

# SocialEconomy

A quarterly bulletin of information for charities,  
voluntary organisations and social enterprises

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## Charities...

# When is a grant a grant?

**The Bath Festivals Trust Ltd appeal heard by the VAT Tribunal in October 2008 provides a reminder of the distinction between grant income (which is not subject to VAT) and income received in the provision of services (which may be subject to VAT, depending on the circumstances).**

In the Bath Festivals Trust Ltd case, the Trust argued successfully that VAT should be payable on the monies it received from Bath and North East Somerset Council - successfully overturning HMRC's decision that it should not. The decision to challenge the incidence of VAT was not a rare form of altruism on the part of HMRC, but rather they saw that if the Trust was receiving consideration for supplying services to the Council, although VAT would be payable on it, the Council may be able to reclaim it under special repayment rules which apply to local authorities. These special rules permit local authorities to reclaim VAT up to a certain overall amount. Some local authorities may be better off in awarding grants where

this overall limit might be exceeded. Moreover, the Trust would be able to reclaim the VAT it had paid on costs associated with providing that service.

A grant would not be a supply of services within the meaning of section five of the VAT Act 1996 and would therefore not benefit from this (in this case) useful treatment.

Key factors which tend towards the payment being construed as a payment for services include the following:

- the charity is providing services to the Council in return for the monies it receives. The tribunal saw the key factor as being that there was a service level agreement, the provisions of

which did not permit the trust a free reign. If it had been in receipt of a grant, the tribunal did not believe that it would have been under some of the obligations in the agreement - such as to attract at least one-fifth of its audience from among the under-25 age group, providing box office facilities to all other cultural events in the area, and so on;

- the funder imposes conditions on the charity;
- there is an 'exchange' between the funder who makes the payment and the charity which provides the services (i.e. the funder is getting a benefit);
- there is a contract which, if breached, can be sued on.

Factors which tend more towards a grant include:

- the charity approaching the funder for funding for a pre-existing activity;

- the charity, not the funder, defines the activities it will undertake and how the monies will be spent;
- the ability of the funder, at any point in the discussions, to walk away from the project.

Clearly this is a question of degree and each situation will turn on its own merits.

It is worth noting that if you are hoping to recover VAT on associated costs, your charity must be registered for VAT and charge VAT to the receiving body. You will also need to take care to ensure that your charity does not fall foul of the limits on taxable trading.

It is very important to ensure that any agreements are properly structured and taking tax advice at an early stage in any discussions is advisable. If you are in any doubt about the tax position of your charity, please seek legal or financial advice.



Sunset over Bath

## Donations to charities in other Member States

You may remember, from the last issue of Social Economy, the case of Persche in which Mr Persche, a German taxpayer was contesting the Finanzamt's refusal to give him tax relief on gifts of bed-linen, towels, zimmer-frames and toy cars to a Portuguese charity. The German authorities refused such relief on the basis that the beneficiary charity was not established in Germany. The Advocate-General opined in October last year that donations in kind constitute movements of capital and that, accordingly, the German legislation was in breach of the EC Treaty which provides for the movement of capital between Member States. Mr Persche should have been given the opportunity to produce evidence to the German tax authority to show that the objectives and management of the recipient charity were charitable under German law.

The Judgment of the European Court of Justice (ECJ) was published on 27 January 2009. The ECJ agrees with the Advocate-General. It is a breach of Article 56 of the EC Treaty for Member State

legislation to offer tax deductions on gifts to bodies within the Member State without allowing taxpayers, who wish to make cross-border gifts, the opportunity to show that they satisfy the requirements for the

relief. The onus is on the taxpayer to show that the gift meets the requirements for the relief. Although this ruling is an improvement, there is still a difference, for example, between a UK taxpayer giving to a UK charity and a French taxpayer giving to a UK charity in that the French donor may be obliged to produce evidence to show that the UK charity manages its charitable activities in accordance with French tax statutes whereas the UK donor would not have to. So whilst this is a big step towards free movement of gifts across Europe, it does not mean complete equality. As yet, HMRC has not commented on the ruling.



