



"BEST ALL-ROUND CHARITY AUDITOR" - WINNER 2006
"OVERALL AUDIT SERVICE AWARD" - WINNER 2007
Annual *Charity Finance* survey

not for profit | school fee composition payment

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introduction

This fact sheet outlines the use of fee composition payments and refers to various factors to be considered in relation to the establishment and operation of fee composition schemes. The common factor is that a capital sum is paid as an advance payment of school fees, the amount of the payment being calculated by discounting the actual amount of the fees over the period covered by the advance payment. The amount of fees to be covered would be predetermined, although it need not be the same throughout the period. Payments can be made at the time of entry or before that time. There can be both personal taxation and inheritance tax advantages to parents and others in making fee composition payments.

factors affecting schools

There will be considerable differences in the approach of schools of different sizes and serving different age groups to the establishment or operation of a fee composition scheme. A senior independent school would normally be substantially larger than a preparatory school and, due to the age of pupils, is likely to have fee composition funds available for a longer period than a preparatory school. The particular circumstances of schools will also vary and this can affect the use to be made of funds received, and therefore the advantages or disadvantages of operating a scheme. In general terms, unless substantial funds are held under a fee composition scheme so that economic use of these can be made over a reasonable period, the costs of administration of a scheme are likely to outweigh the advantages that might be obtained. Successful schemes are normally found where substantial funds can be dealt with; it is then economical to invest the monies for suitable periods to earn a sufficient margin of return, over and above the discount given, to provide a useful benefit to the school.

There may, however, be circumstances where the school can make use of the funds without their investment. Schools may use the funds to reduce their net borrowings and so benefit from the greater margin between the borrowing and the discount rates. Many small preparatory schools which do not operate on an overdraft have considered that the gains to be made operating their own composition scheme are insufficient to

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cover the administration involved in running the scheme. They may prefer to bank the payment in their main bank account rather than maintaining and reporting a separate balance to match the liability.

essentials of a fee composition scheme

The essential factor to be taken into account in such a scheme is that the monies received for fee compositions should be regarded as if held in trust to meet the future fees covered by the scheme, whilst at the same time there is always a potential liability for repayment (full or part) should a pupil not come to the school or not stay for as long as expected. Circumstances may therefore arise where immediate repayment of part of the fund may be required, and a school should always ensure, where a significant level of compensation payments have been received, that funds for such purposes are readily available. It is normally considered that this can only be done either by holding a separate investment of fee composition monies or at least a separate bank account as referred to below. However, it should be noted that where such ad hoc payments are not held in a separate trust, the liability to the parents will rank alongside other unsecured creditors of the School. As with other fee payments, there is no entitlement to income tax relief through the gift aid regime. Where repayments are made, income tax will have to be deducted from the interest element.

fee composition scheme terms

Form FC1 outlines the terms for a fee composition payment. This would be accompanied by an application form FC2 and commonly by a table giving the rates of fee composition required for given periods and amounts of fee. The table will depend on the rate of discount offered by the school and this can vary appreciably, depending on the school's financial position. The rate of discount may also vary from time to time depending on prevailing interest rates. This will, of course, only be profitable to the school where the yield on the funds received or savings on the interest cost of borrowings will cover not only the discount given on fees but also the costs of administration.

use of fee composition scheme funds

In certain circumstances a school may find itself in a position to obtain a substantial effective yield on fee composition monies by holding them in a separate bank account, the credit balance on which is, by agreement with the bank, granted a full offset for interest calculation purposes against an overdraft on another account used for other school purposes. As an example, where a school has had a successful appeal and wishes to carry out the expenditure on appeal objectives in advance of receipt of donations under deeds of covenant and/or gift aid, it may arrange for an overdraft to finance the immediate expenditure. A fee composition account arranged on a "back to back" basis with such an appeal account overdraft for interest purposes will effectively

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be earning interest equal to the rates charged on the bank overdraft and thus likely to show a substantial saving to the school.

