PKF FRANCISCLARK

Chartered accountants & business advisers

Charity *and* Not-for-Profit

Autumn/winter 2018

introduction

Duncan Leslie, Head of Not-for-Profit
duncan.leslie@pkf-francisclark.co.uk

It is over two years since the referendum on Brexit. Everyone said that it would be a painful process and it certainly has been so far. Adding in a volatile political equation has led to a process that has perhaps been more painful than necessary.

However, over those two years, not much has changed. The economy has spluttered along and we have all been trying to prepare for Brexit, without knowing what we are preparing for. Whilst some things are a bit clearer, most of the important elements relating to trade are yet to be agreed. The future availability of grant funding, and in what format, has been somewhat further down the list of priorities.

What we do know is that the withdrawal negotiations will be conducted and agreed as a single package. Some elements will influence others. Nothing is agreed until everything is agreed. Therefore the uncertainty is likely to continue late into Q1 2019. We have been managing this uncertainty for a long time and should prepare for the changes to come through more rapidly than to date. This will require everyone, including charities and those in the not-for-profit sector, to be agile and responsive.

The changes that come through could have a wide range of impacts. These could vary from 'nothing much changes' to 'our world falls apart' and everything in between. Some of the possible consequences are as follows:

Possible impact	Possible consequences for NFP sector
Lower growth	Increased scarcity of donation income
Asset values fall	Lower investment returns
Scarcity of funding	Difficult to invest in new ventures
Strain on public finances	Increased demand for charitable services
UK less attractive place to work for EU nationals	Difficulty in recruitment of suitable staff
Targetted tax changes	Loss of gift aid, or more gift aid availability?
Exchange rate volatility	Uncertainty of overseas investment returns
Different grant markets	More diverse public money income sources
Changing political arena	Goalposts constantly moving
Investment in infrastructure	Opportunities for access to investment funds

Whilst some of these changes may be immediate on Brexit, some may take longer or may not happen at all. Some of these impacts and consequences are quite gloomy, but entirely possible. We would certainly advise organisations to plan for the worst and ensure they develop a reserves policy if they do not already have one in place. Our next article discusses this topic in more depth.

Of course, it could be that none of the outcomes we have suggested happen, and we are at the 'nothing much changes' end of the spectrum. However, it is clear that given the potential outcomes, charities will need to be agile, decisive and entrepreneurial to make the most of what could be a very difficult period for the sector.

Developing a reserves policy

There is no 'one size fits all' approach to producing a reserves policy and no 'right' answers, but a thorough review process should help identify an appropriate target level or range (it does not have to be an absolute) for reserves.

Here are some ideas on factors to consider:

The starting point is to identify **why your charity needs to hold reserves.** For example, to maintain delivery of outcomes, to protect beneficiaries, to respond to variations in funding, and to 'buy some time' in the event of unexpected events or opportunities.

Next, **understand the types of reserves your charity holds.** Your reserves policy needs to focus on free reserves (funds that can be spent freely on charitable purposes), which are as follows:

Total reserves
- Less: endowments and restricted reserves
- Less: designated reserves
- Less: fixed assets and programme assets

= *free reserves*

Look at your income and expenditure. Reserves policies are often framed in terms of a number of months' expenditure but that isn't necessarily logical, especially if expenditure is not the same month on month. It is better to think through the variables rather than taking a formulaic approach.

The less stable or reliable an income source is, the bigger the potential risk. So, consider how you are funded and look at key income streams in terms of both amounts and percentage of total income. How far in advance do you have certainty over income?

Consider how much it costs to deliver your services and the key variables. What is your flexibility to reduce costs if the organisation comes under financial pressure and how many people would be affected (both staff and beneficiaries)? Take into account non-cash items such as depreciation and remember to exclude restricted or designated fund expenditure as that should be covered by equivalent income.

Think about your forecast cash flow, including capital expenditure. Stress-testing the forecast for variations in timings or amounts will help to clarify what you might need by way of a contingency. Remember that reserves not held as cash (e.g. investments or term deposits) may incur interest penalties or crystalise unrealised losses if they are required to be converted into cash at short notice.

