Autumn 2015

haysmacintyre
chartered accountants & tax advisers

ARTS & CULTURE BRIEFING

"Charity Expertise Award" and "Overall Service Award" | Top three for eight consecutive years | *Charity Finance* Audit Survey

Mid-Tier Firm of the Year 2014 | The British Accountancy Awards

LETTER FROM THE EDITOR

Welcome to the Autumn edition of haysmacintyre's Arts & Culture briefing.

In this edition we report on updates from the Charity Commission, lessons learnt from recent inquiries and the impact on the quality and quantity of financial information that charity trustees should receive. Particularly pertinent given the profile of Kids Company at present. Jane Askew, Arts and Culture Audit Manager, comments on the Centre for Economics and Business Research report into the contribution of the Arts and Culture sector in the UK, a helpful report that enforces the view of many that Arts and Culture contributes a great deal to the national economy.

Our tax team revisit the issue of Theatre Tax Relief following the issue of guidance from HMRC. Although our experience has been that the originally intended 'Special Purpose Vehicle' or trading subsidiary route, which was plugged and pushed with so many organisations, is now seen to be more problematic than first thought. Care is required in the implementation of this tax relief and our advice remains that you should approach HMRC with your methodology in advance of submitting any claims to gain their input first. The tax team also comment on other relevant tax areas for Arts and Culture organisations, including the Social Investment Tax Relief, the new employment tax reporting requirements from April 2016 and a summary of recent VAT cases in the sector.

We hope you enjoy reading this edition and if you have any queries regarding the articles, please do contact myself or one of our specialist advisers.

Richard Weaver, Head of Charities and Not for Profit
T 020 7969 5567 **E** rweaver@haysmacintyre.com

LESSONS TO LEARN FROM RECENT CHARITY COMMISSION INQUIRIES

The Charity Commission has so far issued 20 inquiry reports since 1 April this year. The vast majority of these reports, 17, were a direct result of their clamp down on investigating charities that had not filed their accounts on time for two out of the last five years.

The enquiry reports are often high level and do not give a huge amount of detailed information, but what they do show are two very clear messages:

1. Trustees need to understand their duties in complying with the legislative framework to file accounts; and
2. Trustees need to ensure that the financial information that they receive and act on is adequate, and in a form that they understand and is relevant for them to make appropriate decisions for the benefit of the charity beneficiaries.

The first of these findings is not new to the sector.

The Essential Trustee guide, CC3, has been available from the Commission website for many years and, in the light of their recent inquiries, the publication was updated in September. There is a separate article in this briefing on the key focus areas of the updated guidance. All trustees are advised to read, if not the whole publication, at the very least the summary, in order to avail themselves of what is expected of them.

The second of these findings is of greater concern, not just to the Commission, but to the sector as a whole. The Commission set a parameter of charities with income of between £250 - £500,000 of income in setting its criteria for inquiries. Up until March 2015, this was the income range where charities, on the whole, did not require a full audit, but an independent examination, so the rigour of annual audit and the more formalised process of engaging auditors was not present.

This is a grouping that, when combined, raises and manages a significant value of charitable income and assets. The individual findings raise a point that we often see and lecture on in our Trustee Training series, what information should be prepared and reviewed by trustees on a periodic basis?

The recent press reports on the financial vigilance of Kids Company have highlighted the importance of not only the financial management of charities, but also the ability to forecast and be sustainable for the benefit of both current and future beneficiaries. More will no doubt be released once the Commission have finished their own review into the closure of the charity.

Set out is a list of information we would expect all charity trustees to receive on a regular, at least quarterly, basis in order to effectively manage and make decisions within the charities they are custodians of.

INFORMATION THAT TRUSTEES SHOULD RECEIVE:

- **Income and expenditure (by entity if you are a group)**
  Each entity should have a separate income and expenditure account and a consolidation page if in a group.

- **Outturn for the year**
  Projecting the year to date actuals with estimated results to the year-end date helps to analyse and compare to the annual budget and ensure that you have the financial resources to meet your targets.