## Don't Drain Us... the fight against the new 'Rain Tax' continues

**Churches, charities and clubs are continuing a fight to convince Ofwat to follow government guidance and not bill them as if they are commercial buildings. Under the new regime, non domestic properties will be charged on the size of their site area instead of the rateable value of the property.**

'Don't Drain Us' is seeking a review of regulations that would introduce a charity band or the return to rateable value charging for churches, charities and clubs for their water drainage costs. Water bills could be increased tenfold or

more if the rules are applied. It is also seeking an investigation into why Ofwat ignored government guidelines and encouraged water companies to charge churches, charities and clubs as commercial enterprises.

Churches, charities and clubs are encouraged to vote against these new measures. Go to [www.dontdrainus.org](http://www.dontdrainus.org) to have your say. The Charity Tax Group is also collating information about the increased cost from affected charities to lobby for change. If you know your charity will be affected, please contact them via: [www.ctrg.org.uk/contact](http://www.ctrg.org.uk/contact).

## Industrial and provident societies - update on share capital and charitable status

**The focus for organisations wishing to attain charitable status has generally been on the objects - if the objects are charitable, it is a charity, if they are not it is not. However, private benefit can also stop an organisation from being deemed charitable.**

Recent correspondence with the Charity Commission has shown that they take a wide view of private benefit. Their stance is that if interest on shares (something unique to industrial and provident societies) can be paid to members of an Industrial and Provident society, that society is not charitable. This means that unless and until the Charity Commission revise its opinion, any Industrial and Provident society wanting to secure charitable status should

consider removing any power in its rules to pay interest on shares, whether in money or by the issue of further shares. Taking out a loan and paying interest on a loan is not, however, regarded as an automatic bar to charitable status.

For legal advice or assistance on obtaining charitable status for your Industrial and Provident society, please contact Malcolm Lynch at Wrigleys Solicitors LLP by emailing [malcolm.lynch@wrigleys.co.uk](mailto:malcolm.lynch@wrigleys.co.uk).



# Recognising and managing insolvency risk

As charities face increasing costs coupled with a likely reduction in income as the credit crunch bites, it is increasingly important for trustees to not only know the indicators of insolvency but, also, to take active steps to manage the insolvency risk to their charity.

Alarm bells should ring when there is pressure from creditors chasing overdue payments, when your charity is having to run down reserves on a regular basis to meet outgoings, where current liabilities are not covered by current assets (bearing in mind that anything in restricted funds may not be available to meet current liabilities) and where expected expenditure exceeds foreseeable income.

For directors of charitable companies, the provisions of the Companies Act 2006 apply. Such trustees not only have the common law duty to act in the best interests of the charity, they must also take care to minimise potential loss to the company's creditors.

The prospect of insolvency is a worrying topic for any trustee who is concerned about the financial position of their charity. If you are

concerned about the financial prospects of your charity, you may wish to seek legal or accountancy advice immediately. Trustees may safely incur expenditure on such advice since it may lead to a better realisation of assets. They may guide trustees to an insolvency practitioner where appropriate. In small charities it can be difficult to secure the services of an insolvency practitioner since there are no assets out of which the expenses of the insolvency practitioner can be met. Trustees in those circumstances may find that they have to take a hands on approach to winding up the charity. Information may also be obtained from the Insolvency Service website [www.insolvency-service.co.uk](http://www.insolvency-service.co.uk) and the Charity Commission in its publication CC12 - Managing Financial Difficulties and Insolvency in Charities.

Even if none of these alarm bells are ringing for you, you may wish to consider preventative action as a matter of good governance. As a starting point there are a number of questions you might ask:

- When did your charity last carry out an insolvency risk assessment?
- Is the charity able to pay its debts as and when they fall due?
- Are the assets greater than the charity's liabilities?
- How secure and diverse is the source of income?
- Charities which are dependent on a sole source of income may be particularly vulnerable. Are there significant liabilities on the horizon?
- Are there significant fixed costs?
- Do your trustees have sufficient time and skill to devote to running the charity?
- Do your trustees regularly and fully consider financial reports?
- Are financial reports available in advance of meetings?
- Is actual expenditure monitored against budgeted expenditure?