CC19 indicates that trustees should consider what would happen if the charity were to close and how this would be achieved in an orderly fashion. This should not be the main focus of a reserves policy but an awareness of potential 'costs of closure' can be useful.

Stephanie Henshaw, Corporate Partner
stephanie.henshaw@pkf-francisclark.co.uk

Finally, remember that the SORP requires the reserves policy to explain:

- The reasons why the charity needs reserves - i.e. what issues do they need to address?
- The level or range of reserves the trustees consider appropriate;
- Whether the charity already meets the target and, if not, the plans for reaching it;
- How reserves are monitored and reviewed;
- The actual level of reserves in the annual report, identifying and reconciling clearly the free reserves figure.

The new

Charity Annual Return 2018

is here

Louise Bridgett
louise.bridgett@pkf-francisclark.co.uk

After consulting with the sector last year, the Charity Commission has now launched the new-look 2018 Annual Return. All registered charities with an income of more than £10,000 and all Charitable Incorporated Organisations (CIO's) regardless of size must complete an annual return online within ten months of their year end.

Whilst the Commission recognises that there are a number of amendments and additional requirements, particularly for larger charities, they are confident that the user will find the experience more positive. To aid transition, the Commission has made some of the requirements optional this year to allow charities to collect the data in time for next year's return.

The function to view and amend details about charity trustees, contact details etc. has now been made separate and can be updated at any time. The charity will be prompted to check that these details are correct before submitting the Annual Return.

There are three key areas of additional focus in the new return:

Salaries and benefits

The new annual return asks for a breakdown of salaries in income bands and also the total amount of employee benefits paid to the highest paid member of staff.

Overseas expenditure

Recognising the potential additional risk that transferring money overseas can bring, the Commission is seeking to collect information on how charities manage these transfers and monitor overseas funds.

Overseas income

The charity will need to answer questions breaking down the sources of income for each country from where money has been received.

The Commission recognises that charities may need to make changes to their financial systems in order to be able to report some of this information. Therefore, the parts of the questions relating to other private institutions and individual donors are not mandatory until the 2019 return. The same is true of the questions relating to transfers of money outside of the regulated banking system and about monitoring overseas expenditure controls and risk management.

Charities and *Making Tax Digital*

The Government are introducing their Making Tax Digital for VAT (MTDfV) legislation from 1 April 2019. This is due to affect all VAT registered businesses, including charities, with a taxable turnover in excess of £85,000 a year. However, a recent announcement by HMRC issued a six-month deferral for around 3.5% of these affected businesses.

The deferral has been applied to a number of entity types, including: trusts, 'not-for-profit' organisations that are not set up as a company (this includes some charities), VAT divisions and VAT groups. These groups are all now mandated to use MTDfV from 1 October 2019.

MTDfV does not apply to charities that are not registered for VAT or which have registered voluntarily and have a taxable turnover below the mandatory registration threshold.

If an organisation is affected by the changes, it must ensure that the VAT returns it prepares are submitted to HMRC directly by software and not through the existing Government Gateway for the period commencing on or after the applicable date (1 April 2019 or 1 October 2019). Therefore, the charity's method of record keeping must be capable of interacting directly with HMRC and the underlying records must be kept in a digital format by this time.

Many accounting software packages are working with HMRC to develop their digital links (application programme interfaces or APIs) with HMRC. Charities may wish to contact their accounting software package supplier to establish when their package will be able to link to HMRC for MTDfV in order to satisfy themselves of their ability to comply with the new regime.

Alternatively, our recommendation where right for the charity, is a move to cloud accounting. MTDfV and cloud accounting are a real opportunity to truly digitalise the way you work. There are a variety of products on the market that provide benefits beyond the basic bookkeeping functionality that can really benefit a charity; from the removal of the manual entry of invoices and bank transactions, to electronic payment solutions for collection

of subscriptions, and customisable reports for fund accounting and management information purposes.

Cloud accounting with PKF Francis Clark is about more than just software, it is a way of working together to achieve your charity's goals. With remote log-in we will be able to guide your charity and spot potential issues or planning opportunities early on. The availability of real-time, critical information allows you to spot patterns and trends, and take advantage of or address them quickly.

