haysmacintyre

Charity and Not for Profit Briefing

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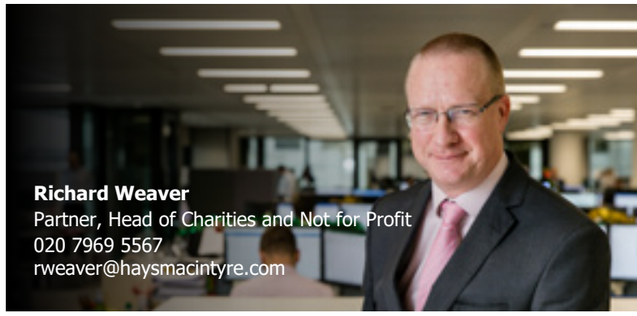
Welcome from the editor

Welcome to this special Charity and Not for Profit Briefing, current as of 1 May 2020. In what is definitely a difficult time for the majority in the charity sector, at this time more than any other, finding appropriate and relevant advice at your fingertips is not always easy. Whilst we have spoken to many clients and provided updates through our COVID-19 webpage, we felt that it would be useful to bring all of this information together in one document.

This edition therefore focuses on a range of questions and queries that we have received recently, some tips and suggestions that we hope you find useful and helpful in managing your charity through these difficult times. My thanks to those who contributed articles and insights to this publication.

A full list of our charity and not for profit team and their contact details are included at the end of this briefing. Please do get in touch if you have any queries in this briefing, or to discuss any other concern you may have. We are here to help.

As the current situation unfolds, further updates to government initiatives and HMRC advice are made regularly. To keep up to date, please refer to our dedicated COVID-19 webpage which can be found at www.haysmacintyre.com/covid-19.



Richard Weaver
Partner, Head of Charities and Not for Profit
020 7969 5567
rweaver@haysmacintyre.com

Government initiatives

Coronavirus Job Retention Scheme
Following the announcement of the Coronavirus Job Retention Scheme (CJRS), we have received several enquiries from clients regarding the processes and practical implications involved. Following a series of guidance notes the Coronavirus Act 2020 Functions of Her Majesty's Revenue and Customs Direction was published on 15 April 2020.

The following provides a summary of some of the frequently asked questions raised by clients and our responses. We trust this FAQ will help answer some of the questions being discussed in your business.

Which employers are eligible to claim under the CJRS?
All UK businesses with employees are eligible to claim which includes:

- Businesses
- Charities
- Not for profit organisations
- Recruitment agencies (agency workers paid through PAYE)
- Domestic payrolls, for example, where a nanny is employed by a family and paid through PAYE
- Public authorities

CJRS is available for employees on the payroll at 19 March 2020.

What about staff who were employed (or were going to be employed) after 19 March?
HMRC have confirmed new employers are eligible to claim under the scheme in respect to employees of a previous business which was transferred after 19 March 2020, if the TUPE or transfer of business succession rules apply to the change of ownership.

If a group of companies transfers employees from multiple payroll schemes into a new consolidated scheme after 19 March 2020, the new payroll will qualify under the scheme.

What is a furloughed employee?
This is a new concept in the UK but essentially it is where an employee is required to take an enforced leave of absence. They will not be allowed to perform any employment duties for the business, in particular those which can be seen as providing services or generating income. The employer must advise the employee of the decision, but equality and discrimination legislation will still apply.

Furloughed employees must have been on the payroll on or before 19 March 2020 (previously 28 February), which include the following contractual arrangements:

- Full-time employees
- Part-time employees
- Employees on agency contracts
- Employees on zero-hours contracts

Unfortunately, employees hired after 19 March 2020 cannot be furloughed or claimed for under the scheme.

Employees who are furloughed can undertake voluntary work. We know of many who are on furlough leave are taking the opportunity to volunteer for the NHS and other support organisations.

Does a furloughed employee retain the same legal rights of employment?
Yes, the employee retains exactly the same employment rights. What has changed is the requirement to provide the services for which they were employed, together with the suspension to their normal salary.

Who else can claim under the scheme?
The scheme has been extended to the following groups, but where they are paid via PAYE:

- Officeholders (including company directors)
- Salaried members of a Limited Liability Partnership (LLP)
- Agency workers
- Limb (b) workers

Officeholders (including company directors)
Where furloughed directors need to carry out particular duties to fulfill certain statutory obligations they owe to the company, they may do so provided they do no more than is reasonably required. They should not carry out any duties which could be seen as generating revenue or providing services on behalf of the company.

Salaried members of a Limited Liability Partnership
Members who are designated as employees for tax purposes are eligible to be furloughed and receive support under the scheme.

To furlough a member, the terms of the agreement between the LLP and the member may need to be varied to reflect the fact that the member will not be performing any duties for the period of furlough and the effect of this on their remuneration from the LLP.

Agency workers
Where agency workers are paid through PAYE they are eligible to be furloughed and receive support under the scheme. The scheme will also include those who are employed via an umbrella company.

The agency will be regarded as the deemed employer, but it will be necessary to discuss with the end client whether they still need the services of the agency worker. Where agency workers are furloughed, they should not perform any duties through or on behalf of the agency that has furloughed them.

Limb (b) workers
Where limb (b) workers are paid via PAYE, they can be furloughed and benefit under the scheme, those who pay tax on their trading profits through Self-Assessment may instead be eligible for the Self-Employed Income Support Scheme.

Will the payments be subject to income tax and National Insurance?
Yes, the payments received under the scheme will be subject to income tax and Class 1 National Insurance which will be deducted from the furloughed pay via the payroll.

What is covered under the scheme?
HMRC will pay a grant to the employer to cover the lower of £2,500 or 80% of the employee's regular pay.

The Government will also pay the employer's Class 1 National Insurance plus 3% workplace pension contributions which will be based upon the furloughed rate of pay.

Personal service companies who are paying their director can also use the scheme, however they will only be able to claim a grant in respect to the salary element, not any dividends extracted from the company.

What about employees who were laid off prior to the announcement owing to no work being available due to the pandemic?
The purpose of the scheme is to protect jobs. If you laid off staff after 1 March, then you can reinstate employees on to the payroll, then furlough them. The furlough pay will qualify under the scheme.

National Minimum and Living Wage
Employees are only entitled to receive the minimum wage whilst they are working. An employee that is furloughed and not working may be paid less than the hourly minimum wage rates.

In contrast, where an employee is required to undertake any training, for example an online training course whilst they are furloughed, then they must be paid the minimum wage for the time spent training even if this is more than the 80% of their wage which is being subsidised.

Maternity Leave, adoption pay, paternity or shared paternity pay

Individuals who are on, or plan to take, Maternity Leave must take at least two weeks off immediately after the birth of a child. If the employee is eligible for Statutory Maternity Pay (SMP) or Maternity allowance, the normal rules apply, and they are entitled to claim up to 39 weeks of statutory pay or allowance.

