

## TAX EFFICIENT CHARITABLE GIVING – AN UPDATE

Over recent years, the Chancellor has encouraged charitable giving by expanding the range of assets which can be donated to UK charities with tax relief, as well as simplifying the paperwork required. Many billions of pounds are donated annually, but only about a third of this is given in a tax efficient manner. At this time of year and following the Finance Act 2006, it is timely to review the various giving options available to the taxpayer.

This update sets out the current position regarding the income tax and capital gains tax relief for various types of gifts. The long-standing inheritance tax relief for gifts to UK charities continues undisturbed.

### GIFT AID

The simplest and most common method of giving by individuals is via qualifying donations (more familiarly known as the Gift Aid scheme). This covers cash gifts including those made under Deeds of Covenant. Any sum given to a charity under Gift Aid will potentially qualify for tax relief at the higher rate of 40%. The charity is able to claim tax back from the government, thus enhancing the value of the gift. If the taxpayer has not paid enough income tax or capital gains tax in the year of claim, any shortfall must be accounted for to the Revenue by the taxpayer and the scheme is therefore unsuitable for non-taxpayers. For a higher rate taxpayer, i.e. one who pays tax at 40%, tax relief is given on Gift Aid payments as follows:

- ▶ A gift to charity of £100 is treated as paid net of basic rate tax of 22%.
- ▶ Charity is able to reclaim £28 (being the basic rate tax on the grossed up gift of £128).
- ▶ Higher rate taxpayer obtains tax relief of £23 (being relief at 40% less 22% on the grossed up gift) so that the net cost of the donation is only £77.

A taxpayer is able to claim relief in a particular tax year for all Gift Aid donations made during that tax year and after the tax year end, up until the date of submission of the tax return. Of course each donation can be claimed only once, and hence good records need to be kept.

This flexibility regarding the year of claim is valuable if a taxpayer pays tax at 40% in one year but a lower rate in the subsequent year, and also results in relief being obtained earlier.

The taxpayer must make a Gift Aid declaration to the charity in order to obtain relief. This can now be done over the Internet or orally so long as the charity keeps appropriate records. Once made, a Gift Aid declaration is effective for all future donations to the same charity by that individual, until cancelled.

### BENEFITS RECEIVED

Generally, Gift Aid tax relief will be denied if the donor derives some benefit from the gift. For example, the purchase of an item at a charity auction will be treated as a payment for goods or services and no element will qualify for relief. There are limited exceptions for very small benefits. Benefits may be provided if they amount to no more than 25% of the value of a gift up to £100, £25 for a gift between £100 and £1,000, or 2.5% for a gift over £1,000, with a maximum benefit per person of £250 from any one charity in any tax year. There are also limited exceptions for free or reduced admission by charities established to maintain buildings or certain other types of property. Substantial gifts may also give rise to difficulties under the recently enacted anti-avoidance rules – see further below.

### PAYROLL GIVING

This is a separate scheme from Gift Aid. An employee or person in receipt of a pension subject to income tax is able to make charitable donations by deduction from his wages or salary subject to PAYE. Tax relief is given as if the amounts deducted were allowable expenses of the donor. Hence, if an employee donates £100 in a tax year and is a higher rate taxpayer he obtains tax relief of £40 so that the net cost is £60. Note that relief to the taxpayer is greater than that given under Gift Aid, although the charity is not able to reclaim any tax. Deductions are not allowable for National Insurance purposes.

Deductions made under this scheme must be paid over to an approved agent or agency charity which passes donations on to the chosen charities.

### GIFTS BY TRADERS

A person (including a company) carrying on a trade is also able to give to charity plant or machinery used in the business, articles made or sold in the course of its trade or medical supplies or equipment for humanitarian purposes, with no notional receipt having to be brought in as income. A gift of plant and machinery to a charity is deemed to have taken place at nil value for the purposes of capital allowances. Such gifts are zero rated for VAT purposes.

### GIFTS OF SHARES

Tax relief is also available for a gift (or sale at undervalue) of shares quoted on a recognised stock exchange, units in authorised unit trusts, shares in OIECs and interests in offshore funds.

For these assets relief is given for both capital gains tax and income tax. Any gain crystallised on the gift is not charged to



capital gains tax (but any loss is disallowed). The 'relevant amount' of the gift is deductible from the taxpayer's income, saving tax at the applicable marginal rate. The 'relevant amount' is the value of the 'net benefit to the charity', which will normally equate to the market value of the shares (as adjusted by costs of transferring the asset and any benefit received in respect of the gift).

The taxpayer obtains a greater amount of tax relief than would be the case with a gift of cash, but the charity cannot reclaim tax on the gift.

If a taxpayer wishes to donate £10,000 to a charity, it would be more tax efficient to give quoted shares showing a large gain rather than cash, since both income tax relief and capital gains tax relief would apply. On the other hand, the charity cannot reclaim basic rate tax on such donations. Claims for tax relief are made on the taxpayer's tax return.

Gifts of other assets (eg unquoted shares) do not give rise to gains subject to capital gains tax but income tax relief is not available.

#### **GIFTS OF LAND**

Relief is also available in respect of a gift of freehold or leasehold land in the UK and is given in the same way as for quoted shares. Joint tenants or tenants in common must all make a gift of their respective interests to the same charity; tax relief will be apportioned between them as they may agree.

Relief is dependent upon the donor obtaining a receipt from the charity concerned confirming the interest acquired and the date of disposal.

There are various clawback provisions if the person making the gift (or anyone connected with him) obtains an interest in any part of the property gifted before 31 January following the end of the fifth tax year in which the gift was made (in the case of a company, before the sixth anniversary of the end of the accounting period in which the gift was made).

Acquisitions of land by charities are exempt from Stamp Duty Land Tax provided that the land is used for charitable purposes and the transaction is not undertaken for the purposes of avoiding Stamp Duty Land Tax.

#### **TAX REPAYMENTS**

Taxpayers are able to indicate on their tax returns that part or all of any tax repayment due to them should be paid to a charity of their choice under Gift Aid. The surrender of the repayment can itself be treated as a donation under Gift Aid.

#### **COMPANIES**

A company may claim relief for certain gifts donation made, as a charge on income.

Such gifts include cash, which is paid without the deduction of tax (no Gift Aid declaration required), gifts of shares quoted on a recognised stock exchange, units in authorised unit trusts, shares in OIECs, interests in off-shore funds and gifts of freehold or leasehold land in the UK.

#### **ANTI-AVOIDANCE: 2006 FINANCE ACT**

A less than welcome provision of the Finance Act 2006 concerns charities' transactions with substantial donors. A substantial donor is broadly a person who makes tax efficient gifts of at least £25,000 to a charity in a period of 12 months or at least £100,000 in a period of 6 years. A donor remains a substantial donor for the following five chargeable periods after exceeding one of the above limits. Various transactions between a charity and a substantial donor are caught, including the sale or letting of a property by a charity to a substantial donor, or the provision of sums by the charities to the substantial donor. It is, perhaps, bizarrely, the charity which suffers tax consequences in such situations; there is no clawback of tax relief from the donor. These provisions are complex and specific advice should be sought.

#### **SUMMARY**

The donation regime has become broader in scope over recent years but more complex. Circumstances will vary from donor to donor and advice should be sought as to the most tax efficient way of giving, in order to benefit from available reliefs.

This update is for information only and does not constitute professional advice. For advice on your particular circumstances or for further information, advice or assistance in relation to any of the matters raised above, please speak to the authors or your usual Dixon Wilson contact.

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