There are additional challenges in complying with MTDfV for those charities which are partially exempt for VAT and/or calculate a non-business restriction of input VAT. This is because most accounting packages do not offer the capability to perform these calculations within the software. HMRC will allow such calculations to be made separately, e.g. on a spreadsheet, so long as any adjustment is posted to the software by way of a journal, or similar, prior to the VAT return being submitted to HMRC.

HMRC has confirmed there will be a 'soft landing' period for organisations to have in place digital links between all parts of their functioning software between April 2019 and March 2020. However, there must be a digital link in place between the charity's accounting records and HMRC for the first VAT reporting period starting on or after either 1 April 2019 or 1 October 2019, whichever applies.

Although April 2019 may sound far away for those organisations affected by the earlier implementation date, charities with a year-end post 31 March 2018 are already in the financial year that will require an element of MTDfV compliant record keeping.

Sue Palmer, Business Solutions Manager
sue.palmer@pkf-francisclark.co.uk

For further information or advice on MTDfV, please speak to your usual adviser or Sue Palmer on 01752 301010.

Employee *benefits*

It might have started with the introduction of auto-enrolment legislation. An industrial-scale revolution of workplace savings implemented by the Government from April 2012 which - whatever the 'whys' and 'wherefores' of the legislation - appears to have brought about greater employee and employer saving, and a greater awareness of the importance of preparing for retirement.

The unintended consequence is that employees are now also much more aware of their wider financial situation, what risks there are to their financial security, what they can do to mitigate these risks and crucially, what they can expect from an employer. These expectations might loosely fall under the banner of 'employee benefits'; employees can now ask not what they can do for their employer, but what their employer can do for them. This should not be seen as a threat but rather as an opportunity.

No doubt there are many employers out there who felt that auto-enrolment was thrust upon them, with unrealistic timescales, overly-prescriptive legislation and additional cost. The same is not true of other employee benefits; there is currently no legal compulsion to offer a group life benefit to staff members, for example. So, moral misgivings aside, why would an employer spend more than it has to on its workforce? For most employers, employees are the single largest expense that impacts on the bottom line.

The answer is revealing for those in the not-for-profit sector. Various studies exist around the level of employee turnover in various sectors. However, they all agree that staff turnover in the not-for-profit sector is higher than the median for UK employers. Providing benefits that your staff appreciate can help increase their satisfaction at work, and inspire greater loyalty and productivity in the workplace.

Tom Parry, Chartered Financial Planner
tom.parry@pkf-francisclark.co.uk

Cost is not the only issue, though, or even the most important. Retention of staff is likely to be a key focus for many organisations.

Encouragingly, a recent study by group risk insurer Ellipse, has shown that the number one reason employers state for offering employee benefits, is to reward staff. However, what is suitable as a reward for one workforce will be different for another; and even within some organisations there are likely to be some benefits which are appreciated by staff more at one level than another. Happily, the world of employee benefits has evolved rapidly in recent times and there is now an unbelievable choice of benefits on offer, and a variety of ways to present those benefits to staff. They're easy to administer, too.

It all makes for a successful recipe:

- increased staff awareness of employee benefits;
- increased staff engagement with these benefits;
- the potential for employers to reward their staff, particularly in the not-for-profit sector;
- the ability to tailor benefits to a particular sector or workforce; and
- easy to manage and inexpensive benefits to choose from.

Most importantly, right now there is the time and opportunity to construct a proposition that is suitable for your workforce, without the pressures of onerous legislation.

PKF Francis Clark Financial Planning have a specialist Employee Benefits division and would be happy to provide further advice on this specialist area. Please call **01392 667000** or email **employeebenefits@pkf-francisclark.co.uk** for further information.

Have you heard of the PayPal Giving Fund?

