

# charity workshop

Issue 2 – 2007

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## It is not a crime for Charities to borrow money

Many charities will have to revert to raising finance at some time whether to purchase a property, other assets, fund delayed income receipts or even to finance deficits.

The key to raising finance is having a well formed plan as to how you are going to pay the interest and repay the principal over time.

There are a number of providers who specialise in providing financial assistance to charities and voluntary organisations whether they are registered charities or not.

Many charities and voluntary organisations have chosen to purchase their properties over the past few years rather than paying the high levels of rent in the current market. By purchasing your own property you can insulate yourselves from rent increases, it will create a valuable reserve as the mortgage is repaid and could provide a useful asset against which you could borrow

in the future.

Funds are available from a number of sources which will assist you in purchasing your property. 100% funding for property purchase is available in the market as well as more conventional commercial mortgages (80% loan to value). Existing mortgages or loans can be refinanced at interest rates/loan periods to suit your needs.

It is often the case that the costs of servicing the mortgage, even up to 100%, are cheaper than current rental levels.

Some Commercial Property is subject to VAT on purchase and specialist tax advice should be sought, however VAT Bridging Finance is also available. Generally, most registered charities and voluntary organisations are exempt from payment of Stamp Duty Land Tax. Again advice should be sought.

## It is not a crime for Charities to borrow money (continued)

Most charities and voluntary organisations will qualify for rates relief from their local authority; generally up to 90% discount is applied.

Should you wish to build your own property, whether for your own occupation or for renting out to other organisations, there are lenders who will again fund up to 100% of the cost of your development. These loans are typically paid out at different stages of construction and the funding will include all allowances to cover grant claims and VAT rebates. Typically interest is rolled up during the construction phase so that no interest or capital payments are due until the building is complete.

To explore lending options, call Beverley Ham, Director of Property Finance, Blacktower Financial Advisers Limited, part of Kingston Smith, on 020 8336 6350.

### SORP 2005 and Parochial Church Councils

Church House Publishing has recently published guidance for Anglican churches on the application of the new Charities Statement of Recommended Practice. Kingston Smith LLP was asked by the Church Commissioners to help revise the previous guide to ensure that PCCs met the new requirements of SORP 2005, particularly in respect of the Annual Report and the format of the Statement of Financial Activities in the context of church accounts. Copies of the guide can be obtained from Church House Publishing ([www.chpublishing.co.uk](http://www.chpublishing.co.uk)). If you have any queries in connection with the interpretation of the recommendations, please contact James Cross on [jcross@kingstonsmith.co.uk](mailto:jcross@kingstonsmith.co.uk).

## Attracting and recruiting a more diverse group of Trustees

Recruiting and retaining the right employees is vital to the success of every organisation. With historically low levels of unemployment in the UK and increases in pay and conditions for workers in both the public and private sectors, many charities and not for profit organisations are finding that they have to work harder to compete for the best staff. And that's before you even get around to thinking about how to attract trustees that have both the skills and commitment so necessary for the role, whilst ensuring that they more accurately reflect the diversity of the environment in which the charity operates.

This issue has been brought into sharper focus recently by the controversy over the government's proposals to bring regulations into force that will ensure that any organisation providing service to the public (or a sector of the public) does not discriminate on the grounds of sexual orientation. This comes on the back of regulations seeking to prevent discrimination on the grounds of race or sex, religion or philosophical belief, disability and age. And for the increasing number of charities and other not for profit organisations that need to tender to government or quasi government bodies for funds, demonstrating a proactive approach to equal opportunity and diversity has become a must rather than a "nice to have". It is easy to understand why some organisations feel that the very ethos of their charity may be undermined if they fail to get the balance right.

We encourage clients to start by reviewing the 'look' of their organisation as well as their current recruitment practices and looking at practical ways to attract and retain a more diverse group of trustees.

Charities are looking for sophisticated ways to enhance their recruitment processes but just reaching for competency structures and psychometric tests may not be the most effective way of improving the recruitment of trustees.

Here's our simple five-step plan to help you recruit and retain the Trustees you need:

### Step 1

Regularly review the 'look' of your organisation. Do your marketing materials, website and other documentation reflect the kind of organisation that you aspire to be? Do you reach out to other local groups that might be a source of new talent for the governance of your organisation as well as being reflective of groups that are under represented amongst your Trustees?

