Not for Profit eNews

February 2022

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Welcome to the latest edition of MHA Not for Profit eNews.

In this issue, we look at the impact of inflation on the Charity sector and the use of dormant assets for Community Wealth Funds. We provide an update on the Government's 2022 National Cyber Strategy, the New Regulations published for LGPS, and grant programmes currently available for charities.

We also look at the Charity Commission's 5 Minute Guides for Charity Trustees that are a great aid to refreshing knowledge on a number of key areas.

Best Regards,

MHA Not for Profit team

Impact of inflation on the Charity sector

It has been reported by the Office for National Statistics (ONS) that inflation hit a high of 5.4% in December and is forecast to continue to rise until at least April, and that such high rates are likely to remain for the next two years. This will mean that costs will be significantly higher than anticipated Charities should be considering the impact this may have on organisational costs, value of donations and investments, and increasing demand for their services.

It is key that those charged with governance of the charity factor in these increases into their planning assumptions as the impact may continue for years. Key areas to consider are changes in demand for services provided, wage negotiations for employees, and revised planning of income targets and delivery.

There are three main ways in which inflation is likely to affect charities:

1. **Charities will see costs rise, especially for staffing:**
   Wages for charity staff will need to rise by 9% in two years to keep up with the predicted inflation. Salaries will be one of the most notable costs increases, which coinciding with the new national insurance rates increase from April 2022 which could see many charities unable to keep up. If the sector salaries start decreasing this could result in significant staff turnover with many positions left unfilled which can only exacerbate the current resource shortfall.

2. **Charity income is unlikely to keep up with inflation:**
   Charity income relies largely on donations, grants, and/or reserves. These are three areas that are likely to impacted by inflation. For donations this may simply be that the donation value will not increase too, meaning that the same amount of income will not represent the same value to the charity.

3. **Changes in demand due to the cost-of-living squeeze:**
   Many charities provide services and support to the most vulnerable in society, who already have an increased need for help following the pandemic. The increased inflation is likely to drive up demand for charity services further. With increased costs, and a lower value of income, it may be difficult to meet these demands. For charities that rely on consumption from individuals, e.g., museums, theatres etc., they too are likely to experience decreases as people may have less disposal income available to partake.

Grant programmes available to charities

There have been many announcements regarding grant programmes that are currently available to charities and accepting applications.

POhWER are offering grants up to £2,000 to support individuals who want to become a trustee or volunteer or who are seeking support concerning their employment, education or health. The grant is also available to groups.

Covid Recovery Fund (Sheffield) are offering grants of £10,000 - £50,000, focused on filling shortfalls due to loss of income due to the impact of the pandemic in voluntary and community organisations. This fund is for registered charity's, charitable incorporated organisations and limited companies with charitable status.

Royal Society are offering grants up to £3,500 to small museums to fund projects that tell stories about science in new and creative ways and which are designed to increase interest in science across society.

Severn Trent Community Fund is focused on funding environmental charities and community groups with grants of £5,000 - £20,000. Eligible organisations must have an average annual income of less than £500,000 over the last three years.

Kent Community Foundation has been given £150,000 of The Arts Council England Let's Create Jubilee Fund, which made £5m available to community and voluntary organisations with charitable aims. There is a particular focus on arts and creative institutions to apply to exhibit Britain's cultural heritage. Grants are to be from £750 - £10,000.

The Fat Beehive Foundation Fund provides small grants up to £2,500 for websites and digital products to other small UK charities. Charities to consider applying for a grant are those that make less than £1m a year.

Sport England is distributing £300 - £10,000 grants from a pot of £5m of National Lottery funding for the Queen's Platinum Jubilee. Specifically, for not-for-profit organisations, Sport England are looking for projects that encourage people to get active. They particularly want to support projects operating in areas of high deprivation.

More information for these grant programmes can be found on the various websites of each funder.

National Cyber Strategy 2022

The Government is working to improve the cyber resilience of individuals and organisations across the UK as part of their £2.6 billion strategy. The Department of Digital, Culture, Media and Sport have published the "2022 cyber security incentives and regulation review".

The review details the progress made since the implementation of the General Data Protection Regulation (GDPR) / Data Protection Act 2018 and the Security of Network and Information Systems Directive 2018, and the Government's planned changes to their approach towards cyber security.

According to the Cyber Security Breaches Survey 2021, two in five businesses report having experienced cyber security breaches or attacks in the last 12 months. Among the businesses that identify breaches or attacks, over a quarter are experiencing these issues at least once a week. COVID-19 has increased our reliance on digital technologies and has changed the cyber security landscape. Around a quarter of the incidents the National Cyber Security Centre responded to in 2020 related to COVID-19.