Employees who qualify for SMP will still be eligible for 90% of their average weekly earnings for the first 6 weeks, followed by 33 weeks of pay paid at 90% of their average weekly earnings or the statutory flat rate, whichever is lower (£151.20 from April 2020).

Where the employer pays enhanced maternity pay, which is earnings related, this is included as a wage cost and will qualify under the scheme.

The same also applies for contractual adoption, paternity or shared paternal leave.

Can the employee undertake any training whilst they are furloughed?

Yes, employees can undertake training while on furlough leave, however the training must not generate revenue for the business neither should it involve the provision of services to the business.

Where an employee is required to undertake any training, for example an online training course, whilst they are furloughed, then they must be paid the minimum wage for the time spent training even if this is more than the 80% of their wage which is being subsidised.

What happens to any benefits in kind and salary sacrifice arrangements?

Under the scheme, benefits in kind are not part of the employee's basic pay, so the reference salary should not include the cost of non-monetary benefits provided by the employer, for example medical benefit.

Similarly, benefits provided as part of a salary sacrifice arrangements (including pensions contributions) which reduce an employee's taxable earnings should not be included as part of the reference pay.

Where an employer provides benefits to furloughed employees, this will be in addition to the salary that must be paid under the terms of the scheme.

Can employees opt-out of a salary sacrifice arrangement whilst they are furloughed?

Normally, employees cannot opt-out of a salary sacrifice arrangement unless there is a life event. HMRC accepts that COVID-19 counts as a life event which could warrant changes to the salary sacrifice arrangement. The employment contract will need to be updated.

How will employers be able to claim under the scheme?

Employers will need to make a claim via the HMRC portal which was launched on 20 April 2020.

HMRC have stated that the following information will be needed:

- The business's ePAYE reference number
- Number of employees being furloughed
- The claim period (start and end date)
- Amount claimed (per the minimum length of furloughing of three consecutive weeks)
- The UK business's bank account number and sort code
- Contact name
- Phone number

Once HMRC has processed the claim they will make payment via BACS into the nominated UK bank account.

Does the business need to pass on all of the grant received under the scheme to its employees?

Yes, the grant is being paid to cover the furloughed salary but subject to the limited set out above.

The employer must not make any deductions from the claims received under the scheme.

Is the amount received via the scheme taxable?

Yes, the payment is effectively the receipt of a grant and will be subject to corporation or income tax depending upon the nature of the business. However, as the full amount received under the scheme will be treated as a salary cost, the business will benefit from a corresponding tax deduction.

The employee will be subject to income tax and Class 1 National Insurance on their furlough pay, which will be deducted via the payroll.

How long will the scheme run?

Initially the scheme was intended to run from 1 March 2020 for three months. However, it has been extended by a further month until 30 June 2020.

The Government will keep matters under review and will announce any further changes or extension dates.

Can the business take the decision not to pay its PAYE and National Insurance liabilities?

No, the purpose of the scheme is to provide support to businesses in meeting their employment costs. Non-payment of PAYE and National Insurance will expose the business to interest and penalties.

What if we pay our employees a reduced salary can we make a claim under the scheme?

No, under the terms of the scheme claims are only possible where an employee has been furloughed.

We recommend that legal advice is obtained where you are proposing to vary an employee's terms and conditions of employment. You must also ensure you are paying the employee at least the minimum wage as required under National Minimum and Living Wage legislation.

For further information on CJRS, please contact Nick Bustin at nbustin@haysmacintyre.com.

Business interruption loans

For SMEs

The British Business Bank (BBB) together with 40+ lending providers are providing a range of financial options enabling SMEs with a turnover of less than £45m to borrow up to £5m, with the first 12 months being interest-free under the Coronavirus Business Interruption Loan Scheme (CBILS). Not all SMEs will be eligible. Further improvements to the scheme were announced on 2 April, which include substantially limiting the lender's right to request (or demand!) personal guarantees. Lenders can no longer request personal guarantees for loans under £250,000 and for loans over £250,000, personal guarantees will be limited to just 20% of any amount outstanding on the CBILS lending after any other recoveries from business assets. The scheme is 'live' (from 23 March) and the BBB strongly recommends that the business's current lender (if also a provider under the scheme) is approached online. Current providers are here. Successful applicants are those that can demonstrate they need emergency funding and can trade out of any short-to-medium term difficulty. Further details are here.

For larger businesses

On 2 April the CLBILS was announced, which is a new scheme for larger businesses. On 16 April the Coronavirus Large Business Interruption Loan Scheme (CLBILS) was extended to all larger viable businesses (with annual turnover of more than £45 million – the upper cap of £500 million has been removed). All firms with a turnover exceeding £45 million will be able to apply for up to £25 million of finance, increasing to £50 million of finance for firms with a turnover of more than £250 million. The finance will be lent at a commercial rate of interest. Similar to the CBILS, the Government will provide the lender with an 80% guarantee. As with the CBILS, the CLBILS is managed by the BBB, and operated by accredited lenders since its launch on 20 April. Further details are on the BBB website here. The Government's latest announcement is here.

For other larger businesses (investment grade companies)

The Covid Corporate Financing Facility (CCFF) was announced as part of the £330bn package and launched collectively by HM Treasury and the Bank of England to provide additional help to firms to bridge COVID-19 related disruption to their cashflows. The CCFF operates via the borrower issuing commercial paper. This scheme is now available for applications. Further details, as published by the Bank of England, are here.

It's important that charities are aware that the charity sector is eligible for both CBILS and CLBILS.

Further information on CBILS and CLBILS can be found on the British Business Bank website and wider COVID-19 government support for businesses can be found on gov.uk.

Information on how to access the government support scheme for larger firms, the COVID Corporate Financing Facility (CCFF), can be found on the Bank of England's website.

Social and Community Capital

Social and Community Capital is a charity and responsible lender funded and supported by NatWest to help social enterprises and community businesses that supports its customers through:

- Loan capital and interest repayment holidays
- Contacting all customers to understand their issues and talk about how the bank can help
- Immediate provision of £500k to be available as grants, with the potential for further grant funds if required in the coming months
- Planning support and mentors for each customer

NatWest Social and Community Capital is also signatory on a joint letter signed by 28 Social Investors to show commitment to work collectively and with urgency to provide flexibility where it is needed and develop new funding programmes. Support available via Good Finance UK includes information on the funds and programmes, support from infrastructure bodies and membership organisations, news and guidance. See the Good Finance COVID-19 Resource Hub for more information.

