



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

schools' | briefing

new reporting requirements | employment status and the Demibourne effect | sponsoring academies
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editorial



Welcome to this Autumn 2008 edition of Schools' Briefing; I hope it won't keep you awake at night!

We are grateful to Bates Wells & Braithwaite for their article on the Corporate Manslaughter and Corporate Homicide Act which is

now in force and has potentially serious implications for governors. We also include a note about reporting serious incidents.

The hoops schools have to jump through when carrying out non-charitable trading are summarised in an account of a recent assignment, and we consider the commercial implications of sponsoring academies, an area where a few schools are gaining a lot of publicity.

We start with an update on reporting requirements in light of the further guidance on the SORP and public benefit. Do contact us if you have any questions concerning any of the matters raised.

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new reporting requirements



The Charity Commission has issued guidance on public benefit along with further guidance on the SORP through Information Sheet – Number 1. Both impact the statutory accounts of independent schools.

Reporting requirements of the public benefit guidance

For accounting periods ending on or after 31 March 2009 governors will be required to address public benefit within their Governors' Report. Many independent schools did this in their report last year and more are expected to follow suit in 2008.

To summarise public benefit disclosure requirements:

- Confirmation that governors have paid due regard to the Charity Commission's guidance on public benefit in deciding what activities the school should undertake.
- Explanation of the significant activities undertaken in order to carry out the school's aims for the public benefit.
- Explanation of the school's achievements in respect of public benefit measured by reference to its aims and to the objectives set by the governors.

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Smaller charities which are below the audit threshold may disclose less detail in their report.

The Charity Commission believes that these new reporting requirements build on existing conditions, which means the current structure of the Governors' Report should not be significantly affected.

Impact of the Charities SORP 2005 information sheet

Information Sheet Number 1 was issued by the Charity Commission earlier this year following a review of the application of the SORP and to provide guidance so as to assist those preparing charity accounts.

The information sheet covers the following areas which are applicable to independent schools:

Interest and finance costs

Previous sector guidance misinterpreted the SORP in stating that interest and finance costs be disclosed within costs of generating funds. However, in most cases interest is paid on overdrafts to fund working capital requirements or on loans to finance building projects, which relate to charitable activities.

The guidance recommends that interest costs be allocated to that activity. Where interest costs cannot be directly allocated to the relevant charitable activity, they should be apportioned on a reasonable basis as with other support costs.

Investment manager's fees

Per SORP 2005 all incoming resources should be reported in the accounts gross. In the past this has sometimes caused problems for schools that hold investments in collective investment schemes, where it is difficult to identify the investment manager's fees. The Charity Commission recognises this by advising that where it is not practical to identify actual or a notional apportionment of costs with reasonable accuracy, then investment income can be reported net.

Business review

Companies Act 2006 introduces the requirement that Governors' Reports of medium and large incorporated schools include a business review. Charitable companies applying the SORP's recommendations are likely to already meet the requirements of this business review. However, many may need to include an expanded narrative on the principal risks and uncertainties that they face.

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Further details of both publications can be found on the Charity Commission website.

employment status and the Demibourne effect



Employment status is a notoriously grey area as there is no definition in tax law for either employment or self-employment. Until recently, where employment status was an issue as part of an Employer Compliance Review, generally an

equitable settlement was reached, and usually an amount in excess of the tax liabilities already met by the individual and employer's NIC would be settled. This has been complicated in recent months because of the outcome in the Demibourne case.

In the Demibourne case, the special commissioners held that the employer was liable to pay the due amount of PAYE/NIC on an employee who had previously been treated as self employed, ignoring the tax already paid by the individual.

After negotiations, HMRC announced in March 2008 that the PAYE regulations would be amended so that where such an issue did arise the income tax and Class 2 and 4 NIC paid by any individual could be taken into account as part of a review and therefore only the balance of liability settled. The same HMRC guidance has also pointed out however that any penalties charged would be based on the full amount of PAYE and NIC due. Internal HMRC guidance was to follow in April; this has not as yet been forthcoming.

There are therefore a number of cases sitting with Compliance Officers that remain outstanding. The recommendation by HMRC at the moment is that liabilities agreed as part of a review should be paid to stop interest accruing even though the review and the level of penalties could not be settled.

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sponsoring academies – commercial implications for independent schools



Academies are now part of the educational landscape. There are 83 in existence and Schools Minister, Lord Adonis, recently stated that the government will have “no difficulty” in going beyond 400. The sponsors of an

Academy supply expertise and potentially funding, and have a key role in governance, setting goals and ensuring community involvement.

