



"OVERALL AUDIT SERVICE AWARD" - WINNER 2009
Annual *Charity Finance* survey

not for profit | fit and proper persons

team



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The 2010 Finance Act introduced changes to the definitions of a charity and CASC as well as strengthening the non-charitable expenditure rules for payments to overseas bodies with effect from 8 April 2010.

As a result of these changes, HMRC are introducing greater administrative and reporting requirements and have greater discretionary powers to withdraw tax relief. Whilst it is unlikely that a UK charity that is not engaged in tax avoidance activities would be at risk of losing its entitlement to tax exemption, recent HMRC comments in the press are not comforting. Even if HMRC's powers are applied sensibly, failure to follow the correct procedures could well result in delayed repayment claims as well as unnecessary and costly disputes.

The changes did not initially receive detailed scrutiny as the dissolution of parliament for the election prevented proper discussion and there was no consultation with sector representatives. Following widespread opposition, HMRC guidance has already been amended and could well be subject to future changes. This factsheet outlines the most significant changes announced so far and gives recommendations for action to be taken in order to minimise risk. It is based on our understanding of the position in July 2010.

payments to overseas bodies

Prior to 8 April 2010, a payment made to a body outside the UK could result in a tax liability for the charity only if the trustees had not taken such steps as are reasonable in the circumstances to ensure that the payment would be applied for charitable purposes. The test is now strengthened so that such a payment would only qualify as charitable expenditure if HMRC consider that reasonable steps were taken. This would previously have been a matter for the Courts and the change is a significant shift of power to HMRC. Furthermore, HMRC perceive a problem with charities not keeping adequate records to prove that their expenditure is charitable. Charities are therefore advised to implement and properly document adequate checks.

new definition of a charity

Charity means a body of persons or a trust that:-

- a) is established for charitable purposes only (as has always been the case),
- b) is located in the EU or Norway or Iceland (previously only in the UK),
- c) has complied with any requirement to be registered with the Charity Commission; or, The Office of the Scottish Charity Regulator; or, an overseas equivalent (putting current practice on a statutory footing), and
- d) has managers that are fit and proper persons (this is a new requirement and is discussed in more detail below).

what is a manager?

The legislation provides that “managers” are persons having the general control and management of the administration of the body or trust. HMRC guidance expands on this and indicates that the term ‘manager’ applies to the trustees of charities, directors of corporate charities, CASC officials and any other officials having general control and management over the running of the charity and the application of its assets. The term ‘general control and management’ has a wider scope than that found in the Charities Act 1993 and, in a typical small local charity the managers would include the chairperson, treasurer, secretary and the rest of the management committee. In a larger charity it may extend to certain employees who are able to determine how a significant proportion of the charity’s funds are spent, such as members of the executive board.

what is fit and proper?

There is no statutory definition of fit and proper persons, but HMRC indicate that the test is concerned with ensuring that charities are not managed or controlled by individuals who present a risk to the charity’s tax position. Factors that may lead to HMRC deciding that a manager is not a fit and proper person include:-

- a history of tax fraud;
- a history of other fraudulent behaviour including misrepresentation and/or identify theft;
- HMRC knowledge of involvement in attacks against or abuse of tax repayment systems;
- being barred from acting as a charity trustee by a charity regulator or Court, or being disqualified from acting as a company director.

It should be noted that an individual considered by the Charity Commission to be a suitable trustee would not necessarily be considered fit and proper by HMRC. HMRC do however indicate that they will take account of the likely impact on the charity’s tax position when applying the test.

failure to meet the test

HMRC will have discretion to decide whether to refuse the charity’s claim to tax reliefs where they decide that one or more of the charity’s managers are not fit and proper persons. This could result in the charity’s income becoming taxable as well as a loss of the right to claim Gift Aid on the donations that it has received. The charity will have a right of appeal to a tribunal.

HMRC indicate that they will exercise discretion if they consider that either, the manager is not able to influence the charitable purposes of the charity or the application of its funds; or, it is just and reasonable to do so. The latter might apply where either: -

- the person has no dealings with HMRC and no control over spending charitable funds; or,
- the charity informs HMRC of the person’s appointment and puts adequate controls in place.

HMRC may also exercise their discretion to treat a charity as having always met the management conditions where they have unknowingly appointed a person who is not deemed to be fit and proper and reach agreement with HMRC to either restrict that person’s responsibilities or introduce adequate controls.

