APPG on Charities and Volunteering
Charity taxation: is it time for reform?
16:00-18:00 Monday 5 February 2018, Committee Room 21

Nick Montagu, chair of the Charity Tax Commission (CTC)
- The CTC will look at the rationale for charities and for their tax reliefs to see how effective the current system is at increasing public good. The CTC will not focus on fine operational detail of how each relief works.
- Over 18 months the CTC expects to take evidence, review and make recommendations for government on how tax can be improved for public benefit. The CTC hopes to inform a government long term vision for the sector, which has been lacking. Recommendations will be realistic, and will try to be cost neutral, not advocating further public spending for the sector.
- The Commissioners are expert and diverse group. HMRC agreed the review is timely and needed, and are observers to the group, alongside HMT. Technical and sector expertise will be provided by a reference and advisory group. The commissioners will issue a public call for evidence, seeking input from anyone with relevant expertise and experience, and will aim to hold a series of meetings across the UK.
- The role of charities is now very different from when the last review was carried out 20 years ago – charities are now surrogates for public service delivery, which has resulted in an increase in earned income, and a move from grants to contracts.

John Hemming, chair of the Charity Tax Group and head of tax at the Wellcome Trust
- There are many aspects of how charities work that weren’t anticipated by tax law – for example books are zero rated, but ebooks aren’t. Digital giving has been invented since the laws were written. The legislation has no flexibility, and doesn’t meet its original intended purpose.
- Charities do pay some taxes, such as VAT and employer tax. Despite being a charity the Wellcome Trust is the 80th highest tax payer of the UK’s 100 largest businesses.
- Charities are considered the end consumer of products they buy, so can’t reclaim most of the £1.5bn they pay in VAT. Charities should not be considered the end consumers as resources are used for public benefit. The lists of items that you can claim relief on, such as medical equipment, soon goes out of date.
- There are quirks to the system. The government outsources services, but must pay VAT on the services it buys, which becomes a disincentive to outsource. For corporation tax, not all sources of income are exempt, so charities are taxed, despite funds being used for charitable purposes.
- The EEC is proposing drastic changes to give member states much more flexibility in how they charge VAT, to allow them to zero rate anything they want. It is uncertain what will happen with Brexit, the UK could potentially lose existing zero rates if we re-enter the EU on new terms.
- We should flip the tax system on its head and give all charities total tax exemption, writing legislation for specific areas Government thinks charities should be taxed on.
- Charities are often caught by anti-tax avoidance legislation, but charities aren’t avoiding tax, as they are tax exempt. Charitable purpose should exempt organisations from anti-avoidance laws. Charities seem to be the collateral damage in tackling tax avoidance, but it should be individuals who are targeted.
Sarah Smith, professor of economics at the University of Bristol

- These reliefs are increasingly claimed – total giving has been flat, but Gift Aid is up 50% in a decade, and higher rate relief is up 100%. This still only accounts for half of donations.
- Reliefs are a transfer from government to charities, and with the pressure on public services people are right to ask why we are funding charities when we could fund education or health.
- The total value is relatively small for the government, but very large for the sector – removing these reliefs would inflict damage on charities without a discernible change to public finances.
- The alternative to tax reliefs could be a grant system. Tax reliefs distribute funding widely – 70,000 charities receive Gift Aid, and it would be hard for government grants to replicate this. Funding doesn’t follow need though, just donor preference. A grant system could follow need but would be costly and may fall foul to regulatory capture.
- Reliefs encourage further fundraising – grants cause charities to focus less on fundraising, but Gift Aid is like match funding, so positively rewards good behaviour. Tax reliefs may also encourage donors to give more, which grants wouldn’t, leading to more funds overall. There is evidence that there is a large jump in legacy giving at the tax threshold, so it is effective at persuading people to give – although simply asking is also persuasive.
- Our previous research for HMT/HMRC found that increasing Gift Aid does cause people to give more if they know the government will too. There is less of a link for higher rate relief; people are not as sensitive to the amount they can claim back, unless the value of the rebate is high and/or people give a large amount. This means it would be most efficient (cost-effective) to target higher rate relief only on larger donations, though a small number of charities will benefit from this.
- There are figures for the amount tax relief costs, but they assume that higher rate payers would pay all of their tax, when they may find other ways to reduce the amount of tax they pay. Savings from reducing tax reliefs may be over-stated.

**Audience Q&A**

Asked whether they would look at different taxation for different charitable activity, for example campaigning or delivering public services, NM said that the commission would be open in looking at ideas, but they first needed to understand the conceptual underpinning of charity tax reliefs.

There was discussion of whether we should consider Gift Aid as public expenditure or a government opportunity loss. JH said that HMRC consider it an opportunity cost- and were it to be treated as public spending it may have to compete with other spending priorities. SS said it is important we consider whether this is an appropriate use of funds when spending is tight – but we know it has a positive impact, and increases money for good causes.

Asked whether we could encourage people to donate more of their salary were they able to deduct the donation from their taxed income, SS said that the evidence shows that the tax rebate for higher rate payers isn’t effective at increasing donations – people are more motivated by the matched giving element of Gift Aid.

Lord Hodgson suggested that the law should be changed to allow people to bequeath their house to charity, but to continue to live in it rent free until they die. You can’t currently, and it would allow charities to borrow against the asset until it came in to their possession.

Asked where we would make up the difference if the government were to allow charities to recoup an extra £1.6bn in VAT, JH said that the proposed changes require all VAT to balance as 12%
on average – so if there were more zero rating for charities, there would be an increase elsewhere. It would be cost neutral for the country but an increase in income for charities.

Asked whether the CTC could consider the needs of small charities, the bulk of whom don’t currently qualify for Gift Aid as they don’t receive donations and more affected by business rate relief and insurance premium tax. NM said that the commission were conscious that most charities are very small.

It was suggested that the current VAT system stops charities collaborating and using their advantage, as VAT is charged on services between charities. This stops charities getting better.