Further information on ways in which NatWest may be able to assist charities during these difficult times can be obtained from Daniel Jacklin via email at daniel.jacklin@natwest.com or phone +44 (0) 07971 386 189.

Chancellor sets out extra £750 million coronavirus funding for frontline charities

In the daily briefing on 8 April, the Chancellor set out a package of support for charities to ensure they can continue their vital work during the COVID-19 outbreak. Charities across the UK will receive £750 million.

The support will be available for frontline charities across the UK – including hospices and those supporting domestic abuse victims.

Of the funding available, £370 million will be used to support small and medium sized charities, including local charities working with vulnerable people and those delivering food, essential medicines and providing financial advice during the outbreak. In England, this support will be provided through organisations like the National Lottery Communities Fund. £60 million of this funding will be provided through the Barnett formula to Scotland, Wales and Northern Ireland.

The UK government will also provide £360 million, through direct cash grants allocated by government departments, directly to charities providing essential services and supporting vulnerable people. These include:

- Hospices to help increase capacity and give stability to the sector
- St John Ambulance to support the NHS
- Victims charities, including domestic abuse, to help with potential increase in demand for charities providing these services
- Vulnerable children charities, so they can continue delivering services on behalf of local authorities
- Citizens Advice to increase the number of staff providing advice during this difficult time

The Government also stated that they will match donations to the National Emergencies Trust as part of the BBC's Big Night In fundraiser later this month – pledging a minimum of £20 million.

It is understood that government departments will now work at pace to identify priority recipients, with the aim for charities to receive money in the coming weeks. The application system for the National Lottery Community Fund grant pot is expected to be operational within a similar period of time.

Charity financial reporting questions

Content of Trustees' Annual Report

COVID-19 will have a significant impact on the drafting of Trustees' Annual Reports.

Each charity will need to consider the impact of COVID-19 on its activities, financial position and future plans.

The key areas of the Trustees' Annual Report where we would expect to see reference to the impact include:

- Principal risks and uncertainties
- Financial review – this would include impact on future reserves position, changes to post year investment values and impact on defined pension scheme liabilities
- Future plans – the impact the epidemic will have on being able to achieve the plans set out, whether these plans have now changed or where core delivery of services will change

More widely, the Trustees' Annual Report represents an opportunity for the trustees to communicate how they are taking account of the key challenges faced by the charity. It may well be appropriate for trustees to report on the impact of COVID-19 on their charity's ability to deliver its charitable purposes during the year, any impact on the charity's wider strategy and on its beneficiaries, in addition to the specific considerations of risk, reserves and financial resilience noted above.

The SORP Committee has issued detailed guidance on the implications of COVID-19 for charity financial report, which can be found here.

Post balance sheet events note

A post balance sheet event is an event that occurs after the end of the reporting period but before the financial statements are approved and authorised for issue by the trustees.

There are two type of post balance sheet event:

1. Adjusting events
2. Non-adjusting events

An adjusting post balance sheet event is an event which provides additional information about conditions that existed at the reporting date, which affect items in the balance sheet, or reported in the statement of financial activities. Material adjusting events are required to be reflected in the financial statements and the effect should be disclosed in the notes to the financial statements and, if sufficiently significant, in the Trustees' Annual Report.

A non-adjusting post balance sheet event is an event which relates to conditions that arose after the end of the reporting period, but which may have a material impact on the charity in the subsequent period and is therefore useful to the reader of the financial statements. Material non-adjusting events are required to be disclosed in the notes to the financial statements.

Examples of adjusting events that may arise due to COVID-19 include:

- The valuation of a legacy that was subject to the disposal of substantial assets that have subsequently declined in value
- New information concerning the recoverability of a debt
- New information that indicates that the charity may not be a going concern
- If there is uncertainty about the charity being a going concern, this must be disclosed. If the charity is no longer a going concern, the accounts must be restated on an appropriate basis.

Examples of non-adjusting events include:

- The announcement or implementation of a major restructuring
- The announcement of a new fundraising appeal or the degree of success achieved by a fundraising appeal
- A material decline in the market value of investments
- The commencement of major litigation
- The entering into of significant commitments or the identification of material contingent liabilities or the giving of material guarantees

Specific examples:

1. Investments and pension schemes
   For charities with significant investments and/or defined benefit pension schemes, it is likely that the impact of COVID-19 on financial markets will lead to a disclosable non-adjusting post balance sheet event due to a material decline in investment values after the reporting date.

2. Cancellation of events
   Where charities are forced to cancel or postpone events for which attendance fees are charged, amounts received in advance of those events and held as deferred income at the balance sheet date may be repayable and may therefore be genuine liabilities. If the decision to cancel the event was taken after the balance sheet date, this would be a non-adjusting post balance sheet event.

   If the charity's events are organised through a trading subsidiary, whose sole activity is the organising of events, then this may have an impact on the subsidiary's going concern status and on the recoverability of any intra-group debt owed to the parent charity. In these circumstances, there may be an adjusting post balance sheet event, because the cancellation decision will have an effect on the circumstances at the balance sheet date.

Disclosure in the notes to the accounts for non-adjusting events after the end of the reporting period.

For each category of non-adjusting event, the notes to the accounts must provide details of the nature of the event and an estimate of its financial effect or a statement that such an estimate cannot be made.

Audit reports and additional work

While logistical challenges in the provision and review of sufficient appropriate audit evidence may be overcome by the benefits of remote working and cloud-based IT systems, or alternative audit procedures, the rapid spread and financial impact of the virus will have many implications for the recognition of balances and transactions in the financial statements, as noted previously, and will complicate the audit process. These will affect the risk assessments of auditors and may require additional time to make relevant judgements, consider or to obtain audit evidence and will have implications for the form and content of the audit report. These matters will all take time for management and auditors to resolve, and again will require careful co-operation and the need to assess the appropriateness of the reporting timetable. Trustees should consider whether a delay to the normal reporting timetable may be preferable if the alternative is a modification to the audit opinion.

Other questions

Income recognition and judgments

Charities with legacy pipelines or regular fundraising events may have well-established methodologies for measuring these income streams, based on the past performance of estimates or other metrics. Are these metrics still applicable? Can we rely on events taking place as planned, with the expected levels of attendance? If events do not go ahead, will we be obliged to repay donors for amounts received in advance? Are we taking proper account of asset price volatility in estimating legacy values?

Going concern

Have you modelled a range of possible outcomes? Have you stress-tested the charity's reserves? Have you considered unrestricted cashflows separately? Do you have contingency plans/available finance?

Challenges and considerations in charity financial management

Events have happened very quickly and the response of charities to these new challenges have varied widely as their sectors have demanded different responses: arts and culture organisations that run theatres and other for-hire spaces have had to close; fundraising charities have had to reforecast and anticipate the loss of income from cancelled public events and fundraising opportunities; and independent schools have activated their business continuity plans and are providing remote learning for their students.

