

A background image showing a group of cyclists in a race, with a focus on the front rider's hands on the handlebars and legs pedaling. The image is slightly blurred to convey motion.

haysmacintyre

chartered accountants & tax advisers

PIMBs Briefing

Winter 2017

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Editor's introduction



Welcome to our first briefing of 2017 for professional institutes and membership bodies.

In this edition we look at 'Management accounts - more than income and expenditure' and how you can engage your Council members and trustees in the organisations' finances. We also consider how to manage

a charity in financial difficulties, which is applicable to all not for profit organisations that may be struggling in these testing times.

Our employment tax team touch on two key topics: Apprenticeship Levy and salary sacrifice arrangements. Nick Bustin who heads our Employment Tax team has provided an overview of the Apprenticeship Levy due to be introduced from April 2017 and explains what has changed and what we need to consider regarding salary sacrifice. Phil Salmon, Head of VAT, takes a look at VAT subscription apportionments and we have included information on BWB's 'Get Legal', an online tool providing a wide range of templates and guidance.

Details of our up and coming events for the sector have been included in the events section at the back of this briefing. These include events with PARN (the Professional Association Research Network) whose special interest group for finance professionals host their events at our London offices. haysmacintyre also sponsor the PARN annual financial benchmarking survey.

While continuing our support of PARN, in 2017 we are embarking on a new relationship with MemCom. MemCom - the resource for membership marketing professionals - offers an annual conference and awards programme and haysmacintyre is the proud sponsor of the 'annual report' award category this year. Details can be found at www.memcom.info/awards and we hope to see many of our clients and contacts entering the awards this year.

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Management accounts – more than income and expenditure

One of the key financial responsibilities of Council members is to ensure strong financial oversight. In this article we explore whether we have outgrown the traditional management accounts of income and expenditure compared to budget and what other new data reports are available.

What are the duties of Council members?

CC3: 'The Essential Trustee: what you need to know, what you need to do' was reissued in July 2015 and explains the key duties of all trustees of charities in England and Wales, setting out what trustees need to do to carry out these duties competently. Within the membership sector, many organisations are charities and therefore their Council members are the trustees. For those membership organisations which are not charities, Council members still have the same or similar overarching financial responsibilities.

Trustees have independent control over and legal responsibility for the organisation's management and administration. They play a very important role and one of their key financial responsibilities is to manage the organisation's resources responsibly. But what does this mean?

Council members must act responsibly, reasonably, honestly and exercise sound judgement. They must make sure the organisation's assets are only used to carry out its purposes. They must avoid exposing the organisation's assets, beneficiaries or reputation to undue risk and ensure they do not over-commit the charity, including taking special care when investing or borrowing. They must also comply with any restrictions on spending funds or selling land.

The Council members are ultimately responsible for implementing appropriate procedures and safeguards and

take reasonable steps to ensure that these are followed. If they fail to do this they risk making the organisation vulnerable to fraud or theft, or other kinds of abuse and will be in breach of their duties.

CC25: 'Managing charity assets and resources' provides guidance on how to help manage the cash, property and staff and states that "a charity can only succeed in meeting its aims if it manages its money properly". It is expected that Council members will plan, manage and monitor the finances of the membership body effectively and while there is a lot of guidance to support Council members, financial management practices vary considerably.

What is the sector doing well and not so well?

Most membership organisations are producing monthly management accounts. On the whole financial decisions are being recorded reasonably well through the minutes. However there is an increasing number of finance directors concerned that while financial information is being presented, Council members are not necessarily engaging in finance. But why not?

Through our training programmes we have asked trustees why. In many cases too much information is being provided. Management packs are getting longer as we add more information. Have we arrived at a point where there is so much information that Council members can no longer see the wood from the trees?





What could good look like?

If we start off by considering why Council members need management accounts. The three objectives are to:

- measure current performance;
- enable financial decisions; and
- evidence fulfilling financial oversight responsibilities.

Typically management packs include an income and expenditure account that compares actual spend to budget. There is often a cash flow forecast and financial projections. Less often is there a balance sheet, key performance indicators (KPIs) or a statement of financial activities.

If we were to start with a blank page and the objectives above, what information might we consider necessary to meet these objectives?

Perhaps to measure performance we would require information on income, expenditure, budgets, variances and explanations. Reports are also required on debts, fees, write offs and provisions as well as a note of borrowings, liabilities and commitments and looking forward, forecasts and contingencies. A balance sheet might help to provide some of this information.

