

Charities Taxation

This factsheet considers various taxation matters that Charities need to be aware of.

A separate factsheet covers the principles of Gift Aid.

What is a Charity?

For tax purposes, a charity must satisfy all of the following conditions:

- be established for charitable purposes;
- be within the court jurisdiction of the EU, Norway or Iceland;
- meet the registration requirements;
- be under general control and management by fit and proper persons.

Registering with H M Revenue and Customs (HMRC)

To claim tax reliefs, a charity must register with HMRC. This is in addition to registering with The Charities Commission.

Is all income and gains eligible for tax relief?

Provided the income or gain is applied only to charitable purposes, it will be exempt from tax.

This exemption can apply to the following income:

- property income;
- dividends;
- interest;
- Lottery income;
- certain trading income (see below);
- donations under Gift Aid; and
- monetary donations from companies.



Non-charitable expenditure

Such expenditure is that which is not used for charitable purposes i.e. not permitted under the charity's articles or other governing document. It can include:

- non-qualifying investments i.e. not common investment funds, land or quoted securities;
- non-qualifying loans i.e. loans not carrying a commercial rate of interest or repayment terms;
- payments to foreign bodies (unless proper steps are taken to ensure that the payment is used for charitable purposes).

If a charity incurs non-qualifying expenditure, for every £1 spent, there is a £1 reduction in the exemption of income in the year (or in the last previous 6 years if insufficient income in the year).

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Can a charity trade?

Ancillary activities

Activities which are ancillary to the primary purpose of the charity will also be tax exempt e.g.

- sale of food and drink to museum visitors;
- sale of confectionary, toiletries, flowers to patients and visitors by a hospital;

Mixed trading

If mixed trading activities e.g. sale of food and drink at a museum to both visitors and non-visitors, the profits will need to be split. The ancillary activities will be exempt and the other activities taxable.

Small trades

An exemption applies to profits if aggregate turnover does not exceed the following annual limits:

- £5,000; or
- if in excess of £5,000, 25% of the charity's total receipts for the year from all courses (subject to an overall limit of £50,000).

Using a trading subsidiary

A charity may wish to engage in trading activities which extend beyond the charity's primary purpose and therefore such activities would not qualify for the tax exemption. A trading subsidiary could therefore be used to undertake such activities.

A trading subsidiary can make a donation to the charity and claim a deduction from its taxable profits. Such a payment is to be made gross and can be made at any time up to nine months after the end of accounting period.

This, therefore, enables the trading subsidiary to calculate its taxable profits prior to having to make the donation. The effect of this is that the trading subsidiary should not have any resulting taxable profits and consequently no corporation tax liability.

It may be beneficial not to make a profit-shedding payment of the whole of the taxable profits, otherwise the subsidiary may not be able to build up reserves and could potentially become insolvent. A corporation tax liability would therefore arise.

Another option is for the charity to provide a loan to the trading subsidiary. However, any such loan must be made on a commercial basis i.e. interest charged, otherwise it will be a non-qualifying investment by the charity.

Filing of corporation tax returns

HMRC may require a charity to complete a corporation tax return. Generally, such a return will be required every five years. A trading subsidiary company of a charity will be subject to the normal corporation tax requirements for a company, although as already mentioned, depending on the amount of the donation made to the charity, it may not incur a corporation tax liability.

This release has been prepared as a guide to topics of current financial business interests. We strongly recommend you take professional advice before making decisions on matters discussed here. No responsibility for any loss to any person acting as a result of the material can be accepted by us.

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