### Step 2

Take time out to look at the content of your recruitment advertising, application forms and other recruitment documents. Check whether you are applying unnecessary criteria that might be discriminatory or asking for information that has no relevance to the job. Where are you advertising? Could you expand where and how you advertise to attract a broader range of potential candidates for the Trustee role. Finally, watch out for the Age Discrimination legislation that came into force last year. Whilst you will want people to have relevant experience that they can contribute to the governance of your organisation, age alone should be no bar to being appointed. Change your recruitment criteria now to ensure that you comply.

### Step 3

Make sure you know your legal responsibilities when recruiting and, if necessary, get some training in effective interview techniques that will boost the effectiveness of your interviews and help you make the right choice for the organisation. This is particularly important if you use panel interviews to select new Trustees. Panel interviews should force you to adopt a proper structure so that all the critical areas are covered and you discover whether they have the relevant skills, knowledge and experience for the role. Unplanned, however, they tend to be unfocussed and confusing for candidates and interviewers alike.

### Step 4

Whatever you do, know what you really want from a trustee before you seek them out. Write a simple but specific person specification setting out the essential and desirable attributes that the ideal candidate should have. Be objective and realistic when deciding which attributes are 'essential' and which are 'desirable'. This needn't be more than one side of A4 paper but it will provide a sound basis for drafting

your advertisement, talking to potential trustees about what the role really entails, conducting your interviews and informing your appointment decisions.

### Step 5

Have a clear plan to improve your chances of retaining good trustees. Be flexible, if you can, about when and where you meet and make sure that Trustees get the relevant papers well in advance so that they can prepare well for meetings. And when Trustees start, have an induction programme in place that covers all the key things that they need to know about your organisation, your employees and your volunteers. Lastly, try and provide opportunities for learning and development for Trustees, both for their personal benefit and so that they really understand the key governance issues, particularly how to manage the relationship between Trustees and management.

Once charities and not for profit organisations have these five key processes in place they will be in a position to attract and appoint high quality Trustees, who are truly committed to the goals of the organisation and reflect the wide diversity of the communities in which they operate and/or the communities to whom they provide services.

For more information, contact Mark Slattery, HR Insight, Kingston Smith's HR Consultancy on 01245 324824, or email [mark@hrinsight.co.uk](mailto:mark@hrinsight.co.uk)

## The budget and gift aid

The Chancellor gives with one hand and takes away with the other.

To help charities build donor relations there is a small relaxation in the amount of benefits a gift aid donor of more than £1,000 can receive, doubling the limit to 5% of the gift subject to a maximum of £500. The change in basic income tax rate, however, will reduce the amount that charities can recover under gift aid by £3.20 for every £100 received. Charities for whom, this recovery is an essential source of income may wish to start taking action now.

# Charities Act 2006

After a gestation period of over four years, the Charities Act finally received Royal Assent on 8 November 2006. None of the Act's provisions took immediate effect and a further wait ensued until the Implementation Plan was issued. Some measures have now been introduced with effect from 27 February 2007 while the remainder will be rolled out over the next two to three years.

The principle changes now in place are as follows:

## Audit threshold

The income and assets thresholds above which charities must have their accounts audited have doubled to £500,000 and £2.8m respectively with effect from accounting periods beginning on or after 27 February 2007. Only one of these limits needs to be exceeded for an audit to be required.

The accounts of incorporated charities with income between £90,000 and £500,000 must contain an accountant's report while those of unincorporated charities with income between £10,000 and £500,000 must be subject to an independent examination. This examination must be carried out by an eligible professional if income is above £250,000.

## Trustee indemnity insurance

Charities can now purchase trustee indemnity insurance where it is in the charity's best interests to do so without obtaining permission from the Charity Commission.

## Trustee liability

The Charity Commission can now relieve trustees of personal liability where they have acted honestly and reasonably. Previously, only the Courts had this power. However, the Commission will continue to treat breaches of trust by trustees very seriously.