The information required to enable financial decisions can be varied. The Charity Commission issued CC27: 'It's your decision: charity trustees and decision making in May 2013'. The guidance provides the principles of trustee decision making and it is the expectation of the Charity Commission that trustees must be able to show how they have followed these principles.

Although there has been a fair amount of discussion on KPIs only a relatively small number of membership organisations do have them. Benchmarking data gives great sector information but every membership body is different and perhaps trend analysis can be more useful.

It is important to identify what information is required for your organisation and the overall sector ratios may not be as useful. Ratios must be defined, explain the relevance, performance expectations and the warning signs.

Council members are required to understand the funds of the organisation and the legal responsibilities associated with those funds. Rarely is there included an analysis of

funds noting any restrictions. At best there may be some reporting through the investment committee if there are invested endowed funds.

Trading activity, particularly non primary purpose trading is increasing as organisations look for alternative income streams to support lower membership fee increases and concerns over publications income. Council members are required to monitor trading to ensure the charity is not funding non profit making activities and if there is trading in the charity, that the small trading tax exemption limit of £50k is not exceeded.

Other areas Council members may need management information on include any breaches of bank covenants and long term commitments.

How might management reporting be developed to focus Council members?

Council members have said the main reasons why they do not engage with finance are because they don't understand the numbers, too much information is provided and they don't know what questions to ask. So how might we improve the way we present financial information to them? We have set out below some thoughts:

- Provide a one page financial summary that clearly sets out the financial position and performance of the organisation. Further detail can be provided as required.
- Do not rely on questions being asked; highlight what the Council members need to know and why.
- Present the information in a more visually appealing way for greater focus and impact. For example a cashflow forecast represented graphically is easier to understand than a table of numbers.

And finally...remember that lots of great information has little or no value if no one understands it.



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Managing a charity in financial difficulties

It's an unwanted statistic but perhaps a sign of the continued squeeze on household incomes that we've recently seen an increase in the number of charities and community interest companies (CICs) seeking advice following cuts in funding.

The problem is most acute for small charities who do not benefit from sophisticated fundraising activities and often cannot afford to take on government contracts due to the associated employment costs.

Faced with the dilemma of protecting the charity's purpose, trustees often face significant demands on their time, as well as facing the risk of personal liability, when a charity is in financial difficulties or under the threat of insolvency. It is therefore important that trustees understand their duties and obligations, particularly when a charity is in financial difficulties.

Being invited to be a trustee of a charity is often a privilege and an opportunity to give back to the community. It can also be a daunting prospect when it comes to understanding the duties and obligations of a trustee. This is never more the case than when a charity is in financial difficulties. This article provides information and advice for trustees of charities facing financial difficulties or under the threat of insolvency.

An unincorporated charity does not have its own legal identity and therefore cannot technically be insolvent; the liabilities of the charity are the liabilities of the trustees (on a joint and several basis).

However, for for practical purposes, it is often appropriate for the trustees to adopt a commercial approach and consider the viability of the charity as a standalone entity, albeit with due consideration for the risk of personal liability.

What are a trustee's duties?

When a charity is insolvent, the trustees must prioritise the interests of creditors. There is no express legal guidance on how trustees should manage this shift in duties and in practice, the requirement to prioritise the interests of creditors will often conflict with the commercial realities of navigating a charity out of financial difficulties or preserving the charitable purpose whilst a way forward is agreed with key stakeholders.

How can trustees protect themselves?

In order to satisfy their legal duties and to protect themselves from the risk of personal liability, we recommend that trustees take appropriate advice – as recommended by the Charity Commission.

On becoming aware of the charity's financial difficulties, trustees should establish the viability of a charity and consider options to turnaround the charity's financial performance or otherwise, preserve the charitable purpose.

A recovery plan will typically involve third party stakeholders and will often take several weeks to agree. During this period, trustees should keep the charity's financial position under constant review to ensure that there remains a reasonable prospect of a recovery and that the position of creditors is not worsening.

When is a charity insolvent?

In England and Wales, an incorporated charity is deemed insolvent (section 123 of the Insolvency Act 1986) if:

- the value of the charity's assets is less than the amount of its liabilities, taking into account contingent and prospective liabilities ("the balance sheet test"); or
- the charity is unable to pay its debts as they fall due ("the cash flow test"); or
- a creditor has served on the charity a statutory demand and the charity has failed to pay or otherwise agree terms with the creditor; or
- a court judgement or other order of court is returned unsatisfied.