Is there a role for independent schools as sponsors? Clearly yes, as some are already involved. For example, the United Church Schools Trust, which owns and manages 11 independent schools, is the lead sponsor of 13 academies through a subsidiary charity, The United Learning Trust (ULT). It is now offering its expertise to other schools such as Marlborough College which will co-sponsor Swindon Academy by sharing its teaching skills, facilities and resources, leaving ULT as lead sponsor to deal with the academy’s operation and management. Other schools involved in sponsorships include Dulwich and Wellington.

No financial contribution is now required from sponsoring schools, an important factor given that parents would be concerned to see their cash funding another school. The government wants the independent sector’s DNA, not necessarily its money. Independent schools must, however, consider the risks and rewards.

Involvement with an academy is a potentially attractive outreach strategy, particularly given public benefit considerations. Research indicates that academy students come from more impoverished homes than the national average. The sponsoring school is likely to provide expertise benefiting a much larger group of less well-off students than it could afford to do by providing bursaries.

However, significant staff and governor time is required in setting up and running the project. Parents will need to be satisfied that their child’s education does not suffer due either to management being distracted, or by a dilution in the school’s service.

Proponents may argue that non-financial costs are offset by the benefits of working with the academy, which may indeed also provide useful insights for the sponsoring school. The relationship is not necessarily a one-way street. However, academies are not the only way of engaging with other schools and the community. Successful partnerships with other state schools, and with youth and community groups exist countrywide and make a significant contribution to society.

There are other downside risks to be considered, most notably the reputational risk if the academy fails. Ultimately sponsors must mitigate the risk of failure through clear strategy, good governance and effective project management; although a cynic may argue that the risk of failure will increase as academies become more numerous and less oversubscribed. Furthermore, the agreements entered into with the DCSF should make clear that the sponsoring school has no underlying financial commitment and provides no indemnity in relation to any unexpected costs.

The sponsoring of an academy represents an opportunity for an independent school to contribute to the wider public benefit and a number have taken this up. Whilst there will be many schools which conclude that sponsorship is not for them, consideration of academies should be on everyone’s agenda.

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“The sponsoring of an academy represents an opportunity for an independent school to contribute to the wider public benefit and a number have taken this up.”

guest article



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They act for large and small commercial organisations, regulatory and other public bodies and individuals, but they are best known for their work with charities and social enterprises.

corporate manslaughter and corporate homicide

How does the new law affect charities?

Known as the “corporate killing law” the Corporate Manslaughter and Corporate Homicide Act 2007 (the Act) came into force on 6 April this year. Charities both large and small should note the implications of the Act and the added risk of criminal prosecutions they may face.

The new offence of “corporate manslaughter”

Under the old law, pre 6 April 2008, it was usually only smaller companies who could be prosecuted for manslaughter offences as it was a requirement that a senior individual of a company needed to be personally involved in the decision or activity that led to the death for prosecution to occur. In larger companies it was unlikely that senior individuals, such as Directors, would be directly involved in the activity that led to the fatal accident.

Under the new law, an offence of “corporate manslaughter” has been created (“corporate homicide” in Scotland) under which larger organisations can no longer escape liability for management decisions that lead to death(s). The key elements of the offence are that an organisation will be guilty of an offence if the way in which its activities are managed or organised cause a person’s death and amounts to a “gross breach” of a relevant duty of care. The organisation will only be guilty if the way in which its activities were managed or organised by the senior management is a substantial element in the breach.

What does this mean in practice for charities?

The Act applies to a range of organisations including charitable companies, community interest companies and charities’ trading subsidiaries. It is unlikely that charitable unincorporated trusts and associations will be caught by the Act (unless they fall into another category listed in the Act such as an employers’ association).

a recent case study – non charitable trading



A School’s turnover from non-educational activities was increasing year by year and it seemed that it would soon exceed both the turnover limit for the small trading tax exemption and the VAT registration threshold. The School

felt that it should explore the option of transferring its non-exempt activities to a trading subsidiary and haysmacintyre was commissioned to undertake a corporation tax and VAT review.

Although a superficial review of the accounts and underlying records would give the impression that the School might soon run the risk of falling within the charge to corporation tax and also breach the VAT registration threshold, our initial interview brought to light various other income streams, raising the

concern that the various limits for exemption might have already been breached a number of years ago, potentially giving rise to significant VAT and tax liabilities, plus penalties.

The VAT threshold was indeed found to have been breached some time ago and we set about formulating a plan of action in order to minimise the consequences to the School. The income streams were considered in detail and we were able to assist in identifying zero rated and exempt transactions in connection with sale of school uniform, income from functions and the hire of sporting facilities that could be excluded from the calculations.

We also advised on claiming VAT on pre-registration stock and expenses together with a proportion of overheads under the partial exemption rules so as to minimise the VAT liability. We oversaw the reorganisation and disclosure process, ensuring that the maximum penalty discounts for full and up-front disclosure were obtained.