## Reducing charities' administrative burden

Unincorporated charities can change their administrative arrangements, e.g. powers and procedures, without reference to the Commission, although there are safeguards for membership charities

to protect members' interests.

Charities can now "self-certify" the use of charity property as security for grants and other transactions in the same way that was previously allowed for loans. The process requires trustees receiving and considering advice from solicitors and auditors.

Where the Commission makes a scheme for a charity, the rules regarding public notification are relaxed, which should lead to a reduction in costs for the charities concerned.

## Small charities

From April 2007, the registration limit above which charities must register with the Charity Commission is to be increased from £1,000 to £5,000 and it will no longer be necessary for charities holding land or with a permanent endowment but with income below the threshold to register.

## The Charity Commission

There are a number of changes to the Commission itself and its powers, many of which will arise in connection with an inquiry into a charity's affairs. Its constitution has been modernised giving it new statutory objectives, functions and duties and its independence from government has been confirmed. One of these objectives is to promote awareness and understanding of the public benefit requirement. A public consultation regarding public benefit started on 7 March 2007 about which much has been written in the press.

The public benefit issue is one that will not lie down quietly and further coverage on this and the next batch of the Act's measures to be implemented will appear in later issues of Charity Workshop.

## Seminar

### Charity Update – Charities Act 2006

In this seminar, we will review the main provisions of the Act.

**Date:** Tuesday 15 May 2007

**Time:** 4.30pm for 5.00 - 6.15pm, followed by drinks

**Venue:** Denbies Wine Estate, London Road, Horsham, West Sussex

**Cost:** £25 (free to Kingston Smith clients)

To reserve a place, email **Dawn Mann** at [ev](mailto:dmann@ksm.com)

# Companies Act 2006

Like the Charities Act, the Companies Act 2006 received Royal Assent on 8 November 2006. It is a massive piece of legislation and was the longest Bill ever considered by Parliament. It runs to 1300 clauses and 16 schedules and takes up 701 pages if you ever decide to read it from cover to cover!

A lot of the Act consolidates earlier legislation and should make understanding company law easier as the Act will become the main source of law. Again, like the Charities Act, the Act's provisions will be introduced in stages with all of it in effect by October 2008. In this article, we try and highlight the main changes that might affect charitable companies and charities' trading subsidiaries and the date of their introduction. It must always be remembered that charitable companies will also have to comply with the provisions of the Charities Act and the charity's constitution.

## January 2007

### Directors' duties

The general duties of directors have developed within case law. The Act confirms case law by setting out seven directors' duties. It is hoped that this will make the duties more accessible and easier to understand.

### Communication

Electronic communications must include the company's name, number, registered office, etc, as business letters are already required to do.

## October 2007

### Meetings and decision making

The requirement for private companies to hold AGMs is abolished and there are new rules relaxing the provisions for the use of written resolutions in place of members' meetings.

## April 2008

Private companies can dispense with appointing a company secretary if they wish.

Accounts must be filed at Companies House one month earlier. The filing dates are nine months after the year end for private companies and six months for public companies.

## October 2008

### Matters concerning directors

Directors will be required to file a service address at Companies House which need not be their private home address, although a private address will still be held as protected information.

While directors have always had a duty to avoid conflicts of interest, where such matters do arise, only the members have been able to authorise the matter in question. It will now be possible for the remaining directors to authorise such matters if the Articles permit. At least one director must be a natural person – previously all directors could be companies.

A minimum age of 16 has been set for directors.

### Governing documents – simplification

The Articles will become the sole constitution document for new companies and will set out the principles governing the way the business is conducted.

The Memorandum of Association will become a form to be filed at Companies House stating that the subscribers wish to form a company and to be the first members.

New model Articles will be available written in clearer English for both new and old companies to adopt.

There will be no need for companies to state their objects giving more flexibility over what they can do.

## Charities Act 2006 and Companies Act 2006

provisions of the Charities Act 2006 and Companies Act 2006.

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For more information, contact [events@kingstonsmith.co.uk](mailto:events@kingstonsmith.co.uk) or phone **020 7566 3850**

# New substantial donor regulations

Are you prepared for the substantial donor regulations introduced by the Finance Act 2006? These regulations were introduced to prevent individuals obtaining unfair tax advantages but could catch out unsuspecting charities resulting in a loss or reduction of tax relief.