The review sets out the Government's changes to their existing approach, as it has been recognised that the current approach is not meeting the fast changes in demand and the scale of reliance being placed on digital platforms. The key policy areas identified relate to foundations, capabilities, market incentives, and accountability.

Cyber threats cannot be eliminated completely since digital technology is open, and openness brings exposure to risk. However, the risk can be greatly reduced to a level that allows society to continue to prosper and benefit from the huge opportunities that digital technology brings. The 2022 National Cyber Strategy will set out the governments approach to managing these risks, to help to protect the public, UK businesses, and critical national infrastructure from emerging threats.

In addition to the review, the Government is consulting on proposals for legislative changes to increase cyber resilience, as well as consulting on embedding standards and pathways across the cyber profession by 2025.

A new dawn for charities in LGPS

David Davison of Spence and Partners, a leading expert in their Public Sector, Charities and Not-for-Profit practice, advises employers and third sector bodies on all aspects of multi-employer schemes. David has reported that there is a new dawn for charities in LGPS, as follows.

Charities have for a long time found themselves trapped in Local Government Pension Schemes, struggling to pay contributions and deal with ever increasing balance sheet liabilities whilst being unable to afford to exit their scheme. Thankfully help is now at hand.

New regulations were published in September 2020 which added new exit options, but each individual Fund needed to consult with their actuarial and legal advisers to formulate their rules and make them completely transparent for charity employers to follow. It's taken a while for Funds to do that, but most are now completed, or Funds will work based on the likely outcome if they're not. The new options available should offer employers much more affordable and flexible exit options and many charities are already utilising these.

The problem

When charities run out of contributing members or look to exit LGPS a cessation (exit) debt will be calculated. This is carried out on a 'nil risk basis' which means that the liabilities, and therefore any deficit, is much higher than on an 'on-going' or FRS102 accounting basis. Many third sector organisations therefore find themselves with the Hobson's choice of continuing to build additional unaffordable liabilities or meeting an unaffordable exit payment. A number of organisations have recently found themselves driven into insolvency by the weight of their pension liabilities.

The new flexibilities

The new LGPS Regulations now formally provide two additional options:-

1. **Debt Spreading Agreement ('DSA') –** this allows exiting employers to enter into agreements with LGPS to fund any cessation debt due over a period of time. This would allow uncertain pension liabilities to be turned in to a stream of fixed payments to be set over an affordable agreed term.

2. **Deferred Debt Agreements ('DDA') –** this allows schemes to defer any exit payment and to permit the employer to carry on in the scheme on an on-going basis. The employer would retain all the same obligations to the scheme with future payments uncertain. However, immediate costs are likely to be lower and therefore much more affordable, allowing employers to better manage the risk of future benefits building up. Valuations would be carried out regularly and contributions adjusted if necessary.

These changes could be hugely welcome for many charities.

The process

The process being adopted looks broadly consistent across Funds:

1. To seek a DSA or DDA the charity should make a proposal to the Fund providing the reasons for the request and any supporting information.

2. The Administering Authority will then consider the request. The assessment will be primarily focussed on the employer covenant (ability to pay) and also any steps the employer can take to strengthen the covenant for the scheme, such as the provision of security or guarantees. The Fund is likely to commission covenant research from a financial specialist as part of the process.

3. There is then likely to be some discussion / negotiation around the terms of any arrangement covering the contributions, term and security arrangements.

