



2010 has been a busy year for the charity sector, with changes coming thick and fast. This update outlines some of the new opportunities and requirements faced by the sector in light of these recent changes.

Charitable Incorporated Organisations

A Charitable Incorporated Organisation ('CIO') is a new corporate structure designed specifically for charities.

At present corporate charities, normally companies limited by guarantee, are subject to dual regulation by the Charities Commission and company law. A CIO offers the opportunity for a charity to operate as a corporate entity, but be regulated solely by the Charities Commission.

This offers the following advantages:

- the members and trustees can be personally safeguarded against any liabilities the charity incurs (unlike an incorporated charity);
- the charity has its own legal personality and can conduct business in its own name; and
- the charity has only one regulator to comply with and one set of legislation.

The legislation needed to introduce CIOs as an available structure is not yet in place, but it is expected to be by early 2011.

It will be possible for existing unincorporated and incorporated charities to change to a CIO. This will be something to consider next year when the details of the new structure become clear.

This may be particularly relevant to small or medium sized charities which prefer not to be subject to the additional layer of administration necessitated by a company structure but whose trustees are concerned by the potential liabilities whilst unincorporated.

What is a charity for tax purposes?

Finance Act 2010 introduced a new definition of 'charity' for the purposes of defining which charities and other organisations are entitled to benefit from UK tax reliefs. This is broadly in line with the previous guidance, with a number of notable exceptions.

There is no sign as yet that the coalition government has plans to overrule these changes, which were passed under the previous government.

Under this guidance an entity qualifies as a charity for tax purposes, and so attracts the various valuable charity tax reliefs and is able to reclaim money under gift aid, if it satisfies the following criteria:

- it is established for charitable purposes only, and is restricted by its governing documents to using all its income and assets for its stated charitable purpose;
- it is established in the UK, in another EU member state, in Norway or in Iceland;
- where it is required to register with a charity regulator, for example the Charities Commission, it is so registered; and
- it meets the management condition, that is its management are 'fit and proper persons'.

One major change here is the extension of charitable tax exemptions to charities in the EU, Norway and Iceland, where previously they were limited to UK charities.

Along with this new definition, HMRC has changed its registration requirements for new charities.

Any new charity, or existing charity which has not previously claimed gift aid repayments or charitable tax exemptions but now wishes to, is required to complete a Form CHAI.

On receipt of this form HMRC will judge whether the charity meets the various requirements for charitable status. If approved, a charity will be allocated a charity tax reference and can then reclaim gift aid and claim the various other tax exemptions.

Charities face 'Fit and Proper Person' test

The new definition of charity for UK tax purposes includes a requirement that organisations must satisfy the 'management condition'.

For a charity, this means that its managers must be fit and proper persons.

Legislation does not provide a definition of a 'fit and proper person', but HMRC have issued some guidance on the matter.

Their definition of 'managers' is designed to cover any person who has general control and management over the administration of the charity, including trustees and directors.

The factors that HMRC will take into account when assessing if someone is fit and proper include:

- A history of tax fraud
- A history of other fraudulent behaviour, including misrepresentation or identity theft
- HMRC knowledge of involvements in attacks against or abuse of tax repayment systems
- Information or evidence pointing towards a heightened risk of involvement in other fiscal or financial impropriety
- Being barred from acting as a charity trustee by a charity regulator or court, or being disqualified from acting as a company director

Where an individual is found not to be a fit and proper person, HMRC will have the discretion to decide whether the management condition has been satisfied.

If a charity appoints a person who unbeknown to them is not a fit and proper person, then HMRC may still treat the charity as having met the management condition throughout the period that individual was in office.

Correspondingly, the charity will not lose its entitlement to the tax reliefs in force.

For existing charities, HMRC will not routinely ask for proof that managers and fit and proper persons.

If challenged however, HMRC will expect a charity to be able to show they have given proper consideration to the suitability of the people they have appointed to positions of trust.

Practical steps

It is suggested that a declaration is obtained for any new managers, trustees and directors appointed post 5 April 2010. There is a template provided for doing this which can be found at <http://www.hmrc.gov.uk/charities/guidance-notes/chapter2/model-dec-ff-persons.pdf>.

It is worth considering obtaining a declaration for all current managers, trustees and directors, so that records are readily available if HMRC ask for proof in the future.

Charities should review their position now, to ensure that they do not lose their valuable charitable status and tax reliefs.

Substantial donor legislation

The substantial donor legislation deals with the relationships between charities and their larger donors, and places limits on the benefits which can be received by large donors. Tax charges can arise on breaching these limits.

The rules have been controversial since their introduction in 2006,

with charities arguing that they are unworkable, and potentially catch innocent transactions entered into with no tax avoidance motive.

The coalition government's emergency budget on 22 June 2010 announced that these rules will be replaced. HMRC is consulting informally on the replacement clauses and final legislation is expected later this year.



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