Similar to the popular and widely used initiatives such as 'Just Giving' and 'Virgin Money Giving', the PayPal Giving Fund helps people support their favourite charities online and helps charities raise funds through PayPal, eBay and other technology platforms. Uniquely however, and unlike the other charity giving sites referred to above, the PayPal Giving Fund does not charge fees or commissions, as operating costs are covered by their partners (PayPal, eBay, GoFundMe and Humble Bundle). This means that a £10 sale on the site, for example, would translate to a £12.50 charity donation, if supporters choose to donate 100%.

Charities can enrol online through an easy set up process on the PayPal website and once this stage has been completed, the charity will appear in the directories of all partner websites. Supporters can then search and select charities, and donations can be made through the various online platforms (PayPal, eBay, GoFundMe, and Humble Bundle). Receipts are then provided to donors and donations are granted to the charities in monthly pay outs.

There are a handful of alternatives when it comes to registering your charity on fundraising sites, and on the surface, they do appear to offer an easy, low risk way of diversifying income streams and gaining wider exposure for charities. However, they all differ slightly and we therefore recommend that you research the sites and consider the pros and cons of each before deciding which funding site(s) is/are best and most suitable for your organisation.

Key tax considerations

for charities and not-for-profit organisations

Stamp Duty Land Tax (SDLT)

Relief from SDLT is available to charities that purchase an interest in land that they intend to hold for a 'qualifying charitable purpose'. That is:

- in the furtherance of the charitable purposes of the purchaser or another charity;
- as an investment, the profits of which are applied to the charitable purposes of the purchaser; and
- that the transaction must not have been entered into for the purposes of avoiding SDLT by either the purchaser or any other person.

Provision is made for relief previously granted on a transaction to be clawed back if, within three years of the transaction, the charity ceases to be a charity or uses the property for purposes other than charitable ones.

VAT

There are various reliefs from VAT that are available to charities, including:

- Advertising - the supply of advertising to a charity on a third party's medium, on any subject including staff recruitment, is zero-rated.
- Disability aids - the supply to charities of certain goods and services which are subsequently made available to disabled people for their personal or domestic use, is zero-rated.
- Construction - the construction of buildings intended to be used solely for non-business purpose can be zero rated. Charities may benefit from zero-rating other building work, for example, widening doorways or adapting a washroom.
- Fuel and power - charities can claim the reduced rate of VAT where fuel and power is supplied for and used for non-business activities.

The VAT rules can be complex, in particular the rules on 'non-business purpose'. Therefore, we recommend that you seek professional advice to ensure your organisation is correctly utilising available reliefs.

Becky Hayes, Senior Manager, Indirect Taxes
becky.hayes@pkf-francisclark.co.uk

Gift Aid - Donors

Charities can claim 25p back every time an individual donates £1 to their charity, providing certain criteria are met:

- The donor must have paid the same amount, or more, in income tax or capital gains tax in that tax year; and
- The donor must have made a gift aid declaration giving you permission to claim it.

There are additional rules that also allow charities to claim gift aid on membership fees, sponsored events, donated stock etc.

Charities can also claim gift aid under the small donations scheme. This allows them to claim 25% back on cash and contactless card donations under £20, without obtaining a gift aid declaration. A charity can claim up to £2,000 in a tax year under the scheme; however, they must also have claimed gift aid in the same tax year and have claimed gift aid without getting a penalty in the last two tax years.

Charitable rate relief

Charities and community amateur sports clubs can apply for charitable rate relief of up to 80% if a property is used for charitable purposes. This is claimed directly from your local council and they can top up the discount to 100% on a discretionary basis.

Laura Waycott, Manager
laura.waycott@pkf-francisclark.co.uk

Gift Aid - Trading Subsidiaries

It is common practice for charities to run trading operations through a 100% subsidiary. Whilst the trading subsidiary's profits are taxable, no tax charge will arise if the subsidiary 'gift aid's' its taxable profit to the charity. The trading subsidiary has nine months from the accounting year-end to make the gift aid payment. This gives the subsidiary sufficient time to draw up its financial statements and prepare the corporation tax computation in order to calculate the level of gift aid payment required to negate the tax charge.

The accounting profit may not be the same as the taxable profits. This could be due to: non allowable costs (legal expenses), deprecation in excess of capital allowances, etc.