This is probably the most advantageous use of fee composition monies for a smaller preparatory school, although it is essential to ensure that the overdraft borrowing is not made dependent on the maintenance of a fee composition account credit balance, so that fee composition monies can be withdrawn at any time. Withdrawals would be made each term to transfer the discounted fees for the term from the fee composition account to the school's main operating account, and the discount would be written off as a finance charge each term.

If the above circumstances do not apply then fee composition funds will either have to be held on ordinary deposit, where rates may not be very favourable as compared with discount rates, or alternatively invested in suitably dated securities with the inevitable cost of dealing in what may be rather small sums. In these circumstances only a scheme with substantial funds available is likely to be economic.

use of separate trusts

Certain large schools hold their fee composition scheme sums in a separate trust. This has the advantage of providing greater protection through ring-fencing. However, the disadvantage to the school is that the trust will not have the benefit of untaxed investment income as it is not a charity.

about haysmacintyre

haysmacintyre, Chartered Accountants and business advisers, works with over 550 charities and not-for-profit organisations in the UK and overseas. Our services include the full range of audit, tax, VAT and comprehensive advisory services. Our multi-disciplinary specialist team has extensive sector experience working for a diverse range of charities. We are based in one location which ensures an integrated and comprehensive approach to our clients' requirements.

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EXAMPLE SCHEME FOR A SCHOOL FEE COMPOSITION PAYMENT

The Governors have decided to offer parents or guardians of pupils entered for, or already at the school, the opportunity of paying fees in advance by a single composition sum, calculated in accordance with the table attached hereto. This allows a discount on standard termly fees for the advanced payment. The method may have personal tax advantages as there is no inheritance tax liability on the composition sum if it is paid by a parent or other person.

Under the conditions of Fee Composition payments, parents have the option of covering either the whole or a proportion of the termly fee and, for consecutive terms, to cover either the whole of the pupil's schooling at the school or, alternatively, a limited period.

The conditions applying to fee compositions are set out below, and a form of application to enter the Scheme is attached, but it is advisable for the actual amount payable to be confirmed with the Head or Bursar before payment is made, as the rate of discount and therefore the fee composition sum may be varied from time to time.

Conditions of Fee Composition Payment

1. The fee composition will cover the chosen amount of fees for the period requested, and the parent will be responsible for any excess of the termly fee account over the amount covered by the fee composition. If the termly account is less than the fee composition the balance will be refunded to the parent. The fee composition does not therefore cover subsequent increases in fees charged unless these are taken into account in fixing the amount of the fees to be covered.
2. If a child for whom a fee composition has been paid does not come to the school the amount of the fee composition [and interest at an appropriate rate] will be refunded in full.
3. If a child for whom a fee composition has been paid does not remain in the school for the period covered by the fee composition agreement, whether due to starting after the expected date or leaving early, there will be refunded for each complete term by which the child's schooling has fallen short of the number of terms covered by the fee composition agreement a proportion of the original fee composition sum to cover the number of terms non-attendance as compared with the full number of terms. If, however, a child is removed without due notice one term's fees will be deducted from the refund.

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4. No adjustment in the fee composition sum will be allowed in the event of a child's date of entry being deferred after the sum has been accepted by the school, but the arrangement will be extended to cover the full number of terms for which the composition has been paid, and if appropriate, a proportional repayment calculated as in 3 above will be made in the event of the period of schooling being less than the period originally chosen.
5. In the event of the general fees being increased, a parent or guardian may pay an additional compositional fee to increase the amount of fees covered by the arrangement, the additional composition fee being calculated in accordance with the table of compositions current at that time.

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FC2

EXAMPLE APPLICATION FOR A SCHOOL FEE COMPOSITION PAYMENT

NAME OF PUPIL: _____

General Fee to be covered by Composition Payment £ _____ per term.

PERIOD to be covered

FROM _____ Term 20__

TO _____ Term 20__

In respect of my son/daughter above I wish to adopt the Fee Composition arrangements set out in the Form FC1 and agree to the conditions set out therein.

I enclose a cheque for £ _____ made payable to _____

Signature of Parent or Guardian

Address: _____

Date _____

Where payment is not made by Parent or Guardian, please also complete below:

Signature of Payer _____

Relationship to pupil _____

Address _____



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