Where a charity has entered into a relevant transaction with a substantial donor, or person connected with a substantial donor, that transaction will be treated as non qualifying expenditure (to the extent that it is not covered by one of the permitted exceptions) and the charity will lose tax relief on this amount.

## What makes a donor substantial?

Broadly a substantial donor is an individual or company who has made gifts, on which they have received tax relief, to the charity of more than £25,000 in any year or more than £100,000 over the last six years. But once someone becomes a substantial donor for a period they are considered to remain a substantial donor for the next five years. Overseas donors who do not receive UK tax relief are excluded.

## Who is considered to be a connected person for a substantial donor?

Connected persons include a relative (sibling, lineal ancestor or lineal descendant) and a spouse and the spouse's relatives. They also include the settler of a trust of which a person is a trustee and a business partner or spouse or relative of a business partner. A company is connected with another company if controlled by the same person or by persons connected with him. As you can see this can create quite a wide net of potential individuals and companies with whom relevant transactions may cause problems.

## What are the relevant transactions?

In each of the following cases reference to a substantial donor includes reference to a person connected with that donor:

- the sale or letting of a property by a charity to the substantial donor.
- the sale or letting of a property to a charity by the substantial

donor unless this takes place in the course of business carried on by the donor and is on arm's length terms.

- the provision of services by a charity to a substantial donor unless the transaction has taken place as part of the primary purpose of the charity and is on arm's length terms.
- the provision of services to a charity by a substantial donor unless this takes place in the course of business carried on by the donor and is on arm's length terms.
- the exchange of property between a charity and a substantial donor.
- the provision of financial assistance by a charity to a substantial donor.
- the provision of financial assistance to a charity by a substantial donor unless the assistance is on terms which are no less beneficial to the charity than those which might be expected in an arm's length transaction.
- investment by a charity in the business of a substantial donor unless the investment is in shares or securities listed on a stock exchange.

Each of the exceptions only applies if HM Revenue and Customs are satisfied that it is not part of an arrangement for the avoidance of tax.

## An example

In August 2006 the Grimsdyke Art Gallery, a registered charity, received a donation of £30,000 under gift aid from Brian Smith, a local millionaire philanthropist. It claimed gift aid tax relief of £8,461. In March 2007 the Gallery bought, at market value of £25,000 a small print from Julia Brown, Brian Smith's sister-in-law. Julia Brown is a connected person of Brian Smith and the transaction falls under heading 5 which has no exceptions – it is therefore caught by the regulations. Tax relief on £25,000 of the £30,000 gift will be lost and the Gallery will be required to repay £7,051 of the gift aid tax previously claimed.

### **What should charities be doing to avoid being caught by these provisions?**

The fundamental step charities need to take is to ensure that their donor records are capable of flagging up all substantial donors and that the records go back at least 11 years.

The next step will be to identify the connected persons of those substantial donors. This of course relies on full disclosure from the donor. Fortunately the Revenue have indicated that they will not seek to penalise charities where there have been inadvertent transactions but each charity will need to demonstrate that it has taken reasonable steps to identify connected persons.

Finally where a transaction with a substantial donor is identified, but is considered to be exempt, the charity should ensure that it has sufficient information to demonstrate that the transaction was undertaken on an arm's length basis as part of primary purpose trading if by the charity or the donor's business if to the charity.

### **Conclusion**

The range of relevant transactions, the connected persons and the period covered increase the chance of a legitimate transaction being caught out and relief lost. Charities need to be aware of the existence of these regulations and ensure that they have taken reasonable steps to demonstrate that any relevant transactions are covered by exemption.





Chartered Accountants

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**Voted best all-round charity auditor for four consecutive years by readers of Charity Finance**

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**Kingston Smith LLP**

Devonshire House  
60 Goswell Road  
London EC1M 7AD

**Contact** Nicholas Brooks, Neil Finlayson or Sandra De Lord

**Tel** 020 7566 4000

**Email** [nfp@kingstonsmith.co.uk](mailto:nfp@kingstonsmith.co.uk)

**Web** [www.kingstonsmith.co.uk](http://www.kingstonsmith.co.uk)