# Exempt and excepted charities update

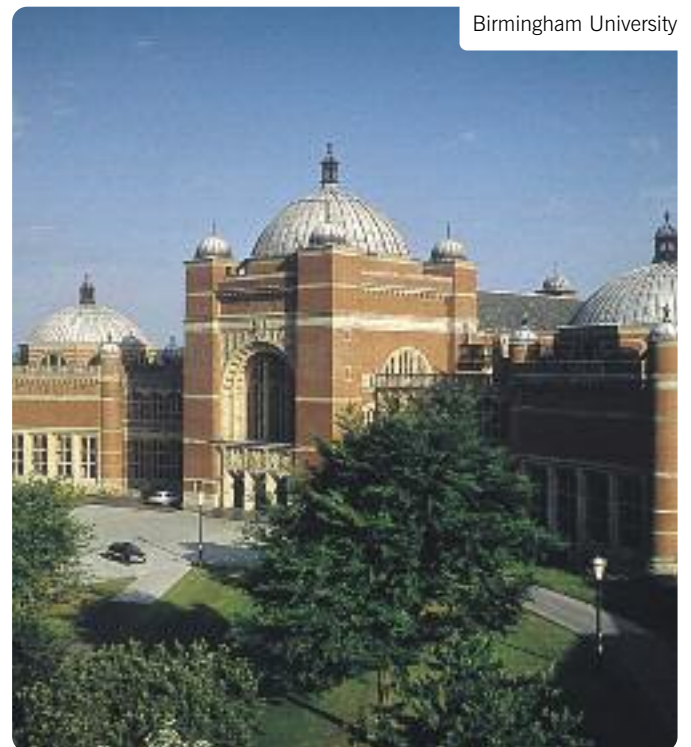
The Charities Act 2006 changes in relation to excepted charities (charities which are excepted from the requirement to register with the Charity Commission provided certain criteria are met) came into force on 31 January 2009, under the Fifth Commencement Order. Traditionally, the main types of charities that have been excepted from registration are voluntary and foundation schools, scouts and guides troops, and certain armed forces charities.

The main change is that from 31 January 2009, any of these charities with an annual income above £100,000 will have to register with the Commission. The Commission is aiming to get these charities registered by 1 October 2009, as from that date the Commission will also begin the process of registering all exempt charities (charities which are exempt from registration with the Charity Commission). Exempt charities are specified in Schedule 2 of the Charities Act 1993 and include mostly universities and higher learning institutions, some national museums and galleries, and industrial and provident societies.

Foundation and voluntary schools are potentially affected by these changes. They were exempt charities, but, from 31 January they

are now excepted charities. In order to put these formerly exempt charities on an equal footing with the other exempt charities, they will have to register from 1 October 2009 if they have an annual income exceeding the £100,000 threshold. Exempt and excepted charities below the £100,000 threshold will not be obliged to register until 1 October 2012. Any exempt charity which is regulated by a 'principal regulator' will not need to register with the Charity Commission, regardless of annual income. For example, the Higher Education and Funding Council for England will regulate most English universities (Cambridge, Durham and Oxford excepted).

The school's delegated budget from the local authority is not counted within the income as the school only acts as the local authority's



agent in spending the budget. Slightly confusingly, capital grants will be considered income so within 5 or 10 years, it is likely that most

(if not all) of these schools will have to register. Amongst other things, this will have accounting implications in many cases.

# Employment...

## Long-term sickness and holiday entitlement



The long running saga of *Stringer v HMRC* (previously known as *Ainsworth*) has taken another leap forward following the recent decision of the European Court of Justice (ECJ), which held that a worker who is on sick leave for the whole of the annual leave period is still entitled to statutory paid leave even though they are not actually at work. The right to paid holiday is not lost and it is for the national courts to decide whether the paid leave can be taken during the sickness absence or is to be carried over.

The House of Lords must now give a final decision, in light of the ECJ judgement. However, there still remains the practical difficulty of fitting the ECJ judgment within the statutory regime, which still requires an employee to actually take holiday, thereby giving rise to a notional return to work which in itself is based upon fitness to work, as well as the statutory restrictions on carrying forward statutory holiday from one leave year to the next.