- **Balance sheet information**
  The one piece of information which is commonly missing from the pack. Without a balance sheet you are unable to verify whether the income and expenditure is in balance. You should have sufficient sight of balance sheet numbers and in particular the breakdown and recovery of debtors, confirmation that the bank accounts have been reconciled and clarity over the completeness of all creditors and accruals at that date.

- **Funds analysis – restricted v unrestricted**
  All of the above information should be available and analysed by fund. It is crucial that you have absolute clarity over the type of fund and the amount of funds available.

- **Cash flow**
  A cash-flow forecast will prove that you do (or do not) have sufficient financial headroom to continue to operate in the way intended. The cash-flow should link and reconcile to the bank balances and income and outturn papers.

- **Prior year comparisons**
  Useful where income streams are consistent (membership organisations for example) but more 'informative' where income streams are less predictable or the types and regularity of funding is less consistent.

- **Commentary/explanations**
  Understand who is providing the commentary. Where you have budget holders, they should provide the analysis to the Finance Team. It is now also common practice for many audit committees to have department heads and/or budget holders present on a cyclical basis to the trustees. This can help with engagement, but also assists trustees in their understanding of the financial risks faced by the operations of the charity.

- **Key indicators/benchmarks**
  Useful where there are key elements to your operations, such as target investment returns, success rates in tendering, turnover of staff, level of grant applications and value. The list could go on depending on the type of charity and what it does. But as a snap shot these KPIs are often more useful than the detailed financial information for the non-financial trustees.

The above list is not exhaustive, and there may be other key reports that are helpful to your charity, but the above should be provided as a bare minimum.

We are often invited to comment on the quality and content of board papers, and it is perhaps an interesting point to review in the light of recent reports. For now though, if you are a trustee, ensure you have a copy of The Essential Trustee and receive the information you need in order to effectively operate financial governance.

Richard Weaver, Head of Charities and Not for Profit
T 020 7969 5567 **E** rweaver@haysmacintyre.com

CONTRIBUTION OF THE ARTS SECTOR

The Centre for Economics and Business Research (Cebr) has recently published a revised report for Arts Council England on the contribution of the Arts and Culture industry to the national economy. Whilst for many charity sectors funding continues to be a challenge and strings have inevitably been tightened, it is great to see some good news coming out of this report in relation to the Arts and Culture sector.

The report was commissioned to measure the value of the Arts and Culture industry as a whole, using official data provided by the Office for National Statistics for the years 2008 to 2013 and it reveals a very positive message. Some of the key findings were:

1. Sector turnover has increased from £12.4 billion in 2011 to £15.1 billion in 2013, representing growth of 22%.
2. Gross Value Added (GVA), which is the net benefit once external cost has been stripped out, showed an increase of 35.8% to £7.7billion.
3. For every £1 of turnover that arts and culture organisations generate, 51p of GVA is added to the economy.
4. The average Arts and Culture sector worker is paid well over the national average at nearly £28,000, and wages rose 2.4% between 2010 and 2013 during a period of low inflation.
5. The number of people employed rose from 123,000 to 128,000.
6. Every pound of public funding going to the Arts Council national portfolio organisations pays back £5 in tax contributions from the sector as a whole, representing an annual return of £2.35 billion to treasury coffers.

It is clear from this report that the Arts and Culture industry has fared well in difficult times, successfully adapting to the economic climate, cutting costs, increasing GVA and making a greater contribution to the UK's GDP. The Cebr Director of Policy and Research, Richard Russell, concludes in his introduction to the report that *'it tells a story of resilience and efficiency, and how the sector has, without losing its creative ambition, succeeded in making more productive use of public funds.'*

The contribution the Arts and Culture industry makes to the economy and the return on public investment is a positive story for donors. The full report can be found at: http://www.artscouncil.org.uk/advice-and-guidance/browse-advice-and-guidance/contribution-arts-culture-national-economy

Jane Askew, Audit Manager
T 020 7969 5683 **E** jaskew@haysmacintyre.com

SOCIAL INVESTMENT TAX RELIEF UPDATE

Social Investment Tax Relief (SITR), introduced for investment by individuals into qualifying social enterprises (principally charities and community interest companies) for the tax year 2014/15 onwards, gives a tax relief very similar to the Enterprise Investment Scheme (EIS) for investment by way of equity or debt.