A “relevant duty of care” will be owed by a charity whenever a duty is owed in negligence. This covers a wide range of circumstances including:

- the duty owed by a charity to its employees;
- the duty owed by a charity owning premises to visitors to those premises;
- the duty of a charity offering care services to its beneficiaries; and
- the duty of a charity organising outdoor activities to its volunteers and beneficiaries.

What are the penalties under the Act?

If found guilty, a charity could be liable to an unlimited fine, a publicity order (requiring the charity to publicise the conviction and/or the sum fined) or a remedial order, requesting the charity to take steps to address the cause of death. In particular for charities, any publicity order could be hugely damaging for the charity’s reputation and brand.

What steps should charities take to protect their position under the Act?

Charities should take the following steps to protect their position in light of the Act:

- Re-examine how the charity deals with risk. How, for example, is the risk of death minimised in the charity’s activities?
- Ensure the charity is complying with all current laws relating to safety such as health and safety and occupiers’ liability legislation. Failing to do so could lead to liability under the Act.

- Ensure that all employees, volunteers, trustees and beneficiaries are provided with the necessary training to prevent fatal accidents occurring.
- Examine the charity’s insurance to check that the costs of defending any prosecutions under the Act and the possible damage to the charity’s reputation are covered. Charities should note that if the organisation is found guilty of an offence and a fine is imposed, no insurance cover would be available. Charities should also check trustees and senior managers’ insurance cover and whether the costs of their investigations under the Act would be covered.

Although it is unclear yet exactly how the courts will interpret the Act, charities should treat the advent of this new legislation as a prime opportunity to ensure that risk is managed effectively within their organisations and that all necessary steps are taken to prevent fatal accidents occurring.

For more information on charity indemnity insurance see CaSE Insurance at www.caseinsurance.co.uk – specialist insurers for charities and social enterprises.

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A similar exercise was undertaken in connection with the direct tax position. Changes in the legislation and its interpretation mean that charities are now deemed to conduct one large trade rather than a number of small ones and significant non-primary purpose trading is less likely to “taint” what would otherwise be exempt income.

“The VAT threshold was indeed found to have been breached some time ago and we set about formulating a plan of action in order to minimise the consequences to the School.”

We were therefore able to identify sufficient turnover from potentially taxable income streams that could be treated as ancillary to the charitable purposes, thereby demonstrating that the School’s turnover from non-exempt trading qualified for the small trading exemption. This not only saved the tax, interest and penalties that could have been due but also the considerable cost of preparing back-dated tax returns.

In addition to the significant savings made in respect of past liabilities, we were able to advise the School on the practicalities of forming a trading subsidiary and its ongoing administrative requirements. This included advice on how the activities could be split between the entities and, in some cases, restructured within the School, so that they could take advantage of the direct tax exemption limits by retaining an element of income that it would have been detrimental to transfer and ensuring that neither entity would need to maintain a VAT registration going forward, giving a considerable administrative saving.

The advice was tailored to meet the specific needs of the School by suggesting a number of possible and practical solutions to their concerns, arising from the need to balance direct tax, VAT, administrative, finance and legal considerations.

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in brief

Payment of trustees

Changes being introduced through the staged introduction of Charities Act 2006 include clarification of the provisions for payment to trustees for services as a trustee. Previously the general rule allowed for payments in return for professional services, expenses and honoraria.

Any payment must also be specifically provided for in the governing document or permission must always be obtained from the Charity Commission.

In deciding whether to go down this route charities should consider whether they can obtain a suitable trustee without payment.

Further information is available following:
<http://www.charitycommission.gov.uk/publications/cc11.asp>

Consultation on Charitable Incorporated Organisations (CIOs) is underway

A CIO is a new corporate structure designed specifically for charities. The CIO model offers charities an alternative to incorporation under company law, and unlike the company law structure will not require 'dual regulation' by the Commission and Companies House, such as with the filing of accounts.

The consultation will close on the 10th December 2008. To contribute visit:
http://www.cabinetoffice.gov.uk/third_sector/Consultations/current_consultations.aspx

Non primary purpose losses

The second and final draft of the corporation tax bill is due in February 2009 and should become law shortly thereafter. As presently drafted, the bill will introduce changes to the treatment of losses of corporate charities from non-primary purpose trading so that a tax liability is more likely to arise (this follows similar changes for Charitable Trusts, which took effect from 2007/08).

Schools that have for VAT reasons previously retained activities such as summer school lettings within the Charity should take steps to evaluate the potential tax costs and whether it might be appropriate to restructure their activities, (possibly using a trading subsidiary,) or broaden their objects to bring such activities within their primary purposes.

Our School Trading fact sheet offers more detail on this matter. Do contact us if you think that you may be affected.

Reporting serious incidents

Recent guidance published by the Charity Commission on reporting serious incidents provides clarification on the definition of a serious incident along with when and how to report.