A gift aid payment cannot be made in a sum that is greater than the distributable profit & loss reserves shown in the company accounts. Therefore, where taxable profits are higher than the accounting profits, a tax liability may arise.

Consideration therefore needs to be given to how a mismatch between accounting profits and tax profits can be avoided. This can potentially be managed by the charity holding capital assets (as opposed to the trading subsidiary) as this will avoid the issue of whether non allowable accounting depreciation exceeds tax allowable capital allowances.

Care is needed when structuring trading activities through a 100% trading subsidiary to ensure that the charity ultimately enjoys the maximum cash benefit possible.

Clive Townsend, Tax Director
clive.townsend@pkf-francisclark.co.uk

Investment *strategy*

Mike Bath, Director
mike.bath@pkf-francisclark.co.uk

With interest rates remaining at historically low levels, holding large cash balances can result in the erosion of a charity's capital in real terms over time. Between June 2008 and June 2018 cash deposits generated a return of just 5.91%, far less than the rate of inflation over this period, meaning that the real-terms value of cash deposits fell substantially. By comparison, Global Equities over the same period returned over 164%. Despite this, many charities continue to carry large cash holdings with trustee boards often shying away from non-cash investments due to the perception of risk.

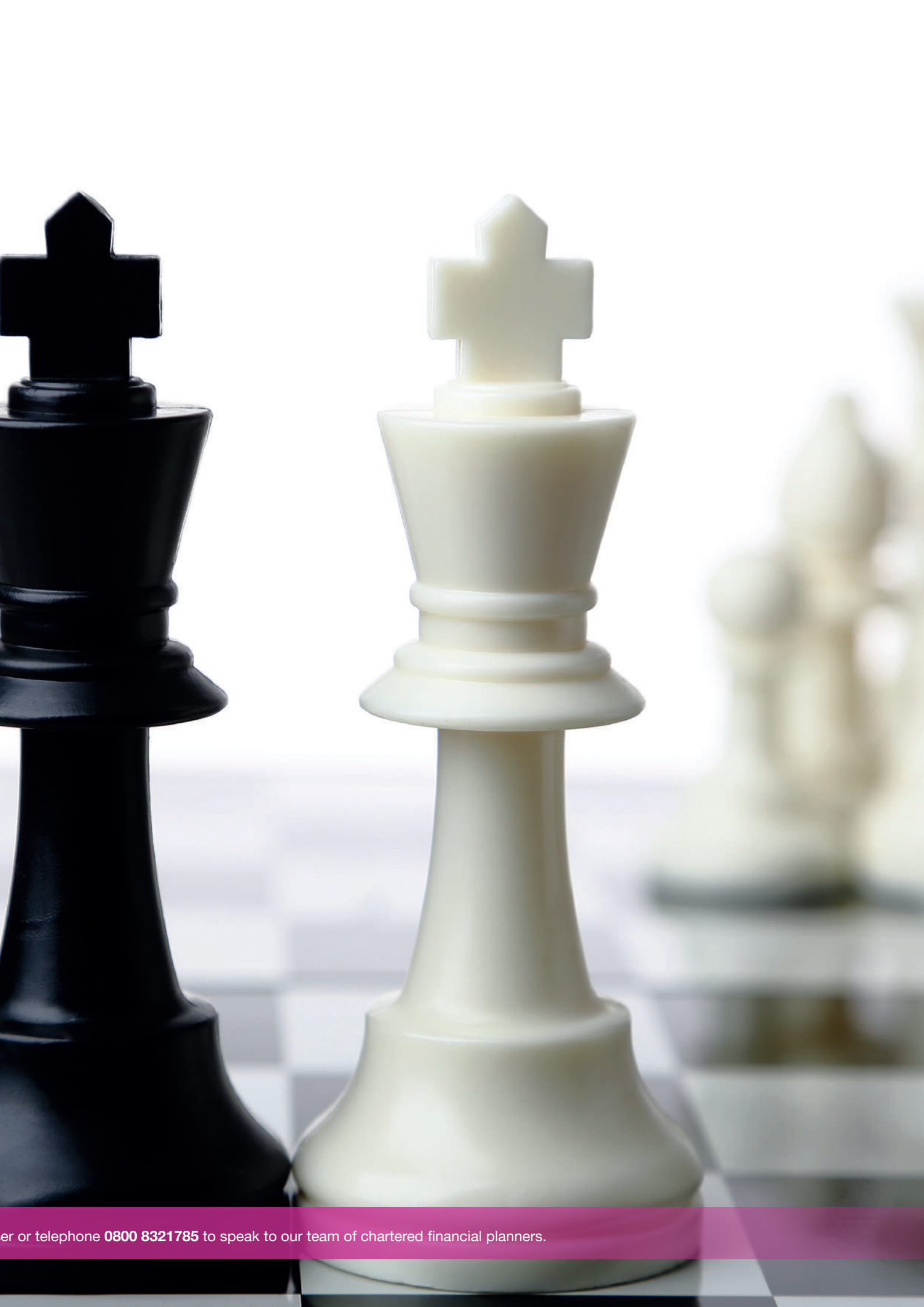
CC14 confirms that charities can invest to further their charitable aims, balancing the return earned against the charity's own risk appetite. It should be noted that cash deposits are not risk-free and are subject to both inflation risk and default risk.