There are a number of financial management and reporting tools that may lend themselves to further consideration in these times and may help in the short term to bridge the gap and provide more available finance, or at least identify potential funding options.

Loan finance and S124
A number of clients have discussed potentially taking out loan finance which the banks are very willing to do in the current climate, especially where there is a valuable charity asset to secure.

Remember that where you do provide any charitable asset as security for a third party loan, you must comply with the requirements set out in S124 of the Charities Act. This requires trustees to obtain advice (which can be from a suitably qualified member of staff, or an independent contractor) that the loan is needed, that the terms and conditions are reasonable, and that you have a cashflow forecast to evidence your ability to service the loan and repayments for the period of the loan.

This is a mechanism to evidence due regard to the position and to safeguard charity assets as far as possible. Whilst the first two requirements are less subjective, the third (the ability to evidence your ability to repay the loan over the lifetime of the facility) may be more challenging in the current environment and you will have to prepare cashflows and forecasts which ideally extend to the end of the financing period to be able to evidence that you can meet the repayment demands of the loan and meet any covenants that are being requested by the bank.

Converting advance payments into a Gift Aid donation
For a number of sectors that have bookings up front (theatres and other for-hire spaces) we have received a number of calls to ask if they can approach members of the public who have already paid for a ticket or hire to convert their funds into a Gift Aid donation. Unfortunately, legislation on this topic is strict. The Government's guidance on Gift Aid includes specific definitions on types of payments and debt conversions, there is a risk that the trail of money in relation to the payment would not fully satisfy the Gift Aid requirements.

As such, the only way to avoid an unsuccessful claim at present would be for the charity to repay the original ticket amount to the customer and ask them to make a new donation. Of course, this is very likely to lead to a much lower take-up rate than for donation conversion.

The Charity Tax Group (CTG) are calling on the Government to allow Gift Aid to be claimed in such situations in response to COVID-19.

Hopefully HMRC will follow the CTG's advice and make changes to their guidance to enable you to claim Gift Aid on the donation. You would then be able to provide donors with guidance on what they can claim.

Investments
For those charities with investment portfolios, the markets have moved in every direction possible as companies, sectors and governments interact on a daily basis. Short term decision-making on longer term portfolios is not normally advisable, however, having the discussions with your investment managers about the best course of action and any short-term cash draw requirements over the coming months will give them a better chance of protecting the underlying value of the portfolio. Also consider their strategy for ensuring that your portfolio remains in the ranges that you have agreed with them in the shorter term – should some asset classes be rearranged to upper or lower ends of the agreed parameters? The best advice is to speak to your investment managers as soon as possible. Investments and current scrutiny of investment performance is covered later in this briefing.

Guidance for fundraising
Charities have an incredible propensity to do good things. In these times, it is not uncommon to want to raise funds in support of the community, from financial support for key workers and NHS staff to providing use of your facilities for alternative uses.

Whilst no one would argue that these are all laudable in the current climate there are three key considerations:

1. Are the activities that you are intending to do within your current charitable objects? Even if they are good things to do, if your governing document restricts your ability to do it, you should not carry out that activity.
2. Utilising your reserves in support of activities that are not in furtherance of your stated objects may also breach your legal duties. You can only use the funds you have for the aims and objectives in your governing document.
3. Redeploying assets for use in crisis is, again, a common consideration, for example allowing the NHS use of a accommodation facility. Even if your governing document allows the activity, you must also consider your insurance: would it cover you in the event that something went wrong? Be sure to check with your insurer to be sure.

If in doubt, seek counsel with your accountants, legal or other advisors to make sure that you are acting in the best interests of your charity and its beneficiaries.

Guidance to help with running your charity during the COVID-19 outbreak
The Charity Commission has a dedicated page which will be updated regularly with responses to commonly asked questions. They also confirm that charities should continue to report serious incidents using the current guidelines and their own judgement and will advise if and when this situation changes. The guidance can be found here.

VAT
In the current climate many charities will have seen a marked change in their mix of income. For those who have complex VAT arrangements, and in particular those that have partial exemption methodologies, it will be key to ensure that the impact the current situation has had on the business flow through to the VAT calculations. These are often complex calculations and our VAT team are on hand to offer assistance to ensure that the calculations and impact on your organisation are managed effectively. For further advice please contact a member of our VAT team below who can also advise on whether a change in your methodology would be beneficial and achievable. For organisations applying the standard method, now is the ideal opportunity to discuss this as the spring VAT return quarter is usually the end of your VAT year. For organisations using non-standard methods, HMRC's guidance says that if there is a significant change in the in the business then they should be contacted, and from what we have seen from the Government's response to date HMRC seem to be far more sympathetic than usual.

Nick Bustin
Employment Tax Director
020 7969 5578
nbustin@haysmacintyre.com

Phil Salmon
VAT Partner
020 7969 5611
psalmon@haysmacintyre.com

Tim Davies
Partner, Head of Tax
020 7969 5645
tdavies@haysmacintyre.com

Remote auditing

In these unprecedented times there are many challenges that organisations, particularly charities, face. With most charities having either December or March year ends, the onset of another audit cycle adds to those pressures. So what is haysmacintyre doing and how can we help to ease the burden?

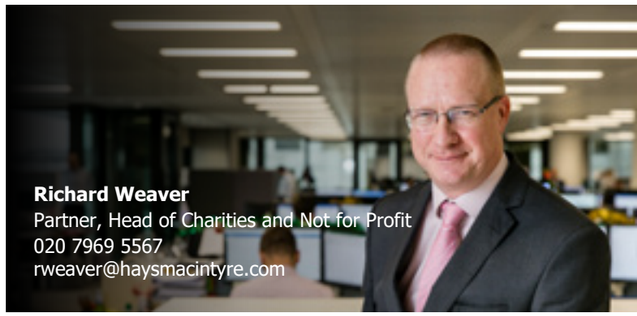
haysmacintyre have invested over the years in having an exemplary IT framework and so we are able to assist clients fulfill their statutory audit duties by deploying our contingency plans and offering remote auditing. Our IT infrastructure allows all staff to work from separate locations through a portal system, which accesses the files as if they were all in our office. Managers are able to access the files and review the work as if they were present with the team. We can set up secure platforms for the sharing of documentation and evidence for the audit file (Sharefile and Inflow as well as email) and keep in touch throughout the process.

