher rate relief will lead to a fall in giving to charity. The research undertaken by researchers from Bristol and Warwick Universities on behalf of HMRC/HM Treasury did not have ready access to larger donors and therefore its conclusions may not be representative of this donor class. This is recognised in the research report which had to postulate data and donor behaviour for those that give more than a couple of thousand pounds per annum.

It seems to us that the risks of introducing a composite rate are just too high relative to any perceived benefit:

- The risk that income to the charity sector (or parts of it) will suffer a fall in net income (resulting from a change in fiscal incentives rather than from external economic factors)
- The risk that the change is not revenue neutral to the Exchequer.

Stewardship requests HM Government to:

- **Drop any plans for the introduction of a composite rate of tax.**
- **Retain the higher rate tax relief on gift aid (and other charitable gifts) as an effective incentive to generous philanthropy.**

2.3 In Year Gift Aid Claims

Although not strictly a Budget matter, it is convenient to make representations here in relation to Regulations presently under consideration by HMRC.

Finance Act 2010, Schedule 8 contains powers for HMRC to limit 'in year' gift aid claims by charities. We understand that this measure is designed to limit very small and sometimes frequent small claims by some charities, which are wholly cost ineffective to process. We wholly support any move to eliminate unnecessarily trivial gift aid claims.

However, this needs to be balanced against the cash flow difficulties that could arise for small charities if the level at which an in year claim is permissible is set too high, or the frequency with which a claim is made is unduly restricted.

Of all the (March 2010) Budget measures, this one generated the most concern amongst our constituent churches and charities. Our conclusions from the representations made to us is that a gift aid claim of just £1,000 per month can be the difference between a church worker receiving their salary or not, since many churches (and Christian charities) simply do not hold reserves enabling them to fund salaries pending receipt of their gift aid claims.

Stewardship requests the relevant Ministers to:

- **set a limit which is no higher than £1,000 for in year Gift Aid claims.**

We believe that a single monetary limit (with no limit on frequency) will address the problem of trivial claims. However, if a frequency limit is to be introduced, we consider that this should not be less than monthly.

2.4 Gift Aid: Transitional relief

Gift aid transitional relief was introduced to compensate charities for the fall in the value of gift aid when the basic rate of tax was reduced from 22% to 20%. The Government undertook to look into ways of increasing the take up of gift aid and launched a Consultation on Gift Aid in June 2007. To date, little by way of tangible developments has emerged from this initiative. In early 2010, HM Treasury set up a Gift Aid Forum to look into ways of improving the Gift Aid system. This was due to report at the end of September 2010.

To allow time for the identification and introduction of more tangible means of increasing the take up of gift aid, we request the Government to extend the present transitional relief beyond the current end date of April 2011. This will enable valuable volunteer capacity to be utilised to its full potential, and community activity and public services delivered by charities to continue, without the additional financial burden otherwise created by its withdrawal.

2.5 VAT: rate and VAT base

Although no specific announcement to this effect has been made, there has been wide speculation that the rate of VAT may need to be increased, if not in this Budget, then potentially during the course of the present Parliament.

It is important to be clear that any increase in the VAT rate has a direct and immediate impact on the charity sector. Charities are rarely able to recover all of the input VAT that they incur, and in many cases, the recovery rate is nil where, as is often the case, the charity achieves its purposes through 'non-business' activity.

Any increase in the VAT rate will mean charities are less able to deliver the public services that this Government has acknowledged they will need to increasingly rely on in this time of austerity.

Equally, any move to reduce zero rates or otherwise alter the VAT base will have an adverse impact on the charitable sector.

Stewardship requests HM Government to:

- **to carefully consider the impact on charities of any plans that they may have or may develop to raise tax though VAT changes.**
- **Consider compensating relief to charities if a rise in the rate of VAT is proposed. We and colleagues in the sector would be pleased to assist in the design of such a relief, mindful of the constraints of Europe in framing this.**
- **to resist any narrowing of zero and reduced rates, as they apply to charitable activity.**