The issues that a board should consider in formulating an investment policy may include:

- the level of capital available for longer term investment;
- the investment holding period (non-cash investments should typically have an investment time horizon of five years of more);
- the target level of return on the investment over a period and an applicable benchmark to test returns against;
- the trustees' risk appetite;
- diversification of risk; and
- ethical considerations, such as excluding certain sectors or entities.

Having defined an investment policy, the trustees should seek expert advice on how best to achieve their investment aims. Charities investing smaller amounts may find unitised funds such as unit trusts or OEICs the most suitable vehicles to meet their objectives. Charities with larger amounts to invest are able to access discretionary fund management with direct access to an investment manager who can build a bespoke portfolio across a wide range of asset classes based on the trustees' objectives. The investment strategy adopted should not be regarded as 'cast in stone' but should be regularly reviewed as the charity's activities and objectives change.

If you would like to discuss your charity's investment options further, please speak to your usual PKF Francis Clark advis



er or telephone **0800 8321785** to speak to our team of chartered financial planners.

Caring for *our* communities

Each year our offices nominate a Charity of the Year to support for the duration of the year ahead. We are proud to raise and thousands of pounds in support of these valued local causes each year.

In 2018/2019 we are supporting:

Woodside Animal Welfare Trust
Plymouth

Dorset Mind and The Chestnut Nursery
Poole

Oakhaven Hospice Trust
New Forest

Wiltshire Air Ambulance
Salisbury

Invictus
Truro

FORCE
Exeter

MDUK - I Fight for James
Torquay

ARC
Taunton

Supporting Elmer's Big Parade Plymouth

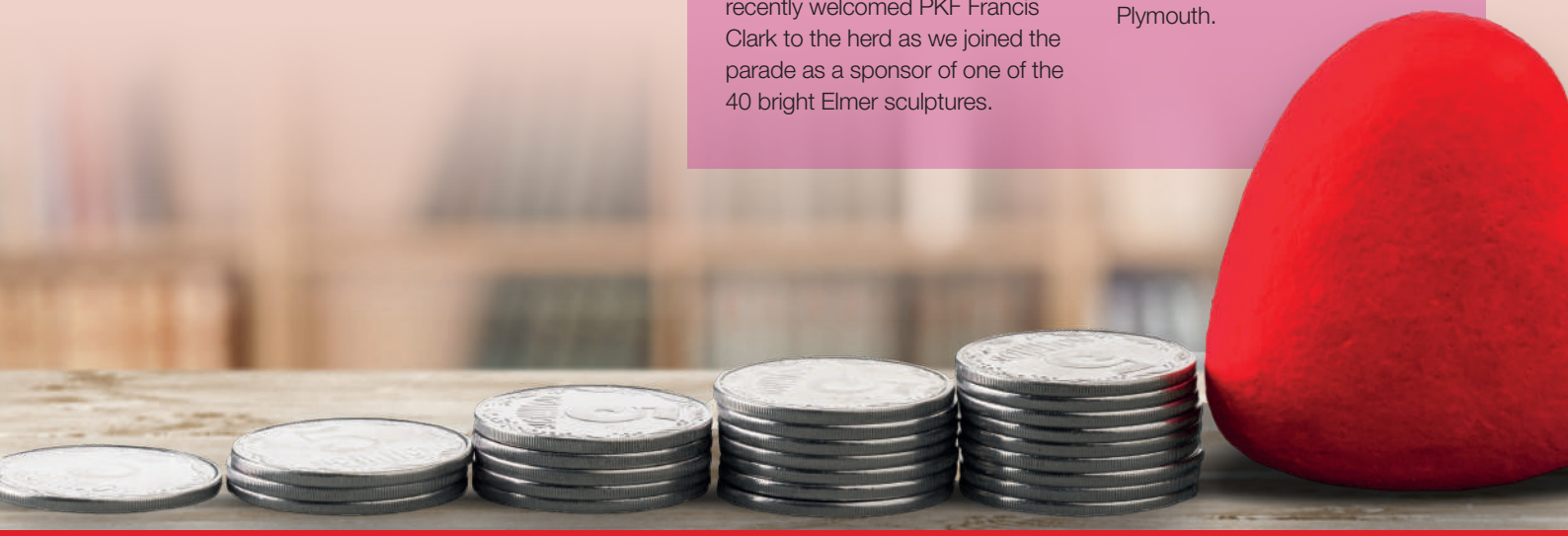
For ten weeks in the summer of 2019, a parade of 40 fabulously colourful and unique elephants will be taking visitors on a trail around the beautiful city of Plymouth and the surrounding areas.

As part of the national celebrations for the 30th birthday of the much beloved children's character 'Elmer', by Devon born artist and author David McKee, St Luke's Hospice Plymouth are bringing the mass participation, family friendly trail to Britain's Ocean City.