There are, however, a number of critical requirements that charity clients can do to assist in the process and work together to ensure that we operate as smoothly as we possibly can. These are:

- Have a set of accounts prepared one week in advance of any fieldwork timetable. This allows us to plan and focus our work in the right risk areas and helps to identify any reporting changes as quickly as possible.
- Have lead schedules with support for all balances in the preparation of the accounts. The charities 'audit file' can be sent through the secure portal or emailed to us.
- Download the nominal ledger transaction history. From these reports we are then able to select the samples of entries that we wish to test so that your team can extract this information and securely send the information through the portal facility.
- Prepare documentary notes on any key judgements and estimates used in the preparation of the accounts. These documents are particularly useful audit evidence but are also helpful internal documents to keep as a permanent record.
- Going concern – this is now the most fundamental judgement that is being made when both the trustees and auditors sign off. New guidance was issued by the ICAEW on 16 March 2020 on the areas to consider and the implications for auditors. These are uncertain times, and so one cashflow will not be enough. You will need to consider various scenarios and document the assumptions you are making, and your boards will need to review these carefully before they make a conclusion. As auditors we will also need to critically assess those assumptions and be comfortable with the results.
- Additional disclosures will be necessary even for those organisations that have strong balance sheets to evidence the risks that are now faced and the impact these may have on the business, even though we may not have the clarity that we would all like. We are seeing an increasing number of examples in different sectors of these additional disclosures and so we can help you reach a point where your disclosures are adequate in order for us to sign off.

These systems and processes are designed to keep the cycle running with as little disruption as possible, but inevitably there will be matters which delay the process compared to previous years. We want to work with our clients to help them in these times, and hopefully the above sets out an approach that will work for most charities and ensure that, we help you meet your statutory obligations.

Whilst the main audit work can continue to be carried out, it may be that there are very good reasons why a charity and its board may wish to delay signing the accounts. Going concern considerations and having more clarity over the current situation are obvious examples. We set out further considerations for going concern later in the briefing. A key date to have in mind is your filing deadline: a reminder that Charity Commission deadlines and Companies House deadlines differ. The Charity Commission requires accounts within 10 months of the year end, Companies House requires filing within nine months of the year end. Consider whether, given the nature of your business and the reserves that you have available, waiting until later in the year to complete the going concern work and signing off is beneficial to you.



Richard Weaver
Partner, Head of Charities and Not for Profit
020 7969 5567
rweaver@haysmacintyre.com

Trading subsidiaries and corporate Gift Aid payments

Although the Government appears to be making some welcome concessions in respect of individual Gift Aid, corporate Gift Aid is less flexible due to the nine month payment deadline and the potential for 'wasted charitable donations', both of which are enshrined in tax law.

Charity trading subsidiaries where income has dropped off may therefore need to reflect, plan ahead and take early action in order to avoid:

1. Unexpected corporation tax liabilities due to insufficient cash and/or distributable reserves to pay up previously generated profits
2. Not being able to claim tax relief in respect of a previously made donation (a 'wasted charitable donation') due to insufficient profits

Insufficient cash and/or distributable reserves

The first scenario is likely to be more common. The subsidiary may not yet have paid its taxable profits up to its parent charity, which must be done within nine months of the year end in order to be set against those profits for tax purposes.

Crucially, the payment must be physically made in cash (not just an accounting entry) and there must be sufficient distributable reserves at the time of the payment. This is particularly important in the situation where a subsidiary is already 'borrowing' reserves from the subsequent accounting period, perhaps due to, for example, expenditure disallowable for tax purposes or timing differences on fixed assets.

So, in the scenario where a previously profitable trading subsidiary is now likely to make a future trading loss, what options are available?

- If cash and reserves are still available, consider making any planned donations sooner rather than later, to ensure corporation tax relief can still be claimed against the previous year's profits.
- Defer the payment and retain some profits and pay corporation tax at 19%, normally due nine months and one day after the year end. A planned retention of profits might be sensible if a full donation would leave it in difficulty and the charity is unable or unwilling to support the subsidiary (see below).
- Consider a carry back of future trading losses to the previous 12 months. Depending on timing, this may still result in cashflow issues, as any corporation tax for the earlier period would likely need to be paid prior to the loss carry back claim. We would hope that under the circumstances it might be possible to agree an extended deferral with HMRC, where it can be demonstrated there will be losses available to carry back that would eliminate the liability. By the date any corporation tax and/or corporate Gift Aid would be due, it is likely that a reasonable estimate of losses would be known.
- Loan or invest: could the parent charity justify making an investment (most likely a loan) in the trading subsidiary? This will be heavily dependent on individual circumstances but any injection of cash by the parent charity must be an 'approved charitable investment'. This is a huge topic in itself, but broadly it must be, and should be possible to demonstrate, that any loan or investment is made for the benefit of the charity. This may be more difficult to demonstrate where the subsidiary is loss making and therefore it is very important that revised business plans and forecasts are examined to ensure it is in the financial interest of the charity to support its ongoing activities, with a particular focus on when it is expected to return to profitability. Amongst other considerations, loans will usually need to carry a commercial interest rate and all decisions should be formally documented. Ideally any loan or investment should be made after any corporate Gift Aid payment, rather than as a short-term solution simply to allow this to be paid. HMRC have been known to object to such circularity in arrangements. Loans and investments will be simpler to justify where a primary purpose trade of the charity is being conducted through the trading subsidiary, as any required funding is likely to be a charitable application of funds.

Wasted donations

Corporate Gift Aid/donations cannot create or increase a tax loss. As such, wasted donations (where donations exceed taxable profits) could result in a future difficulty making sufficient donations to eliminate a tax liability, due to depleted cash and reserves, but without the benefit of additional brought forward tax losses.

Where it is possible to do so, we would recommend consideration of the charity making a repayment of any excess donations which are not necessary for corporation tax purposes, or otherwise reducing the planned donation (where this has not already been paid). Whilst the tax considerations of a charity making a repayment largely relate to timing, there may also be legal implications, particularly where a deed of covenant is in place. Legal advice should be sought if this is to be considered.

Every trading subsidiary and its relationship with its parent charity will be unique and there are many options to consider, therefore please get in touch with your usual haysmacintyre contact to discuss your particular circumstances.

Alice Palmer
Manager
020 7396 4375
apalmer@haysmacintyre.com

Investments

Investment assets are, for many charities, a long term investment that will provide an income to supplement their other income generation, but for others it is the key income stream on which they rely.

Depending on the risk profile of your organisation and the need to balance income and capital growth, there are many and varied approachs to investment strategies, but does your investment policy need some CPR?

Charities and investment matters: a guide for trustees (CC14) recommends that if your organisation has investments, it should have a written policy that sets out what it is aiming to achieve through its investments.

A written policy provides a framework for making investment decisions, helping trustees to manage the organisation's resources effectively and demonstrate good governance. Regardless of size, having a written investment policy is important for all organisations with investment assets.

Most organisations we come across have an Investment Policy or a Statement of Investment Principles. However, in most cases, the documents are either out of date or need some love. Often, it's both.