Accounting records	Maintain up-to-date accounting records, including details of creditors (present and future) and trading and cash flow forecasts to enable directors to take an informed view as to the prospects of the company.
Board meetings	Hold regular board meetings, from the time of becoming aware of the company's financial difficulties and minute all discussions as to the solvency of the company and conclusions as to why the company should continue to trade.
Suppliers	Avoid incurring further credit from suppliers or lenders (including company credit cards) - wherever possible, goods should be paid for in cash.
Creditors	Avoid payments to creditors, even under duress, to prevent the risk of preference - this includes paying deposits into an overdrawn bank account.
Assets	Avoid disposals of the company's assets (including defraying credit balances) and ensure that all insurances are maintained.
Connected parties	Avoid transactions with connected parties – where such transactions are considered, they should be at open market value or better and supported by independent verification.
Customer deposits	Avoid accepting customer deposits unless you are certain that the order will be completed – where the business relies on customer deposits, consider opening trust accounts to safeguard deposits.
Creditor actions	Refer creditors, in particular those claiming retention of title or liens over goods, to an insolvency practitioner engaged by the company.
Resignation	Take advice of a lawyer or a licensed insolvency practitioner if considering resigning as a director or in instances of conflict between directors – resignation may lead to allegations of failing to act in the interests of creditors.

Can a charity continue to operate whilst insolvent?

The short answer is 'yes' and it is often in the interests of all stakeholders, not least service users but also creditors, to continue to operate the charity but with due care and attention.

The test for when to close a charity and stop the charitable service is one of reasonableness, if at any time the trustees conclude that insolvent liquidation is inevitable, they must take steps to stop services, mitigate costs and wind up the affairs of the charity.

Typically, trustees might review a charity's accounts and budget on a quarterly or annual basis. However, when a charity is faced with financial difficulties, it is important that trustees continually review the charity's financial position (both current and forecast) to confirm that the charity remains viable and able to trade out of its financial difficulties.

Trustees should keep a charity's financial position under constant review when the charity is in financial difficulties.

What steps can a trustee take to deal with a charity in financial difficulties?

If a charity is suffering from short term cash pressures, it may be possible for the trustees to approach an existing or alternative lender for additional funding. The trustees may also be able to identify non-essential assets to be disposed of (including by sale and leaseback) or increase fund raising activities.

Where the causes of financial difficulties are more ingrained, it may be appropriate for the trustees to consider restructuring measures, including:

- a review of costs; or
- changes to services and activities; or
- a compromise with creditors; or
- a merger or sale to another charity.

For an incorporated charity, it is possible to formalise a compromise with creditors through a company voluntary arrangement (CVA), legally binding all unsecured creditors. An incorporated charity may also appoint Administrators to seek a moratorium against legal actions by creditors.

Neither a CVA nor the protection of an administration is available to unincorporated charities, although it is often possible to agree informal arrangements with creditors as part of the rescue of a charity. Given the risk of personal liability to trustees of an unincorporated charity, it is essential that they seek early advice if an unincorporated charity is in financial difficulties.



Closing a charity

The process to wind up a charity's affairs is often set out in the governing document.

For a solvent charity, the process is usually straightforward, although trustees may need to consider how best to allocate or transfer assets, including endowments and property, before closing the charity. In certain circumstances. This may be best achieved through a members' voluntary liquidation (MVL).

For an insolvent charity, the trustees should instruct a licensed insolvency practitioner to wind up the charity via creditors' voluntary liquidation (CVL). This is not possible for an unincorporated charity, although the trustees should still seek professional advice to ensure that the closure of the charity is properly undertaken and that the trustees are not exposed to personal liability.

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How can we help?

For trustees of a charity in financial difficulties, we are able to assist them to quickly assess the viability of the charity and put in place measures to ensure an effective turnaround of the charity's financial performance, whilst providing peace of mind to the trustees that they are properly fulfilling their duties.

Where a charity is suffering from temporary cash flow concerns, it may not always be possible to arrange additional funding with the charity's existing lender. In such circumstances, we are able to introduce alternative funders to assist the trustees to manage cash flows and avoid the threat of insolvency.

Where the causes of the financial difficulties are more ingrained, we are able to advise on turnaround and restructuring options, as well as on insolvency options. We are a member of the Charity Commission's 'approved panel for interim management services', which include restructuring and insolvency services.