## Reasonable adjustments and knowledge

**Under the Disability Discrimination Act an employer is required to make reasonable adjustments. This does not apply where the employer did not know and could not reasonably be expected to know that the person was disabled or would be at a disadvantage.**

The Employment Appeal Tribunal (EAT) have ruled that in order for the exemption to apply each of the following four parts of the test have to be satisfied, i.e. the employer:

- does not know that the person has a disability;
- does not know that that person is likely to be at a substantial disadvantage compared to a person who is not disabled;
- could not reasonably be expected to know the person had a disability; and
- could not reasonably be expected to know that the person is likely to be at a substantial disadvantage compared to a person who is not disabled.

Clearly, the test has become more difficult but, by no means impossible, for employers to satisfy.

The key issue is one of awareness of the potential for disability discrimination and the potential for those who are disabled to be put at a substantial disadvantage. The test is not that anyone disabled may be disadvantaged but, that "that person" in particular either has a disability or is disadvantaged. For example, placing a job advertisement in a newspaper may well disadvantage all potential blind applicants (have you considered alternative means of advertising your vacancies?); but, that is not relevant where the person actually disadvantaged has

some other form of disability, for example the adjustment required relates to some less apparent disability for example time off work to attend medical appointments. This issue is one of knowledge but it does not mean that the correct course for an employer is to ignore it. The "ought reasonably to have known" provision allows knowledge to be inferred, for example through a conversation between the disabled employee and a line manager even in situations where on a job application form the employee may not expressly disclose any disability. Where the employer encourages a positive environment which allows an employee to disclose, in confidence, any disability; where the employee refuses to make any disclosure (where the employee is not acting reasonably) then an

employer will be better placed to argue both that it did not know of any disability and could not reasonably be expected to have known. (**Eastern and Coastal Kent PCT v Gray.**)



# Charities and Social Investment...

## Social Investment - an alternative to grants

**Social investment by a charity is not about making money. It is not even about making money ethically. Instead, it is investment which is intended to further the objects of the charity. So if your objects are to reduce unemployment, you may invest in start-up businesses if they will provide jobs for the unemployed and the public benefit outweighs the private benefit. The loan is hopefully repaid and then can be re-lent.**

It is an idea seen in charities working in the developing world. A charity gives a cow. The beneficiary gives the first calf back to the charity. She/he benefits from the milk, the future calves and the wealth of having a cow. The charity has another cow to give to someone else on the same terms.

It sounds good but there are risks to consider and factors to weigh up. Trustees always have a duty of care to their charity and must act within the powers and pursue the charitable objects for which their charity was established. It may be that trustees need to seek independent financial advice as to the appropriate level of return for a loan or in assessing the financial prospects of a business. There are a number of charities and

not for profit organisations which engage full-time in business lending in the UK or the developing world - is it sensible to use their experience? Social investment is not treated as an investment by the Charity Commission, but is seen as a different application of funds for grant making purposes. Whilst it may seem to be a win-win situation, there is a risk that if you have banked on getting a certain return on your investments and they fail, your charity may not have the funds that it anticipated having. Depending on the social investment policy you decide to pursue, a high default rate on loans may suggest that the charity had poor checks and balances in place which may damage its reputation.

If your charity is thinking of engaging in social investment, the trustees should set out in a clear policy both why and how the charity does so. What are the priorities for your particular charity? Do you favour projects which are likely to have a good return or do you favour those which may be riskier but, if

successful, will have the most social benefits? Lastly, the charity should not just hand the money over, but the trustees should consider how the relationship will end before it starts. Particularly, if lending to or buying shares in a non-charitable organisation, the charity should monitor how the funds are used. When is the loan to be repaid and on what terms? What if the organisation uses it for non-charitable purposes or changes its objects or starts working in a different area?