In many cases, the document was created by decision makers that are no longer with the organisation. Naturally, as your organisation evolves, so does the need to maintain and improve your investment governance.

Without a robust set of documents, it's very difficult to observe how your investment manager is doing. Not only should there be aspirational performance objectives, your policy should also include appropriate benchmarks, any income requirements, tolerances to risk, ethical criteria, and diversification expectations.

Many decision makers with an organisation have their own opinions on how this should look and therefore need help facilitating and documenting the objectives of the collective. Maintaining and reviewing the policy regularly is then paramount to ensuring the quality of your ongoing governance.

When working with organisations, we assess whether their objectives are:

- **C**lear?
- **P**rioritised?
- **R**ealistic?
- **M**easurable?

In our experience, whenever we are presented with a policy document, almost every single one fails our CPR(M) test on one criterion; more than half fail on all four.

The success of anything can only be measured when you are clear on what you are trying to achieve.

Leaving significant amounts of monies in cash that you don't need or can't use - permanently endowed funds, for example - is no longer appropriate. Inflation is eroding capital because interest rates continue to be so low. Couple this with the uncertain economic background, both at home and overseas, and the need for sound governance has never been greater.

The burden of ensuring that your investment portfolios are appropriately invested and can continue to deliver your objectives falls to trustees, financial directors and often other members of the senior management team.

Where time is an issue, or trustees only meet a few times of year, we have seen many organisations employing professional advisors to help. This can remove an element of risk and ensure there is a constant eye on the portfolio. They can also help provide a valuable insight to help your organisation achieve your objectives and ensure that the investment solutions are appropriate, suitable and the strategy is repeatable.

Max King
Assistant Director, EPOCH Consulting
077 3870 6318
max.king@epochconsulting.co.uk

Other key considerations for charities with investment assets

Charities hold investment for a variety of reasons, as we have already noted. The key to any relationship with your investment manager is to ensure that your policy is up to date, but also, in these times, that they are made aware of any need to draw down on the capital value of the portfolio and when you believe you may need to do so.

There are ways in which your investment manager can organise the portfolio to ensure that it is more liquid at the right time for you, or to recommend a revised investment portfolio mix to align the portfolio with your need for cash.

For those charities that have adopted the accounting principles of total return, this will need to be monitored carefully. You should not be drawing on income if the capital value of those investments has fallen below their deemed initial value. Make sure that you are clear on the value of any unapplied income fund on which you can draw and project to ensure that you know for how long this fund can be drawn upon in line with your chosen total return. In the event that you do draw income when you should not, a recoupment of the original investment value will need to be made.

Fraud awareness

Organisations have taken swift action to comply with government guidelines over social distancing which has led to many organisations working remotely and establishing new ways of working. This has meant putting business continuity plans into action over the last few weeks. As the dust settles over changes to the working environment, sadly, fraudsters will try to take advantage of the emergency and change of working environment measures to defraud organisations.

Action Fraud has reported that fraud reports related to COVID-19 have increased by 400% in March alone. The figures reported include fraud scams to both individuals and organisations. Action Fraud has also reported over 200 instances of COVID-19-themed phishing emails.

Changes in the way of working requires careful consideration. It is important to analyse how the existing control framework and compliance with policy and procedures are being applied throughout the organisation and at an operational level. Many organisations have furloughed staff who were key to operating controls which means these controls are no longer functioning or allocated to others creating potential lack of segregation of duties. Individuals working from home also means reduced physical contact time with colleagues and certain processes and control work-arounds being introduced to limit business interruption.

We have evaluated key fraud risks that organisations need to be aware of to minimise their impact. Key areas to consider include:

- **Procurement fraud** – there are a number of ways an organisation can be defrauded. Some scams involve the sale of personal protective equipment, such as face masks and gloves online. Some sellers have been fraudulent by not delivering items after payment has been made or delivering items that are not up to standard.
- **Bank detail changes (payment diversion)** – this has been a well-known scam by fraudsters where supplier bank detail changes are requested by email or letter. Any change request to standing data requires validating and this should be done using contact details available in the database or public domain to verify the change.
- **New supplier fraud** – setting up new suppliers remains a key control where appropriate due diligence checks are essential before a supplier is set up on the ledger.
- **Payroll/HR related fraud** – change requests to HR regarding employee's payroll bank details should be validated and not just completed based on email communication or phone numbers given in the email requesting the change.
- **Internal fraud** – as people work remotely and staff members are being furloughed, the segregation of duties requires careful consideration. The situation gives rise to risk of internal fraud around payments and financial reporting or failure to spot an external fraud attempt.
- **Courier fraud** – as more people self-isolate, fraudsters will carry out courier fraud by cold calling the organisation, purporting to be a bank to gain their trust. The ultimate aim of this call is to trick the organisation into handing over money or their bank details. Raising awareness about fraud instances and reinforcing protocols about unsolicited calls is vital.
- **Remote working and IT security fraud** – as more people work from home, fraudsters may capitalise on slow networks and IT problems, to commit computer software service fraud. Be wary of cold calls or unsolicited emails offering you help with your organisation devices or to fix a problem.
- **Phishing fraud** – these attempt to trick people into opening malicious attachments which could lead to fraudsters stealing organisation's sensitive information, email logins and passwords, and banking details.
- **Impersonation of HMRC or other regulators** – there have been several instances where fraudsters are impersonating regulators. Organisations should be vigilant and contact regulators using contact information available in the public domain or a reliable source.

Simple steps for organisations to take preventative measures:

- Provide guidelines to reinforce existing policy and procedures and raise awareness over fraud matters.
- Monitor the current situation and keep up to speed with common fraud themes and alerts given by Action Fraud.
- Carry out due diligence on suppliers that the organisation engages with.
- Do not click on links or attachments in unexpected or suspicious emails.
- Contact your bank immediately if you think you've fallen for a scam. Your bank will NEVER ask you to transfer money or move it to a 'safe' account.
- Implement additional verification checks and procedures before making changes to standing data (i.e. supplier bank details or employee bank details).
- Implement additional verification checks and procedures before making payments, for example making use of video conferencing facilities.
- Report all fraud instances to Action Fraud.

We would also highly recommend a publication by the Fraud Advisory Panel, a body set up by the ICAEW to provide information and advice in this area. The publication can be found here.

Advice on protecting your organisation from fraudsters

Fraudsters are exploiting the spread of COVID-19 coronavirus to attempt a variety of scams and cybercrime. NatWest's online Security Centre has information on how to protect your business from the latest threats.

Rakesh Vaitha
Senior Manager
020 7969 5629
rvaitha@haysmacintyre.com

Reserves

Now more than ever, charities are reviewing their reserves and the ability to draw down on them in this particularly difficult period.