For any further advice please contact Sarah Cook of FRP Advisory. Initial consultations in person or advice by telephone are free of charge.

Apprenticeship Levy

The Apprenticeship Levy will be introduced from April 2017. The levy will be payable by all employers, regardless of whether they employ apprentices or not. This will be charged at the rate of 0.5% of the gross payroll costs, if the payroll costs exceed £3m. Despite representations having been made to Government Ministers it has been confirmed that there will be no exemptions for charities. Furthermore, it will not be possible for a charity to use part of their Apprenticeship Levy to help fund the training of volunteers.

How will the Apprenticeship Levy be calculated?

The Apprenticeship Levy will be calculated by reference to the gross payroll costs upon which a charity is due to pay Class 1 (Secondary) National Insurance contributions. Where a charity is regarded as a 'public body' (as defined by the Freedom of Information Act 2000), IT will need to take into account payments made to personal service companies as part of the Apprenticeship Levy calculation.

All employers will benefit from a £15,000 allowance, meaning that nothing will be payable by employers with payroll costs below £3m.

Example

Gross payroll costs	£5m
Levy calculation at 0.5%	£25,000
Less allowance	(£15,000)
Apprenticeship Levy payable	£10,000

However, for groups of employers (including connected charities) there will be one allowance which applies to the whole group, rather than each employer within the group receiving its own allowance. Finance Act 2016 includes a provision which will enable connected employers to decide how they want to allocate the allowance.

How will the Apprenticeship Levy will be collected?

The Apprenticeship Levy will be collected via the payroll as part of the charity's real time reporting obligations. Consideration will need to be given as to whether the £3m limit has been exceeded based upon the last two years' payroll costs. Furthermore, it will be the responsibility of each charity to advise HMRC as to whether they are subject to the Apprenticeship Levy.

Other points to consider

Charities will be able to use their Apprenticeship Levy contributions to pay for training (but not salary costs) for those who meet the definition of an apprentice. Details of your Apprenticeship Levy contributions will be maintained on a dedicated digital account from which you will be able to purchase apprenticeship training from a registered provider. It is envisaged that an employer can be registered as a provider and draw down from their account the costs for providing any "in-house" training. Charities will initially have 24 months to use their Apprenticeship Levy contributions. It is proposed that from 2018 a system will be introduced for employers to transfer any unused Apprenticeship Levy, with further details to be announced.

Further guidance is still awaited ahead of April 2017. However, any charity with a gross payroll cost which exceeds £3m should be considering the charge whilst planning their budgets for next year.

Charities will also want to consider whether they have any roles within their organisation where the recruitment of apprentices may help them to derive any benefit from the Apprenticeship Levy. The Skills Funding Agency will be publishing information concerning how services will be delivered in accordance with the legislation.



Salary sacrifice or “optional remuneration arrangements”

Following the Autumn Statement, the Government has now published the Finance Bill 2017 which includes the draft legislation proposing changes to be made to salary sacrifice arrangements.

The draft legislation sets out significant changes to salary sacrifice (including flexible benefit) arrangements, referred to as “optional remuneration arrangements” which many charities and not for profit organisations use to help deliver benefits to employees in a tax efficient manner. The draft legislation is subject to a period of consultation which will close on 30 January 2017.

The Government has stated that providing benefits via salary sacrifice has established a degree of inequity between those employees who derive a benefit on a tax favourable basis compared to individuals who may only be able to acquire a similar benefit out of their net disposable income. Consequently, where benefits are provided via an optional remuneration arrangement, the benefit will be subject to tax and National Insurance on the greater of:

- the amount of salary sacrificed; and
- the cash equivalent set out in statute.

However, if the proposals remain unaltered then only the following benefits can be provided as part of an effective tax and National Insurance arrangement:

- employer pension contributions;
- employer provided pension advice based upon recommendations of the Financial Advice Market Review;
- employer supported childcare and the provision of workplace pensions;
- cycle to work scheme arrangements; and
- ultra-low emission cars.

haysmacintyre, as part of our response to the Government’s consultation, expressed concern that the changes were being introduced too quickly and did not take into account other changes which are due to come into effect from 6 April 2017, for example the Apprenticeship Levy.

We felt the consultation document did not fairly reflect:

- reasons why the benefit is being made available in the first place;
- the nature of the benefit provided; and
- the lifestyle choices an employee has made before entering the salary sacrifice.