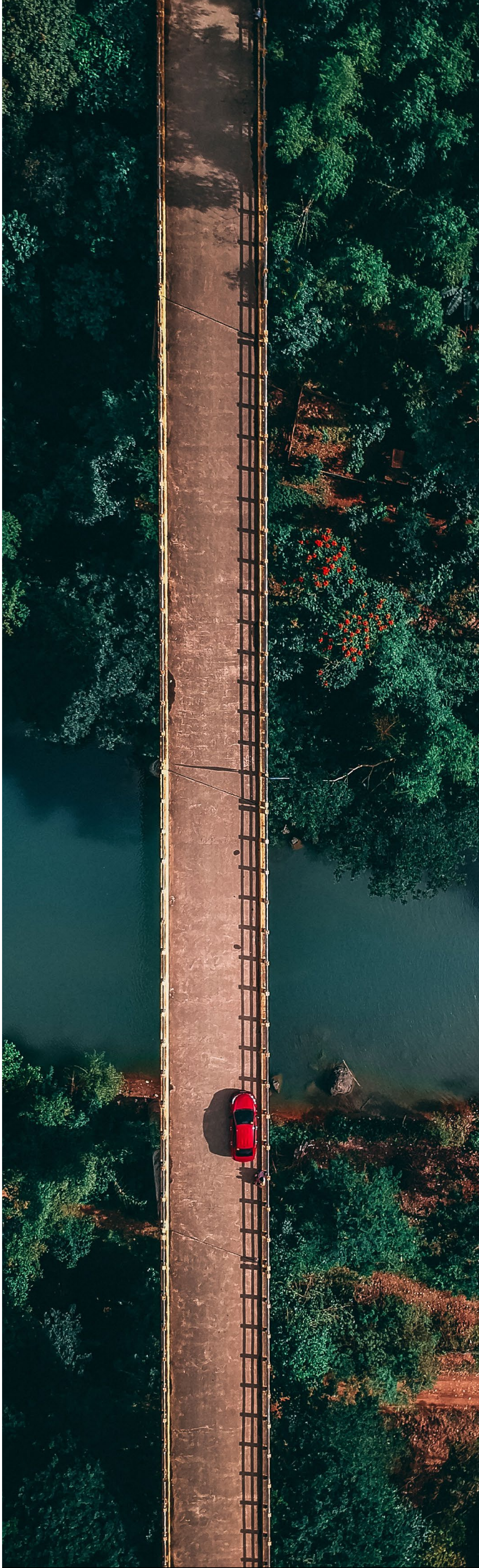
4. Once a basis is agreed this will then be documented in a formal legal agreement.

5. This process is likely to take between three and six months when you add in charity Board and staff engagement.

Clearly the more challenging the financial circumstances which the charity finds itself in the more difficult any negotiation is likely to be. It has however been recognised, right back to the original consultation on the proposed changes, that even where an employer provides a weak covenant entering into some sort of agreement, which reduces future risk by stopping further accrual, this could be preferable to the status quo and provide greater protection for continuing employers. It cannot be in anyone's interests to see employers continue to accrue liabilities well beyond the point they are affordable and then to continue to provide for further accrual.

Conclusion

Given the budgetary pressures charities are likely to be facing as we emerge from the Covid-19 pandemic, these changes represent a significant opportunity for organisations to manage a major financial risk. Charities should therefore engage with their professional advisers and Funds to consider what approach would best suit them.



New Year Resolutions – 5 Minute Guides for Charity Trustees

Making a fresh start for 2022, the Charity Commission has reminded Trustees that they have a number of handy 5-minute guides which can be used to refresh knowledge on a number of key areas.

These 5-minute guides cover the following key areas:

Purpose – As a trustee, you must run your charity in a way that complies with your charity's governing document and the law. This includes making sure your charity achieves its purposes.

Managing charity finances - As a trustee you must take steps to make sure that your charity's money is safe, properly used and accounted for. Every trustee has to do this. Even if your charity has an expert to manage its finances, you are still responsible for overseeing your charity's money.

Managing conflicts of interest - As a trustee you must make decisions based only on what's best for your charity. Do not allow your personal interests, or the interests of people or organisations connected to you, to influence these decisions.

Making decisions at a charity - As trustees, you need to work together to make the best decisions you can for your charity. Often there will not be a perfect solution. Your decision can be different from one another group of people would reach, but it must be an informed and responsible one in your situation.

What to send to the charity commission and how to get help - Your charity's entry on the register is public information. It must always be up-to-date – you can easily use the register of charities to check your charity's entry. You and the other trustees are responsible for making sure your charity's entry is up-to-date, even if you ask someone else to do it for you.

Safeguarding for charities and trustees - All charities have a responsibility to ensure they don't cause harm to anyone who has contact with them. Charities working with children or adults at risk have extra responsibilities. As a trustee you must make sure your charity fulfils this responsibility. Even if you delegate some activities to a safeguarding lead or group, you retain overall responsibility.

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At MHA we also have a number of resources which can help Trustees - more can be found at our **MHA Trustee Hub** or feel free to get in contact with one of our specialists across the UK.

Dormant Assets to be used for Community Wealth Funds

The UK Government has blocked an attempt to allow dormant assets to be used for community wealth funds by removing an amendment to the Dormant Assets Bill that would have allowed money raised to be used to create community wealth funds.

