

Charities

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81.2 Tax Treatment of Gifts to Charity

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Charities receive generous treatment under many tax codes;¹⁰⁵ such treatments therefore qualify as tax expenditures.¹⁰⁶ The HMRC figures for 2019–20 show the total cost of tax relief for charities was £5.7 billion, and total relief for individual giving including IHT and higher rate relief on gift aid was £1.7 billion.¹⁰⁷ Tax relief for charities on national non-domestic rates was £2.3 billion, IHT was £1.0 billion and SDLT was £280 million. A reason behind the major changes made to the Charities Act 1993 by the Charities Act 2006 was the need to see whether these benefits were justified.

The income tax provisions were rewritten by ITA 2007, and the TA 1988 rules, much amended and rephrased in 2006, were rewritten by CTA 2010 for companies. The 2006 changes were heavily criticised as giving a general impression of attempts to stifle charitable giving and limiting charitable tax relief.¹⁰⁸ The rules on transactions between charities and tainted donations have, it is said, enormous potential for damaging relations between charities and donors, and for increasing administration costs. So much will depend on how the sometimes vague rules are applied by HMRC.

¹⁰⁵ Among many background tax policy sources, see Inland Revenue, *Discussion Document* (1999); Banks and Tanner, *Taxing Charitable Giving*, IFS Commentary 75 (Institute for Fiscal Studies, 1999); Chesterman (1999) 62 *MLR* 333; Chesterman, *Charities Trusts and Social Welfare* (Weidenfeld & Nicolson, 1979), esp ch 10; Krever and Kewley (eds), *Charities and Philanthropic Organisations: Reforming the Tax Subsidy and Regulatory Regimes* (Australian Tax Research Foundation, 1991); Scharf, Cherniavsky and Hogg, *Canadian Policy Research Network Working Paper* (1996); Surrey (1976) 84 *HLR* 352; Surrey, *Pathways to Tax Reform* (Harvard University Press, 1973); Andrews (1972) 86 *HLR* 309, esp 344–75; Bittker (1969) 78 *Yale LJ* 1285; Bittker (1972) *Tax Law Review* 37; McDaniel (1972) 27 *Tax Law Review* 377; and McNulty (1984) 3 *Virginia Tax Review* 229.

¹⁰⁶ See Surrey, *Pathways to Tax Reform*, esp 20, 223–32; and Feldstein, in Aaron and Boskin (eds), *The Economics of Taxation* (Brookings Institute, 1980). For vigorous criticism of one application of this approach, see Bittker (1969) 78 *Yale LJ* 1285. On US rules for deduction, see Bittker and Lokken, *Federal Taxation of Income, Estates and Gifts* (Warren, Gorman & Lamont, 1989), ch 35; see also Griffith (1989) *Hastings LJ* 343.

¹⁰⁷ HMRC Statistics, Cost of Reliefs.

¹⁰⁸ Evans [2006] *BTR* 531; see also Parry-Wingfield, *The Tax Journal* (14 August 2006) 9, and (21 August 2006) 5.

81.1.1 Tax Policy Considerations

Turning briefly to the general tax policy considerations, it is noteworthy that Simon says nothing about the charitable deduction in his *Personal Income Taxation*. The Canadian Royal Commission recommended the continuation of the deduction for charitable contributions and the exemption of the income of charities, but also recommended that the beneficiary should be taxed on any benefits received.¹⁰⁹ The 1955 Report of the UK Royal Commission made some suggestions, but its most telling point was that a more restrictive definition of ‘charity’ was needed.¹¹⁰ The Meade Committee Report and the Mirrlees Review say virtually nothing about charities.

81.1.2 Definition of Charity

FA 2010, Schedule 6, paragraph 1 defines a ‘charity’ for tax purposes as a body of persons or trust that—

- (1) is established for charitable purposes only,
- (2) meets the jurisdiction condition,
- (3) meets the registration condition, and
- (4) meets the management condition.