A lot has been written about reserves and reserves policies, and having sufficient funds available to run the organisations efficiently and meet your future strategy. Many in the sector were criticised for 'holding on' to more than they needed – perhaps the new norm, whatever that may look like, will revisit this particular area for charities and acknowledge that in a very uncertain world, having reserves over and above that to run the business effectively is not actually a bad thing.

We set out below two specific examples of reserve considerations which might help in the current situation.

Endowment funds

Endowment funds come in two types: expendable and permanent.

Expendable endowment funds have always been a bit of an accounting anomaly, particularly from a legal perspective. The notion that you can have an expendable endowment does not sit easily with the legal definition of an endowment which is supposed to be something that is preserved into perpetuity. That said, those that have expendable endowments should consider how the charity should make best use of this pot, as there are no real restrictions over its use and it can provide essential funding for ongoing activity in these times.

Permanent endowment funds are more challenging. These are funds where the intention is for capital value, ultimately to be preserved and only the income arising (or capital gains) can be used for other charitable purposes. There is, however, an interesting loophole for permanent endowments which may not be obvious. Where the endowment funds are represented by properties and investment portfolios, and where you have used unrestricted cash in prior years to develop a property on an endowed site, that spend has also become endowed (or it should have been). What is often lost is that the use of unrestricted funds to capitalise into endowed assets is in fact a loan between the unrestricted fund and the endowment fund. If the endowment fund also holds investments, it is possible to consider utilising those investments to repay the loan and provide unrestricted cash to the charity, ultimately settling a credit that exists in the endowment. The endowment is still preserved in terms of its underlying value.

Restricted funds

These has always been a choice in the SORP for funds that were raised for restricted charitable purposes: to retain them as restricted funds going forward or to transfer them to unrestricted funds once the project/restriction has ended.

If you consider a fundraiser for a capital project, once the project is complete, and there are no further restrictions placed upon you by the donor, the project asset and the remaining fund becomes unrestricted in your hands – you have met the restriction.

Many charities have historically chosen to retain such fund balances as restricted and matched their accounting treatment with the depreciation charge on the asset created.

Given the current circumstances, you could reconsider whether these funds are actually restricted, or whether reclassifying them as unrestricted may assist you. It might not release cash as this is an accounting disclosure change, but what it will do is reclassify those properties as unrestricted and available to the charity for realisation if necessary.

Reserves policy

Looking at reserves policies more generally, it is worth recapping what is required by the charity SORP. Your reserves policy should state the total value of reserves that the organisation holds, broken down between the various types of funds, Endowed, Restricted and Unrestricted.

The 'free reserves' of a charity is a calculated number. It is the unrestricted funds, less anything that is tied up in fixed assets that form part of the unrestricted fund, less anything that you have chosen to designate.

Remember that this calculation can result in you having negative free reserves, particularly if you hold significant high value fixed assets. In this case, a careful narrative should be used to explain the position and it may be helpful to use designations to emphasise this position in the accounts themselves (i.e. set aside a fixed asset designated fund to the extent that you are able to out of general funds, to mirror the calculation of free reserves). At least this way the readers of the accounts are better informed that whilst you may have a significant high value balance sheet, the majority of the value is tied up in bricks and mortar which is not readily convertible into cash for use in the business.

Having calculated your free reserves, you should compare this figure with what you believe the desired level of reserves are. We often see a figure quoted which is a percentage or set number of months worth of anticipated expenditure. Taking a more risk based approach to the desired level of reserves has been common more recently, looking at the likelihood of loss of key income streams for example. However you calculate your figure, the most important aspect for a reader of the accounts is to be able to relate your reserves policy and what you currently have available to your future strategy and this is often a missing element in many sets of accounts that we see. Make full use of the statutory accounts to tell your story.

Going concern

Going concern assessment and disclosures

All charities are required to assess the appropriateness of the going concern basis of accounting when preparing their financial statements. Charities are required to adopt the going concern basis of accounting, except in circumstances where the trustees determine at the date of approval of the financial statements either that they intend to liquidate the charity, to cease operating, or have no realistic alternative to liquidation or cessation of operations. Under the going concern basis of accounting, the charity is assumed to continue operating for the foreseeable future without the intention or need to liquidate or seek protection from its creditors. Assets and liabilities are therefore recorded on the basis that they will be traded or settled in the normal course of business.

Many charities will be affected, either directly or indirectly, by the COVID-19 pandemic and its resultant economic effects and uncertainty. The trustees' assessment of the charity's ability to continue as a going concern will need to reflect the likely impact on the charity's various revenue streams and the degree of uncertainty that exists over the range of potential outcomes. Many charities have diversified sources of income, which may protect them from uncertainty to an extent, but this will also add to the complexity of the going concern assessment because there will be many more different scenarios to consider.

Charities already face more onerous disclosure requirements than commercial undertakings with regard to going concern and it is important that the trustees' assessment, both of the appropriateness of the going concern basis of accounting and of the potential presence of material uncertainties which may cast doubt on the charity's ability to continue as a going concern, is robust.

What is required?

Assessing going concern is not a new concept. The audit regulations have required auditors to assess the trustees consideration of going concern as part of any audit report sign off. However regulators, even before the current pandemic, identified this particular area as one where the regulations and guidance needed to be updated. This was in part due to a number of high profile corporate collapses and an effort to regain public confidence in the work that auditors do in this area.

The new guidance was issued in December 2019. Additional guidance on disclosure for COVID-19 was also issued in March 2020.

The changes really reflect the needs of all organisations to produce accurate cashflows and forecasts, supplemented by a narrative of the assumptions that underpin the projections. It is for the auditors to then stress test the numbers and the assumptions to become content that the represent a valid expectation that the organisation has sufficient availability of cashflow to manage the business for at least twelve months from the date of signing the accounts.

In the current climate, it is likely that one set of assumptions will not be sufficient. There will need to be scenarios which identify the different potential outcomes. They will need to consider, for example:

- Assumptions around the impact of social distancing on the nature of the business
- Timing of any lifting of the lockdown
- Assumptions around the return to fundraising events
- Impact on investment returns and potential draw down of investments to cashflow the business
- Affect of the current position on a total return investment policy
- Cashflow impact of government deferral schemes, or deferral of other key expenditure items, i.e. rent
- Assumptions around the repayment of loan finance
- Ability to fund known commitments
- Recovery of debtors that are still outstanding

One key aspect of this work is that it is not for the auditors to validate the going concern assessment for you. It is for management to present the trustees with this information and for trustees to be comfortable with the judgements, estimates and assumptions being made. The auditors then need to do sufficient work to challenge those judgements, estimates and assumptions to become confident that they are reasonable and that they are in line with their knowledge and understanding of the business and the environment in which that business operates.