Elmer's Big Parade Plymouth recently welcomed PKF Francis Clark to the herd as we joined the parade as a sponsor of one of the 40 bright Elmer sculptures.

Duncan Leslie, Head of Not-for-Profit said: "We are delighted to support Elmer's Big Parade Plymouth in support of St Luke's Hospice who do such wonderful work caring for the families of the city affected by life-limiting illness. We look forward to tracking down our Elmer around the streets of Plymouth next summer!"

It is anticipated that Elmer will attract over 200,000 tourists to Plymouth and the auction of the sculptures at the end of the summer will raise funds directly for St Luke's Hospice Plymouth.



The charity and not-for-profit sector is important to us and we endeavour to give our support wherever we can, however, unfortunately it is not possible to support every request. We review our CSR arrangements regularly and our support of local charities takes many forms including non-financial support by our people for charitable events. Please get in touch if you have an innovative idea that you would like us to consider.

Charity Commission *updates*

Since our last newsletter the Charity Commission has released one new and two updated publications along with a report on public trust in charities and guidance on insider fraud in the sector. Other publications of interest can be found at:

https://www.gov.uk/government/organisations/charity-commission/about/publication-scheme

- **Finding new trustees (CC30)**
  (Updated May 2018)
- **The essential trustee: what you need to know (CC3)**
  (Updated May 2018)
- **Charity trustee welcome pack**
  (Published April 2018, updated May 2018)
- **Trust in charities 2018**
  This report presents the findings of independent research conducted by Populus into public trust and confidence in charities in 2018.
- **Focus on insider fraud: research report**
  This report outlines findings from a Charity Commission study into how insider fraud is affecting charities.

EXETER	PLYMOUTH	POOLE	SALISBURY	TAUNTON	TORQUAY	TRURO
01392 667000	01752 301010	01202 663600	01722 337661	01823 275925	01803 320100	01872 276477

Please visit our website for your local office expert **pkf-francisclark.co.uk**

If you would like to be added to, or deleted from our mailing list, please contact Peter Finnie, peter.finnie@pkf-francisclark.co.uk or sign up online at: **pkf-francisclark.co.uk**

PKF FRANCISCLARK
Chartered accountants & business advisers