

# Questions to ask...

## ...ABOUT CHARITIES AND CORPORATION TAX

Most of the income and gains received by charities are exempt from Corporation Tax, provided that the money is used for charitable purposes. However, there has been a recent trend in charities seeking to diversify their income streams by providing their services for a fee or trading outside of their original objects. If charities undertake trading activities, they need to ensure they stay within the tax exemptions or otherwise Corporation Tax may arise. Below are ten questions charities should consider.

### 1. Does your trading income fall within the charitable trade exemption?

Charitable trading is defined as trading exercised in the course of carrying out a primary purpose of the charity, such as:

- A religious charity selling bibles
- A charitable school charging pupils
- A charitable clinic charging patients or selling medicines

A charitable trade can also be one that is carried out by the charity's own beneficiaries.

A charity's purposes are stated in its governing document.

### 2. Is your trading income seen as 'ancillary' trading?

Ancillary trading includes activities that are closely linked to the charity's main purpose and are also deemed to be exempt from tax under the charitable trading exemption.

Examples as suggested by HMRC include:

- The sale of textbooks in a school
- Sale of food and drink in a cafeteria to visitors to exhibits by an art gallery or museum
- Sale of food and drink in a restaurant or bar to members of the audience by a theatre

### 3. Do you fall under the exemption for small scale non-charitable trading?

Charities are also exempt from Corporation Tax on **non-charitable trading** where the income is less than £80,000 per annum. This exemption extends to all other income not covered by a specific exemption. All income not covered by these exemptions must be added together to establish whether the limit has been breached.

If your charity has income of over £80,000 arising from non-charitable trading, then the **entire profit** on these activities will be subject to Corporation Tax.

### 4. Should you consider your current structure?

If a trade is not a charitable trade and therefore does not qualify for a Corporation Tax exemption, a trading subsidiary can be used to carry out the trade. It is important to note that the subsidiary company will not itself be a charity and its profits will be chargeable to Corporation Tax. However, profits can be donated under corporate Gift Aid to the charity, thus reducing or eliminating the company's taxable profits and, because the donation is exempt in the charity's hands, Corporation Tax exposure can be reduced.

### 5. Are you aware of the accounting rules for donations made by subsidiary companies to their parent charities?

FRS 102 and the second edition of the Charities Statement of Recommended Practice (SORP) requires donations from subsidiaries to parent charities to be accounted for consistently with the accounting treatment for dividends – ie the payments are not a donation expense but **a distribution of profits from reserves**. The income is accrued by the parent and as an expense in the trading subsidiary when there is a legal obligation at the reporting date for the payment to be made.

### 6. Do you have a licence agreement between the charity and trading subsidiary?

Any use of the parent charity's land and buildings by a trading subsidiary should be covered by a formal license of the property concerned from the charity to the subsidiary, with an appropriate charge made.

## 7. What if your trading subsidiary is loss making?

Care should be taken where a charity is financially supporting a trading subsidiary that is loss making. This is because a charity is subject to rules on how it uses its funds and any amounts loaned or invested should provide a benefit to the charity.

## 8. Do you sell donated goods?

Many charities raise funds through the sale of donated goods, which may be a regular activity at a charity shop, or an ad hoc activity, such as an auction.

The sale of donated goods, usually in the form of items sold from charity shops, is generally not regarded as a trade for Corporation Tax purposes. However, when the goods are subject to significant restoration or upcycling resulting in a material change to the nature of the original donated goods, this may be regarded as a trading activity and be subject to Corporation Tax.

## 9. Do you generate rental income?

Generally, rental income received by a charity from land or buildings is exempt from Corporation Tax, provided the profits arising are applied for charitable purposes. Where services or assets over and above those that are usually supplied by a landlord are provided by the charity, these activities may instead constitute (taxable) trading rather than rental income.

## 10. Have you received a notice to complete a Corporation Tax return?

Charities are required to complete and submit Corporation Tax returns if they are served with a notice from HMRC. A Corporation Tax return includes a set of the charity's accounts and a computation of the tax due, in addition to the return form itself.

Charities with consolidated income over £6.5m must submit their accounts to HMRC in iXBRL format.



## Contact



Vikram Sandhu  
Director

T +44 (0)20 7396 4349

E vsandhu@haysmacintyre.com

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