The best way to prevent delay is to start on these forecasts early. Don't leave them to the last minute and discuss with your auditor what they require at the planning stage of the audit.

Contracts and legal considerations

The COVID-19 restrictions have left charities wondering what happens if they are unable to fulfill their obligations under a contract, for example by cancelling an event or suspending a service.

Here are the most common issues and challenges to think about when there are obligations to perform under a contract, with particular focus on force majeure and frustration.

The starting point will be to review your key contracts as soon as possible. You'll need to consider:

- What are the parties' obligations under the contract, and when must they be performed? Are the obligations stated sufficiently clearly?
- How does COVID-19 impact on the parties' ability to perform their respective obligations under the contract? What specific practical difficulties does it create?
- Does the contract contain provisions allowing one or both parties to terminate it, or postpone performance? If so, in what circumstances can the parties do so?
- Does the contract explain what the consequences of termination, or delayed performance, would be? In particular, what are the financial consequences for the parties, and do you risk being sued for a failure to perform your side of the bargain?
- Is performance of the contract physically or commercially impossible, such that it may have been frustrated?
- Can you rely on COVID-19 and its effects as a force majeure event? Is there an express force majeure clause in the agreement? What, in practice, are the consequences of invoking it?
- What would you ideally like to achieve – ending, suspending or varying the contract – and how important is it to preserve your commercial relationship with the other party?

Whilst there are no hard and fast rules, and each contract will need to be considered on its own specific facts, we discuss below some general principles that will help you to work out what your legal position is likely to be and inform your position in negotiations with the other party.

Frustration

In some circumstances, performance of a contract may be 'frustrated'. A contract may be discharged on the grounds of frustration when something occurs after the contract has been entered into which makes it physically or commercially impossible to fulfill the contract, or changes the parties' obligations into something entirely different from what they had envisaged.

In the context of COVID-19, a contract might well be frustrated because of a change in the law that makes fulfilling the contract illegal, by removing all or a substantial amount of the benefit that one party receives from the contract, or by a delay beyond the parties' control that goes far beyond what was envisaged by the parties when the contract was formed.

A party cannot rely on the concept of frustration if the contract has already made express provision for COVID-19 and its impact (for example under a force majeure clause). You can't rely on frustration if the event was or should have been foreseen by the parties, or just because the contract is no longer commercially attractive to perform in the present circumstances. Many contracts will fall into this last category.

Force majeure clauses

In English law, force majeure refers to a set of circumstances beyond the reasonable control of the parties to a contract. You can't rely on force majeure unless the contract expressly refers to it. If so, it will define what a force majeure event is, for example, war, natural disasters, disease, 'acts of God' and so on. The volcanic ash cloud that caused major travel disruption in 2010 is an example of a force majeure event.

Where any of these circumstances apply, the parties will be excused from performance of their obligations, at least until the conclusion of the force majeure event(s). A force majeure clause will normally set out clearly how the obligations under the contract will be affected in the event that the clause is triggered.

If your contract contains a force majeure clause, you will need to carefully review the wording and consider whether the impact of COVID-19 falls within the definition. If the clause refers to a 'pandemic' or a similar situation, it may come to your aid. Likewise, if the Government takes further legislative or administrative action that impedes performance of the contract, such as restrictions on travel or movement, you may be able to rely on that.

Even then, you will need to be able to show that the force majeure event has prevented, or sufficiently delayed or hindered, the performance of the obligations under the contract, i.e. that there is a causal link.

Whether you are excused from performing your obligations entirely, or just entitled to a delay, will depend on the exact wording.

If you intend to invoke a force majeure clause, you will need to discuss the matter with the other party to the contract and, preferably, reach agreement.

You can find a more detailed article about contracts and coronavirus here.

Contracts are just one of the areas where charities are seeking legal advice. Others include:

Charity meetings – can we hold valid trustee meetings despite the lockdown?
What matters at the moment is making the best decisions you can, not how you make them. However, this brief guide to trustee meetings aims to help you to get the procedure right.

Can we release funds from our restricted funds and endowments?
There may be some scope to release restrictions, for example by considering whether they are in fact legally binding, or using powers in the governing document or the Charities Act 2011. See this article for more detail on this.

Can we borrow to raise additional funds?
Many charities may be looking to borrow in order to provide liquidity to sustain their operations during the current crisis. Trustees should consider not only whether the terms of a proposed loan are suitable for the charity, but check that the charity has the power to enter into the loan in the first place. This article takes a brief look at different types of charitable entity and how they can check whether they have the power to borrow.

There is more information on the legal issues affecting the sector in the Bates Wells coronavirus hub.

Phillip Kirkpatrick
Deputy Managing Partner and Head of Charity, Bates Wells
020 7551 7762
p.kirkpatrick@bateswells.co.uk

Robert Oakley
Partner and Head of Dispute Resolution, Bates Wells
020 7551 7792
r.oakley@bateswells.co.uk

Charity and not for profit team

If you need guidance on any audit and accounting, financial reporting, statutory obligations, funding, employment tax or direct tax matter you can contact any member of our charity and not for profit team at the details below.

Richard Weaver
Partner, Head of Charities and Not for Profit
020 7969 5567
rweaver@haysmacintyre.com

Adam Halsey
Partner, Head of Faith Charities
020 7969 5657
ahalsey@haysmacintyre.com

Anna Bennett
Partner
020 7969 5542
abennett@haysmacintyre.com

David Sewell
Partner
020 7969 5568
dsewell@haysmacintyre.com

Jeremy Beard
Managing Partner
020 7969 5503
jbeard@haysmacintyre.com

Kathryn Burton
Partner, Head of PIMBs
020 7969 5515
kburton@haysmacintyre.com

Lee Stokes
Partner
020 7969 5656
lstokes@haysmacintyre.com

Murtaza Jessa
Partner, Head of Charities
020 7969 5551
mjessa@haysmacintyre.com

Steve Harper
Partner
020 7969 5608
sharper@haysmacintyre.com

Tom Wilson
Partner
020 7969 5697
twilson@haysmacintyre.com

Tracey Young
Partner, Head of Education
020 7969 5654
tyoung@haysmacintyre.com

Tax specialists

Louise Veragoo
Not for Profit Tax Director
020 7969 5682
lveragoo@haysmacintyre.com

Phil Salmon
VAT Partner
020 7969 5611
psalmon@haysmacintyre.com

Nick Bustin
Employment Tax Director
020 7969 5578
nbustin@haysmacintyre.com

haysmacintyre

haysmacintyre
10 Queen Street Place
London EC4R 1AG

T 020 7969 5500
F 020 7969 5600
E marketing@haysmacintyre.com

www.haysmacintyre.com
@haysmacintyre

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