As with EIS the individual investor can deduct 30% of the cost of the investment from their income tax liability, any capital gain will be tax free and the investment can also be used to rollover other capital gains.

The current limit for investment by an individual is £1 million in a tax year and receipts by the social enterprise is limited to total qualifying investment of €344,827 over three years. The Government announced in the 2014 Autumn Statement that it would apply for EU state aid clearance to increase the limit for an enterprise to £5 million per year, and £15 million in total, but that clearance has not been forthcoming so far.

The last Coalition Budget in March 2015 also announced a new Social Venture Capital Trust Scheme to encourage indirect investment, to be introduced in a future Finance Act.

The use of SITR funding has been somewhat limited to date, but it has been used to set up a commercial trading activity to subsidise charitable activities (FareShare), to assist in buying community facilities (FC United in Manchester), and to fund innovative services under a government pay by results contract (Ambition East Midlands). An SITR fund has also been established in Bristol to support local social enterprises. While the limits are still quite restrictive and cheaper finance, particularly for property transactions, may be available elsewhere, charities and other not for profit entities should consider SITR as a potential source of funding to support or expand their activities.

For further information or guidance on applying for SITR, please contact Helen Berg or Katharine Arthur.

Helen Berg, Tax Director
T 020 7969 5557 **E** hberg@haysmacintyre.com

Katharine Arthur, Head of Tax
T 020 7969 5610 **E** karthur@haysmacintyre.com

THEATRE TAX RELIEF: DETAILED GUIDANCE RELEASED

HMRC has at last published more detailed guidance in their manuals on theatre tax relief (TTR), which has been available from 1 September 2014 to Theatrical Production Companies (TPCs).

The relief entitles a TPC to additional tax relief for expenditure on a qualifying theatrical production, of 25% for touring productions and 20% for other qualifying productions. The credit can take the form of an additional deduction in computing taxable profits, or, if that creates or increases a loss, a payable tax credit. The repayable credit will be 20% for a touring production and 16% for others, based on the current 20% corporation tax rate.

Because the TTR is available to TPCs that are within the charge to corporation tax, charities and other not for profit organisations can qualify, even if they are not in fact taxpaying due to exemptions applying to their various sources of income. They should be aware, however, that the claiming of TTR may restrict their ability to claim grants or similar forms of State aid for the same production. Subject to the usual considerations on charitable status, the role of the TPC can be undertaken by the charity itself, or by a wholly owned trading subsidiary. Which structure is most appropriate will depend on individual circumstances, and VAT implications will also need to be considered.

The deduction or tax credit is calculated by reference to core expenditure – expenditure directly incurred in producing and closing the production, and excluding development and normal running costs - up to a maximum of 80% of total core expenditure by the TPC.

The definitions of qualifying TPCs and qualifying theatrical productions are complex and need to be considered in detail for each case. Careful identification of the costs which can be considered core expenditure will also be needed to maximise the benefit of claims. The HMRC guidance gives useful detailed explanations and examples for these areas and of how the relief can be calculated and utilised.

Helen Berg, Tax Director
T 020 7969 5557 **E** hberg@haysmacintyre.com

WHAT ARE YOUR EMPLOYMENT TAX REPORTING REQUIREMENTS?

Following the introduction of Real Time Information reporting for PAYE purposes, attention is now turning towards the reporting requirements as they relate to benefits in kind.

While the stated aim is to reduce the administration burden for employers, additional costs are potentially in store for many charities. This article provides an introduction to a number of changes which will come into effect from 6 April 2016.

ABOLITION OF THE £8,500 BENEFITS IN KIND THRESHOLD

There have been calls for some time to provide consistency on the reporting of benefits in kind for all employees, regardless of their earnings level.

The removal of the £8,500 threshold will mean all employees will potentially be liable to tax on the benefits in kind they receive. No tax will be due where the employee's income from all sources is less than the personal allowance (£10,600 for the 2015-16 tax year).