As a response to the consultation process the Government has incorporated some transitional rules which will impact employees who have entered a salary sacrifice arrangement on or before 5 April 2017. The transitional relief will cease at the earlier of:

- end of the arrangement; or
- there is a change to the arrangement; or
- renewal of the contract; or
- 5 April 2018.

Furthermore, the transitional period will be extended to 5 April 2021 where one of the following benefits are provided via a salary sacrifice:

- cars;
- living accommodation; or
- school fees.

At present, there are concerns as to whether an arrangement can last until 2018/2021 and we will need to see if there are any changes made before the legislation is fully enacted.

The new legislation is due to come into effect from 6 April 2017. Those charities who are currently providing benefits via salary sacrifice will need to consider:

1. if the benefit is one of the “favourable” benefits, in which case no further action will be required; or
2. the benefits provided are not one of the “favoured” benefits and consideration will need to be given as to:
 - a. whether the benefit should continue to be provided;
 - b. how best to optimise the transitional rules; and
 - c. review of existing remuneration arrangements.

Charities will need to carefully consider their existing salary sacrifice arrangements and make any changes based upon legislation which will be effective from 6 April 2017 but unlikely to be enacted until the Summer.



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VAT subscription apportionments

Unannounced changes of policy introduced by HMRC following the Serpentine Gallery VAT Tribunal mean that concessions for non-profit making membership bodies to apportion their subscriptions can only be used when members have a vote in the organisation's activities.

HMRC take the view that usually a payment of a subscription to an organisation is consideration for a single supply which would either be standard-rated for most organisations, or exempt for certain sporting bodies and various types of professional body set out in the VAT legislation.

However, there has been a long standing extra statutory concession which allows non-profit making membership bodies to apportion their subscriptions and look through to the underlying benefits of membership.

For example if you are one of the professional bodies whose membership is exempt but you provide a hard copy publication as a benefit of membership then the concession allows you to treat a part of your subscription as zero-rated which has a beneficial effect on your VAT recovery.

Similarly if the starting point is that your subscription is standard-rated and you provide a hard copy publication to members you can use the concession to apportion your subscription and treat part as zero-rated to reduce the amount of output tax you have to pay out of your subscriptions.

HMRC appear to have made an unannounced change of policy on this concession and following the Serpentine Gallery VAT Tribunal case a few years back are now taking the view that the concession can only be used for non-profit making organisations whose membership have

a vote in what the organisation does, for example at an AGM.

For organisations whose members cannot vote, they take the view that the organisation is not a membership body, it is instead merely a Supporters organisation and therefore the concession cannot be used.

We have come across a number of instances of this unannounced change of policy being applied and at first individual officers were simply bringing the change of policy to the notice of the organisation concerned and advising them that the concession could not be used going forwards. However we have become aware of at least one instance where the officer has issued an assessment to recover back tax as a result of the concession no longer applying.

This was particularly galling for the organisation concerned as its members used to have the right to vote, but voted to give up this right to streamline the administration of the charity, a decision which might not have been made had HMRC's change of policy been made public.



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Get Legal

In the current climate of increased regulation and heightened scrutiny, many charities are turning their attentions to their internal policies and practices. Compliance is high on the agenda across the sector, but how can smaller organisations with limited legal budgets ensure they are meeting their legal and regulatory obligations?

Bates Wells Braithwaite's (BWB) Get Legal is a unique online tool providing a wide range of template legal documents and guidance notes for charities and social enterprises, which can be customised to the bespoke needs of your organisation through a guided step-by-step process. Once you purchase a document, you are led through a series of responsive questions, the answers to which will intelligently tailor the document to your organisation's specific needs.

The question process is intuitively designed and supplemented with notes for ease of completion. Bates Wells Braithwaite is one of the leading law firms in the UK to specialise in charity law and each document

comes with the reassurance of having been drafted by one of BWB's experts, but is optimally priced for charities and social enterprises, at about one-tenth of the cost for a solicitor to create it. From a simple employment contract, to essential governance documents, to a variety of key policies, Get Legal can help your organisation to be confident in compliance, at an affordable rate.

Karen Collins

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Future events

Trustee Training: Introduction to charity finance and reporting	14 February 2017
Trustee Training: What every trustee should know	1 March 2017
NGB Finance Special Interest Group	7 March 2017
Civil Society Board Leadership Stage 1	16 March 2017
Trustee Training: What every trustee should know - Refresher	29 March 2017

For further information on these events please visit www.haysmacintyre.com/events or contact our Events team

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