Two other definitions are also set out in paragraph 1: a ‘charitable company’ means a charity that is a body of persons and ‘charitable trust’ means a charity that is a trust. ‘Charitable purposes’ are defined by reference to the Charities Act 2011, section 2, as purposes that fall within section 3(1) of that Act and are for the public benefit (as defined in section 4). The list of charitable purposes in section 3 includes the prevention or relief of poverty and the advancement of such matters as education, religion, health, human rights or animal welfare plus a general ‘sweeper up’ head for purposes analogous to or within the spirit of the listed purposes. In *The Independent Schools Council v The Charity Commission for England and Wales (and others)*,¹¹¹ the Upper Tribunal shed some light on the meaning of the ‘public benefits’ requirement in the Charities Act 2006—which is substantially the same as that now in the 2011 Act—as it related to fee-charging schools. The decision is also relevant to other charities that charge for services. According to the Tribunal, the provision of education by independent schools is not in itself a public benefit, and charitable schools must ensure that children of families who cannot afford the fees are able to benefit from what the schools do in a way that is neither minimal nor token. The Tribunal also decided that it was for the charitable trustees to decide how best to do this in each charity’s particular circumstances. Following the decision the Charity Commission issued revised guidance on the public benefit requirement.¹¹²

¹⁰⁹ Carter (chair), Canada Royal Commission on Taxation, *Report*, vol 3 (Ottawa, 1966) 222–27 and *ibid*, vol 4, 131–36.

¹¹⁰ Royal Commission on the Taxation of Profits and Income, *Final Report*, Cmnd 9474 (1955) para 175.

¹¹¹ [2011] UKUT 421 (TCC). For a case in which the taxpayer company failed to show that it was established for charitable purposes only, see *Helena Housing Ltd v Revenue & Customs Commissioners* [2011] STC 1307 (UT).

¹¹² See <https://www.gov.uk/government/collections/charitable-purposes-and-public-benefit>.

Leaving aside the possibility of registration elsewhere, in the UK a charity must be registered with the Charity Commission unless it is an exempt charity. Registration with the Charity Commission is conclusive evidence that the body is a charity. For this reason HMRC may object to a registration, as in *IRC v McMullen*,¹¹³ or may ask the Charity Commission to take steps to deregister a charity; they may also refuse relief on the ground that income is not applied for charitable purposes. In addition, charities must be ‘recognised’ by HMRC in order to qualify for tax relief. Recognition is an administrative process, which involves providing HMRC with the charity’s details including bank account information and registration number along with the creation of a digital account with HMRC.

Political parties are not charities, and while there are specific reliefs from CGT and IHT for gifts to them, there is no specific income tax relief. Special but restricted reliefs have been made available to those community amateur sports clubs which do not qualify as charities.¹¹⁴

81.1.3 Tax Relief for Charities

In general, the most important tax reliefs available to a recognised charity are:

- (1) charities do not pay tax on most income and gains used for charitable purpose (‘charitable expenditure’). This includes donations received, profits from trading and fund-raising events, bank interest and other investment income, rental income, and gains from the disposition of capital property;
- (2) charities are eligible for an 80% discount on business rates on non-domestic buildings;
- (3) charities can reclaim tax that has been deducted on donations (ie gift aid);
- (4) charities are exempt from stamp duty land tax on property not purchased for re-sale;
- (5) charities are entitled to pay a reduced rate of 5% VAT on fuel and power and a zero rate on some goods and services, including advertising and items for collecting donations as well as medicine and medical equipment.

Charities are required to pay tax on other forms of income, including profits from developing land and money not used for charitable purposes (‘non-charitable expenditure’).

81.2 Tax Treatment of Gifts to Charity

In UK tax law, gifts to charity have been deductible for income tax purposes if they were made in the form of (a) charitable covenants, (b) gift aid, (c) payments under

¹¹³ [1981] AC 1, (1981) 54 TC 413.

¹¹⁴ CTA 2010, ss 658–671, ex FA 2002, s 58 and Sch 18, as amended, eg by FA 2004, s 56. Such clubs that register with HMRC are allowed gift aid repayments, with retroactive effect from 1 April 2010 in relation to gift aid and 6 April 2010 in relation to gift aid claims.