However, the employer will be liable to Class 1A National Insurance (NI) on benefits in kind reported on form P11D. Similarly, there will potentially be an increase in the tax and NI liabilities due where employers have entered into a PAYE settlement agreement with HM Revenue & Customs (HMRC).

BUSINESS EXPENSE ALLOWANCE

Currently, where an employer pays any expenses or provides benefits in kind, these need to be declared on an employee's P11D each year.

Strictly speaking, employees are required to claim tax relief on any reimbursed expenses incurred "wholly, exclusively and necessarily" in the performance of their employment.

Where an employer can demonstrate that they had adequate controls and procedures in place, HMRC will grant them a dispensation resulting in only taxable benefits in kind being declared. The business expense allowance, which is replacing dispensation agreements, will place greater emphasis on the employer to determine whether any payment fulfills the "wholly, exclusively and necessarily" test.

It is our recommendation that all employers review their current expenses policy to ensure that they are up to date and fully understood by your employees.

PAY-ROLLING ON BENEFITS IN KIND

Following representations made by a number of organisations (including a number of charities), it is intended that the tax and NI due on certain benefits in kind can, in future, be collected on a voluntary basis through the payroll, without the need to submit a form P11D for those benefits in kind.

The legislation will enable employers to account for tax and NI through the payroll on the following benefits:

- Company cars;
- Car fuel;
- Medical benefit; and
- Gym subscriptions.

At present the legislation is fairly prescriptive as to the nature of the benefits it relates to, but there is also the opportunity to payroll other benefits, for example, telephone expenses. Where any additional benefits are pay-rolled, then the employer will still be required to submit a P11D to HMRC.

For many charities the pay-rolling of benefits will help to considerably reduce their year-end reporting obligations.

However, where a charity is going to operate the pay-rolling of benefits regime, now is the time to start thinking about how this will be managed.

RECENT CONSULTATIONS

At present we are expecting changes in the legislation with regards to:

Provision of living accommodation

The Office of Tax Simplification concluded their review regarding the tax treatment of living accommodation in the latter part of 2014. We are still awaiting further developments from the Government as to any changes in the legislation they are likely to introduce.

Termination payments

The tax and NI treatment of termination payments is currently the subject of an HMRC consultation. The review is considering:

a. Aligning the tax and NI treatment of termination payments;
b. Removing the distinction between contractual and non-contractual payments;
c. Looking at the basis upon which any exemption will be due, for example, linking it to statutory redundancy pay, or the employee's length of service; and
d. Removal of any exemption where salary sacrifice arrangements are in place.

Travel and subsistence payments

This is currently the subject of a discussion paper issued on 23 September 2015 and is reviewing the basis upon which tax relief is due for employees who do not have a permanent place of work.

The Chancellor of the Exchequer's Autumn Statement, which is due to be delivered on 25 November, is eagerly awaited.

For guidance on your reporting requirements, please contact Nick Bustin.

Nick Bustin, Employment Tax Director
T 020 7969 5578
E nbustin@haysmacintyre.com

LEARNING FROM RECENT VAT CASES

BRITISH FILM INSTITUTE (BFI)

The VAT exemption for cultural services applies to the grant of a right of admission by an eligible body to a museum, gallery, art exhibition, zoo or to a theatrical, musical or choreographic performance of a cultural nature.

The British Film Institute (BFI) successfully argued that the exemption should also apply to the grant of the right of admission to the National Film Theatre and various film festivals. This was on the basis that the UK legislation outlined in the first paragraph above did not correctly reflect the underlying EU VAT Directive.

This was on the basis that Annex H to the Sixth VAT Directive (the predecessor to the current one) listed categories of supply which are eligible for reduced-rates. These include admissions to shows, theatres, circuses, fairs, amusement parks, concerts, museums, zoos, cinemas, exhibitions and similar cultural events and facilities.

Earlier European case law also supported the argument that exemption should apply by stating that a provision in European law which appeared to give Member States an element of discretion over which services they could exempt.