It is unhelpful that the rules have been drafted to catch as wide a range of situations as possible but to allow HMRC to then exercise discretion. In the absence of a clearance procedure, there is no way to be certain that a charity is not at risk. Whilst we would hope and expect that HMRC will seek to apply the legislation appropriately, this can be subjective and there is a recent history of HMRC changing established practices as they are written into statute and seeking to apply old and, for all other intents and purposes, redundant legislation to the detriment of charities.

documentation

- new charities - HMRC have issued a new Charity's Application Form (ChA1) which should be completed by any charity that wishes to take advantage of the Gift Aid scheme or other charitable tax exemptions and is not already recognised as a charity with HMRC. The form can be found at <http://www.hmrc.gov.uk/charities/cha1.pdf>

A similar form for CASCs is available at

<http://www.hmrc.gov.uk/casc/cascapp-form.pdf>.

It should be noted that the forms are currently being revised and HMRC only require details of between 2 and 4 responsible persons from whom they will accept future instructions rather than details of all managers for the purposes of the fit and proper tests as requested on the current form.

- all charities - changes to contact details for the charity, authorised officials, responsible persons, nominees and bank or building society account details now need to be notified on the new HMRC Charities Variations Form (ChV1). HMRC indicate that any relevant changes should be notified on the appropriate form at least one month before making a Gift Aid claim using the new details. The authorised official is the person responsible for making repayment claims and dealing with HMRC in connection with the charity's tax affairs and the responsible persons would generally be 2 to 4 trustees nominated to be able to notify changes to and also deal with HMRC on the charity's behalf. The current form indicates that there is no need to give details of responsible persons but it is assumed that these notes on the form will change. The current form is available at <http://www.hmrc.gov.uk/charities/chv1.pdf>.
- existing charities – should nominate 2 to 4 trustees or directors to act as responsible persons on the first occasion of filing a Charities Variations Form. Thereafter, HMRC will only change the charity's record on the instructions of the responsible persons or authorised official.
- model declaration for fit and proper persons - HMRC suggests that trustees may wish to obtain a declaration from any new managers, trustees and directors appointed after 5 April 2010. They have published a basic guide to the fit and proper person rules together with a model declaration form for new managers.

recommendations

- all managers for the purposes of the fit and proper persons test should read HMRC's basic guidance and anyone appointed after 5 April 2010 should complete the attached model declaration, which is available at <http://www.hmrc.gov.uk/charities/guidance-notes/chapter2/model-dec-ff-persons.pdf>.
- the authorised official nominated to deal with Gift Aid claims and to submit tax returns should make themselves familiar with the detailed HMRC guidance which is available at <http://www.hmrc.gov.uk/charities/guidance-notes/chapter2/fp-persons-test.htm>
- the authorised official should ensure that relevant changes are reported on the correct form and in good time to be processed before the next Gift Aid repayment claim is due to be made.
- consideration should be given to HMRC's stated expectation that charity trustees should be able to show, if challenged, that they have given proper consideration to the suitability of people they appoint to positions of trust or influence in the charity, especially where they are able to exert control over the charity's finances and tax

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affairs. There is no indication as to how this might apply to existing managers and it may be safest to obtain "fit and proper" declarations from all existing managers.

- charities making payments to overseas bodies should make sure that reasonable checks are carried out to ensure that the funds will be applied for charitable purposes and that the checks are properly documented. In deciding what is reasonable, due regard should be given to: -
 - o the charity's knowledge of the overseas body
 - o previous relations with the overseas body
 - o past history of the overseas body
 - o the size and regularity of the payments

HMRC's detailed guidance is available at
http://www.hmrc.gov.uk/charities/guidance-notes/annex2/annex_ii.htm#9

about haysmacintyre

haysmacintyre, Chartered Accountants and tax 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.

haysmacintyre is a founding member of MSI Global Alliance (MSI), an international alliance of independent legal and accounting firms, with 250 members in 100 countries.



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save the date:

Thursday 18th November 2010
"An Introduction to Tax for Charities"

registration from 2.00pm to 2.30pm. The seminar will finish at 5.30pm

This event is aimed at the finance staff of charities and not for profit organisations. It will cover the basic principles of direct tax, VAT, employment tax, and the fit and proper issues that have been outlined in this publication.

Further information will follow on our website shortly.