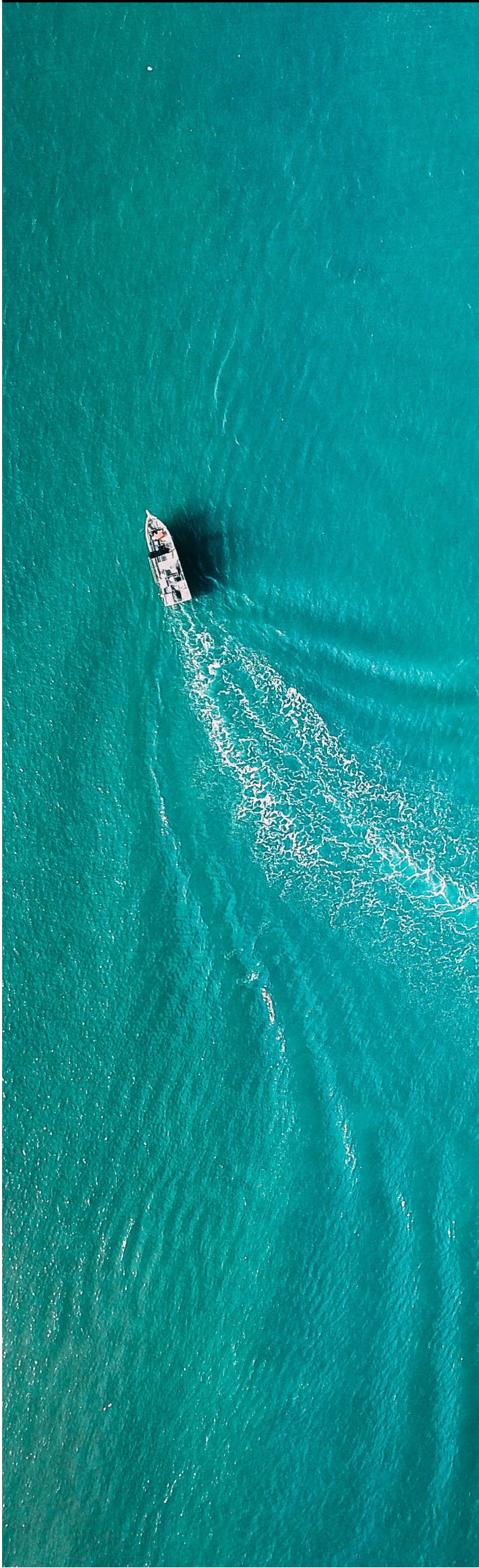
The Dormant Assets Bill is designed to expand the 'dormant assets scheme' to include sectors including: insurance, pension, investment, wealth management and securities sectors.
The legalisation was widened to include these sectors in the House of Lords, so that these funds could be used to;

> **make grants and other payments to support the provision of social infrastructure to further the wellbeing of communities suffering from high levels of deprivation and low levels of social infrastructure.'**

The aim was to help deprived communities, using these dormant assets in a pooled way to provide positive outcomes.

However, the bill which has since passed the House of Commons was altered at committee stage, during the second week in January 2022, to remove the amendment.

The Charities Minister, Nigel Huddleston, has agreed to run a consultation once the bill (which had cross party support) has royal assent on making community wealth funds a possible use for dormant assets in England.



Charities providing accommodation - VAT

HMRC have failed in their attack on a charity providing hostel accommodation to the homeless. The first-tier tribunal have recently found in favour of City YMCA London (CYL) regarding the VAT treatment of rent from homeless people in their hostels.

The Tribunal found that there was no supply of welfare services such that the welfare exemption for charities did not apply to CYL's income. The case focused on whether the tenant had exclusive possession similar to a licence to occupy land which would result in the accommodation being treated as similar to hotels and boarding houses and therefore standard rated but being eligible for the 28 day rule to exempt the income for the accommodation element after the 28th day whilst still allowing for full deduction of input VAT. Being a hotel or similar would also allow CYL to make use of the COVID-19 temporary reduced rates applied to hospitality - 5% between 15 July 2020 and 30 September 2021 and 12.5% between 1 October 2021 and 31 March 2022.

Following an inspection, HMRC decided that the agreements with the tenants did not meet the conditions to be treated as a licence to occupy and could not fall under the hotel and similar rules. VAT at 20% was therefore due with no reduced rates applicable.
This would have meant a substantial increase in the amount of VAT payable and therefore CYL appealed to the first-tier tribunal. The tribunal found in favour of CYL ruling that contractually there was a license to occupy the accommodation and the hostels' purpose and function was similar to a hotel. We are waiting to see if HMRC appeal the decision.

If you are a charity and supply accommodation, it is important to ensure that the agreements between the charity and the users reflect a licence to occupy arrangement. With this in place the providers, including charities, can take advantage of both the COVID-19 reduction in the VAT rate, to 5% and then 12.5%, as well as the 28-day reduced VAT rule for accommodation suppliers.

Please contact our VAT team here if you would like to discuss how this case impacts your charity, or for any other VAT advice.

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