A serious incident is a matter which could 'significantly harm' the charity's property, work, beneficiaries or reputation. The guidance states that it is 'good practice' for trustees to report any such incidents to the Commission when they arise.

Trustees can report serious incidents to the Commission in one of the following ways:

- by contacting Charity Commission Direct in writing at PO Box 1227, Liverpool L69 3UG;
- by calling 0845 300 0218; or
- by email.

The following details are likely to be of importance:

- whether an incident has actually happened, or whether there have been allegations/suspicions that it has happened;
- when the incident happened;
- who was involved, their position in the charity and whether they are still involved with the charity;
- the impact that the incident has had on the charity and/or its beneficiaries;
- whether there has been any publicity as a result of the incident;
- what action the trustees have taken and the outcome of any inquiry they have conducted into the incident;
- whether another regulator, law enforcement or government agency is involved; or
- whether there are any statutory provisions governing the incident.

Further information can be found by visiting the following weblink: <http://www.charitycommission.gov.uk/investigations/rsi.asp>



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library schemes and weddings – VAT implications



Our theme this quarter is “rent”, though the issue is that “rent” is not always what it seems to be, so you will need to think more widely than you might at first imagine.

Renting out school facilities for celebratory events, such as wedding

receptions, usually involves a mixture of venue hire and catering. It has long been assumed that the venue hire in this context is not a rent, but rather part and parcel of the catering and therefore subject to VAT in full. That is true, but it has often also been thought that merely renting the venue would be exempt because there were no “added value” services. This is now doubtful, following the Chewton Glen Hotels VAT tribunal decision. This concerned a hotel, and it was held that venue hire was also taxable because the service constituted something considerably more than a mere right over land. As to whether that would also be the analysis for a school, that is possibly debatable, but certainly it sharply increases the risks associated with treating this activity as exempt.

Contrast this with HMRC’s declared policy in cases of charges made for the use of school facilities for conferences. Whilst in many cases these charges will be wholly exempt if such facilities are used by other eligible bodies to educate their students, if, for any reason, the customer is not an eligible body, the supplies of catering and overnight accommodation are taxable rather than exempt. But HMRC accepts that the component of such charge relating to the use of classrooms and halls (if not for physical recreation) can be exempt, since all that is supplied to that extent is a bare right to occupy “land”. This, of course, assumes that no option to tax has been made over the buildings.

Talking of which, options to tax and their connection with “library schemes” bring into focus situations where HMRC would far rather the rental supply was exempt.

As piloted by Newnham College, this scheme supposedly allows VAT recovery on the cost of building a new library. The college (or school) incurs the VAT on construction costs, and opts to tax the building. It charges rent to a subsidiary company which has been set up to provide library services. It adds VAT to that rent, and reclaims all of the VAT on construction costs. The library company reclaims VAT on the rent, and makes a charge for library services to the college/school (a part of which may be zero rated, though that is another story!).

The House of Lords had to decide whether this worked, and in particular whether an anti-avoidance rule stopped the rent charged by the college being taxable. This revolved around the definition of “occupation”. The Lords decided the college was not “in occupation” and that determined the case in favour of the library scheme (though the arguments would probably apply far more convincingly to universities than to schools).

But HMRC were cunning, in that they refrained from bringing a second line of argument into the fray, since they wanted to test the specific anti-avoidance rule alone. The second line of argument is the argument generally known as “abuse”. It is a general anti-avoidance principle which relies for its effectiveness on the arrangements being seen to be contrived principally to avoid VAT, and to have scant commercial or operational rationale. That second line of argument may or may not have been successful. It can be predicted that other iterations of the “library scheme” will have to contend with that second argument, and may well fail as a consequence.

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VAT update

We are pleased to report that certain schools we have been advising have agreed claims with HMRC in excess of £50k each in regard to a strictly time limited opportunity for claiming historically overpaid VAT. For reasons perhaps best left unexplained, it is possible to review your VAT returns for the period 1973 to 1997 and claim any overpaid or under claimed VAT. There is even a possible argument in favour of unregistered schools doing this.

In our experience it is the failure to have claimed VAT on overheads which is the most likely source of claims of this kind. The window for claims is open until 31 March 2009, following which they will not be entertained at all. The three year cap will be reinstated, and the opportunity will be lost. Time is running very short, so please contact us to discuss this opportunity.

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future events

Trustee Training for Charities

Our annual Trustee Training series will be held in Autumn/Winter 2008.

The sessions are:

23rd October – Understanding charity accounts
4th November – Protecting your charity's reputation
18th November – Investing in turbulent markets
27th November – Charity law update
22nd January 2009 – What every trustee should know

Schools' Conference

Our 2009 Schools' Conference will take place on the 4th February at Drapers Hall, London.

For further information, please contact:

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