a payroll deduction scheme ((a) is now merged into (b)). Today the starting point for gifts of money is ITA 2007, sections 520–523 (charitable trusts) and CTA 2010, sections 475–477A (charitable companies). If the gift qualifies for gift aid, it is grossed up at the basic rate and treated as the charity's income of the grossed up amount.¹¹⁵ If the charity becomes liable to income tax later on, the charge is made under section 521, as envisaged by ITA 2007, section 3(2). Payment by HMRC to the charity is authorised as from the passing of FA 2008; it is not technically a repayment of tax but an authorised payment from public funds. Since 2013 there is a small donations scheme which provides a top-up payment of 25p for every £1 of eligible donations of £30 or less up to an annual maximum payment of £1,250, without the paperwork normally required for gift aid.¹¹⁶

There are deductions in computing trading income of costs incurred in sending employees to work for charities.¹¹⁷ For gifts of trading stock to charities, special rules override the usual deemed market value receipt for disposals other than in the course of the trade.¹¹⁸ Other rules have removed the application of the non-deduction rule for business gifts, etc¹¹⁹ from gifts to charities.¹²⁰ For CGT purposes, a taxpayer who makes a gift of an asset to a charity is treated as if the asset were sold for a sum such that no gain, no loss arises on the disposal.¹²¹ The relief exempts a donor from liability to CGT on the gain. It is far less generous than the US rules, which not only exempt the donor from any liability on the gain but also permit the donor to treat the full market value as a contribution to charity for income tax purposes and so as available for deduction against other income.¹²² These US rules were wide open to abuse: for example, T would give a car to his church and claim—and get a deduction of—the value of the car (\$10,000) even if the church eventually sold it for only \$3,000. Restrictions eventually followed.

Gift rules introduced by FA 2000 were at first confined to shares and other securities; they gave rise to abuse which was countered by legislation in 2004.¹²³ Relief for gifts of land was introduced by FA 2002.¹²⁴ Gifts of other assets, eg pictures or books, do not yet qualify.

The favourable CGT treatment extends also to settled property. Thus, where property has been held in a non-charitable trust and then, under the terms of the trust, a charity

¹¹⁵ ITA 2007, s 520 and CTA 2010, s 475, ex FA 1990, s 25(10) and (12).

¹¹⁶ Small Charitable Donations Act 2012. The small donations limit was raised from £20 to £30, with effect from 6 April 2019: see Small Charitable Donations Act (Amendment) Order, SI 2019/337.

¹¹⁷ ITTOIA 2005, ss 70–71 and CTA 2009, ss 70–71, ex TA 1988, s 86.

¹¹⁸ ITTOIA 2005, s 108–110 and CTA 2009, 105–108, ex TA 1988, s 83A (gift in kinds to charity) and 84 (gifts to educational establishments).

¹¹⁹ Ie ITTOIA 2005, s 45, ITEPA 2003, ss 356–358, CTA 2009, ss 1298–1300, ex TA 1988, s 577 (but not other rules such as ITTOIA 2005, s 34, CTA 2009, s 54, ex TA 1988, s 74(1)(a)).

¹²⁰ ITTOIA 2005, s 47(5) and CTA 2009, s 1300(1),(5), ex TA 1988, s 577(9).

¹²¹ TCGA 1992, s 257.

¹²² See eg Speiller (1980) 80 *Columbia L Rev* 214.

¹²³ TA 1988, s 587B, added by FA 2000, s 43 and amended by FA 2004, s 139. These rules are now in ITA 2007, ss 431–440 and CTA 2010, ss 206–212. The schemes attracting the Revenue's attention are described in Press Release 2 July 2004, [2004] *Simon's Tax Intelligence* 1573.

¹²⁴ ITA 2007, ss 441–442 and CTA 2010, ss 213 and 216, ex TA 1988, s 587C, added by FA 2002, s 97.

becomes absolutely entitled to that property, there is no charge to CGT. This is achieved by the charge on the deemed disposal specified by TCGA 1992, section 71 being treated as if it were a no gain, no loss disposal.¹²⁵ Under the IHT rules, a transfer of value to charity may be an exempt transfer (see above §53.2).¹²⁶ Also, an estate can pay IHT at a reduced rate of 36% if 10% or more of the net value of the estate is left to charity.¹²⁷

¹²⁵ TCGA 1992, s 257(3).

¹²⁶ IHTA 1984, ss 23–25.

¹²⁷ IHTA 1984, Sch 1A. See also <https://www.gov.uk/inheritance-tax/giving-to-charity-to-reduce-an-inheritance-tax-bill>.