In the present economic climate, when trustees may be seeking to conserve their grant making activity social investment might be an interesting alternative. For example, Oikocredit, the Dutch not for profit developing country micro lender, offers a two per cent financial rate of return and a social return from its micro credit activity. For its prospectus visit [www.oikocredit.org.uk](http://www.oikocredit.org.uk) (**Charities and social investment.** [www.charitycommission.gsi.gov.uk](http://www.charitycommission.gsi.gov.uk))



## Local Authorities...

### Duties as trustees

**It has recently been reported in Third Sector that Birmingham City Council has been accused of inappropriate use of a charitable trust's property. Highbury, a 31 acre estate, was left by Joseph Chamberlain to the people of Birmingham in the 1930s for general charitable purposes. The Council, which is the sole trustee of the charity, has been using the main building on site as a conference and banqueting centre and another building as offices for social services staff without, it seems, paying rent to the charity. The Moseley Community Development Trust complained that there is a conflict of interest in the Council running the property as landlord and tenant of the buildings.**

This serves as a reminder for any local authority which acts as trustee of a charity, they must comply with their duties to act in the best interests of the charity including the duty to avoid conflicts of interest. Charity Commission guidance highlights potential dangers for local authority trustees to be aware of: they are not free to deal with the property of

the charity in the same way as they deal with corporate property; conflicts often arise between the interests of the local authority and its council tax payers and those of the charity and its beneficiaries on the other hand; and whenever local government reorganisation occurs, care should be taken to tell the successor what property is held on charitable trusts.



Highbury Hall, Moseley

Anyone affected by this may be interested to read Charity Commission guidance CC29 - Charities and Local Authorities, CC3 - The Essential Trustee: What You Need To Know, OG 56 B1 - Operational Guidance on Local

Authorities and Trustees and A Guide to Conflicts of Interest for Charity Trustees. These can all be downloaded free from [www.charitycommission.gov.uk](http://www.charitycommission.gov.uk). (**Third Sector 24.2.09.**)

# Social Enterprise...

## Community Interest Companies (CICs) - a consultation

The Department of Business, Enterprise and Regulatory Relief (BERR) has announced in February 2009 a consultation on proposed amendments to the CIC regulations. A number of the amendments relate to other legislation such as the 2006 regulations setting up the asset locked Community Benefit Society (CBS) under Industrial and Provident Society legislation.

Other proposals relate to defining sections of the community and the consideration of not only community benefit, but also detrimental effects. Interestingly, there is no consultation on what is regarded as one of the more problematic features of the CIC, namely the cap on distributions. However, that should not prevent you from making a submission on that account.

Of course, if that is a problem, the potential of conversion of the CIC to a CBS may be a way round the distribution limit since the CBS distribution lock has greater flexibility since it bases the distribution lock on the potential to obtain commercial capital.

[www.BERR.gov.uk](http://www.BERR.gov.uk)



# Environment...

## Implementing a stern report



Like buses, three pieces of legislation which came along at the end of 2008 can be viewed as long overdue. The Climate Change Act 2008, the Energy Act and the Planning Act will have a substantial impact on the UK's energy future until 2050. Inevitably, it will have a great impact on businesses, charities, communities and land owners too.

The Climate Change Act obliges the UK Government to cut greenhouse gas emissions by 80% by 2050. A carbon budgeting system, which caps emissions over five year periods, will act as a five year framework. The Energy Act sets out a system of subsidy for renewable energies to 2037. Under the new system renewable technologies are banded by technology with larger subsidies for emerging technology

such as wave power and off shore wind. Small home size renewables, including renewable heating will be able to receive a small fixed tariff.

The most controversial of the new laws is the Planning Act which permits the Government to create an infrastructure planning commission to take decisions over large infrastructure projects such as energy projects over 50 MW.

Contributors to this edition of Social Economy are Chris Billington, Sue Greaves, Natalie Johnson, Malcolm Lynch, Sylvie Nunn, Helen Wray and Tim Wrigley.



Could we help with your banking needs?

Contact Unity Trust Bank, Nine Brindleyplace, Birmingham, B1 2HB, tel: 0845 140 1000 or visit [www.unity.co.uk](http://www.unity.co.uk)

If you require legal advice on charity and social economy law

Please contact Malcolm Lynch at Wrigleys Solicitors, 19 Cookridge Street, Leeds, LS2 3AG, tel: 0113 204 5724, or visit [www.wrigleys.co.uk](http://www.wrigleys.co.uk)