This judgement was appealed by HMRC to the Upper Tribunal, who upheld the judgement in August 2014.

HMRC appealed the matter further to the Court of Appeal, and we now understand that they have referred the matter to the Court of Justice of the European Union (CJEU).

It is likely that there will be no final decision from the CJEU before late 2016 at the earliest, and more likely it will be some time in 2017.

Our view is that the BFI has a very strong case and is likely to be ultimately successful. We would therefore advise any bodies who think they have a similar claim to lodge it now. It is unlikely that HMRC will make any repayment before the decision of the CJEU, but by lodging a claim now you prevent periods from becoming time barred under the rule which prevents claims from being made in respect of periods which are more than four years ago.

CULTURAL EXEMPTION

Following from the BFI case above, a further point is that it is important to remember it is the grant of the right of admission which qualifies for the exemption. Companies which tour productions therefore need to establish whether they are granting the right of admission, or whether it is the venue which is doing so.

If it is the latter, then the point is whether it is doing so as a disclosed or an undisclosed agent. It is the former, then the venue merely acts on behalf of the company which is still regarded as granting the right of admission.

THE CHANCELLOR, MASTERS & SCHOLARS OF THE UNIVERSITY OF CAMBRIDGE (UNIVERSITY)

This case concerned the recovery of VAT on the costs of managing an investment portfolio. It is therefore not specific just to the Arts and Culture sector, but potentially still relevant. HMRC's view was that any VAT on the costs of managing investments related only to the sale of those investments and was therefore either an exempt supply of securities or other financial instruments, or more likely was not a business activity at all following the European Court's judgement in the Wellcome Trust case.

The University argued that the income from their investment portfolio was unrestricted income which underpinned the entire mixture of taxable and exempt supplies it made, and as a result the VAT on the costs were simply an overhead cost which should be partly recoverable. This was supported by both the First-tier Tribunal and Upper Tribunal, but we understand that HMRC has now been granted leave to appeal to the Court of Appeal.

Once again this means that there will be a delay of about a year or so before this matter is resolved, but we would recommend that any affected organisation lodges a claim so as to avoid becoming time barred.

As this case follows in the line of cases from the Church of England Children's Society case which upheld very similar principles, our view is that HMRC do not have a strong case.

UAB SVEDA

The last case we would draw your attention to is, at this stage, only an Opinion from the Advocate General (AG) of the CJEU. We await the final judgement with interest.

For some time HMRC has been seeking to advance an argument that where organisations (invariably non-profit making bodies) make taxable supplies which do not fully cover the cost of making them because they are subsidised out of own resources from donations, or which are underpinned by grant funding, then there should be a restriction on the amount of VAT which can be claimed. The AG's Opinion strongly suggests that this argument is incorrect. The case in question is Lithuanian and no official translation has been released but if it is followed by the Court then it means that HMRC's argument is incorrect.

There have been some other CJEU cases which also support the views of the AG, so if HMRC have sought to advance an argument that the mere receipt of non-business income (as opposed to carrying out non-business activities) should give rise to a restriction to the right to deduct VAT, then we would recommend that this is challenged.

Phil Salmon, VAT Partner
T 020 7969 5611 **E** psalmon@haysmacintyre.com

haysmacintyre
chartered accountants & tax advisers

Future events

Identifying and managing risks in a charity	2 December 2016
Charity law update	12 January 2016
What every trustee should know	3 March 2016
What every trustee should know - Refresher	23 March 2016
Introduction to charity finance and reporting	19 April 2016
What every trustee should know	23 May 2016
Network of Women Chairs	Multiple dates available on our website

For further information on these events please visit www.haysmacintyre.com/events or contact our Events team on 020 7969 5500, events@haysmacintyre.com

Should you wish to receive an electronic version of our briefing in the future, please email our Editorial team on marketing@haysmacintyre.com

haysmacintyre
26 Red Lion Square
London
WC1R 4AG

T 020 7969 5500 **F** 020 7969 5600
E marketing@haysmacintyre.com
www.haysmacintyre.com
@haysmacintyre