The Charity Law & Practice Review

SOME TAX PLANNING OPPORTUNITIES WITH THE NEW INCOME TAX RELIEF FOR GIFT OF SHARES AND SECURITIES TO CHARITIES[1]

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Introduction

The income tax relief for gifts of shares and securities to charities is found in s.587B ICTA 1988, inserted by s.43 FA 2000. It is one of the more significant reforms to emerge from the review of charity taxation, and has important tax planning implications. We refer to it as Qualifying Investment Donations relief or QIDR. The relief applies to individuals and companies and the rules are broadly similar for both, but for convenience we shall consider the position of individuals first.

The Conditions for Relief

The following conditions must be satisfied for the relief:

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1 This article is based on the new edition of *Tax Planning & Fundraising for Charities* by Robert Venables QC and James Kessler (3rd edition, 2000).

The authors are grateful to Christopher McCall QC who first pointed out the implications of QIDR for overcoming the problem of *St Dunstan v Major* at a Key Haven Conference in October 2000.

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(1) An individual disposes of the whole of the beneficial interest in a qualifying investment to a charity.[4]

(2) The disposal must be "otherwise than by way of a bargain made at arm's length".

(3) The disposal must be to a "charity" (in the income tax sense).

See s.587B(9).

Qualifying Investments

The disposal must be of "qualifying investments" which means any of the following:

(a) shares or securities which are listed or dealt in on a recognised stock exchange;[5]

(b) units in an authorised unit trust;

(c) shares in an open-ended investment company; and

(d) an interest in an offshore fund.

See s. 587B(9).

The Operation of Relief for the Individual

Unlike Gift Aid relief, there is no grossing up of the donation and no tax reclaim by the charity. Instead relief is given by the technique of a deduction from total income: section 587B(2)(a).

There is no relief against capital gains tax on chargeable gains accruing to the individual. So he should limit his donation to his taxable income or (to maximise the tax advantage) his income subject to tax at the higher rate.

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4 It follows that if investments are held jointly by (say) H and W, relief does not apply if H makes a gift of his interest. If H and W simultaneously make a gift of the whole it is considered that the relief applies by virtue of s.6(c) Interpretation Act 1978.

5 Defined in s.841 ICTA 1988.

"The Relevant Amount"

The amount of the relief is described in the section as "the relevant amount".

This is *prima facie*:

(a) where the disposal is a gift, the market value of the qualifying investment at the time when the disposal is made;

(b) where the disposal is at an undervalue, the difference between that market value and the amount or value of the consideration for the disposal.

Two adjustments are made to this figure.

First, if the donor or a connected person[6] receives benefits in consequence of the disposal, the value of the benefit is deducted from the "relevant amount". See s.587B(5). The position is similar as for Gift Aid[7] except that:

(1) QIDR does not have an equivalent to the Gift Aid exemptions for small benefits and rights of admission and

(2) benefits restrict the relief, but do not nullify it altogether. This is significant, as will be seen.

The second adjustment relates to the incidental costs of making the disposal but those costs will normally be trivial.

CGT Relief

Very generously, the usual CGT relief on gifts to charity will also apply on the gift.

Position of the Charity

Section 587B(3) provides:

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6 Defined s.839 ICTA 1988.

7 See Tax Planning and Fundraising for Charities, 13.10 (The No-Benefit Rule).

> "The consideration for which the charity's acquisition of the qualifying investment is treated by virtue of section 257(2) of the 1992 Act as having been made –
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> (a) shall be reduced by the relevant amount; or
>
> (b) where that consideration is less than that amount, shall be reduced to nil."

In short, the individual's income tax relief is deducted from the charity's base cost for CGT. However, this will not normally concern the charity, because it will qualify for the usual CGT relief on its gains.

The sum given is not treated as the income of a charity (contrast Gift Aid).

Charity Aid Foundation

The CAF offer a scheme where they accept gifts of shares and other qualifying investments, with onward transmission of proceeds of sale of the investments to any charity.

Gift and Immediate Sale

In principle, it is possible to give the investments to a charity by declaration of trust, sell as nominee for the charity, and transfer the sale proceeds to the charity. It is essential that the documentation is all correct, or else QIDR relief will be lost, and the transaction treated as a cash gift to charity.[8]

Corporate Donor

The relief also applies to a company (but not to a corporate charity). Like corporate Gift Aid, the method of giving relief is that the "relevant amount" is treated as a charge on income: see s. 597B(a)(ii).

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[8] That cash gift would normally qualify for gift aid relief, but the basic rate relief is enjoyed by the charity, not the donor.

Maximising the Benefits

Gift of Shares

If shares (or other qualifying investments) are given to charity, there is no capital gains tax on the donor. There will be an income tax relief for the value of the shares.

Sale and Gift of Proceeds

If shares are sold and the proceeds given to charity, there will be a charge to capital gains tax on the vendor but Gift Aid relief from income tax/capital gains tax should be available on the whole of the amount gifted

Optimum Saving: Sale to Charity at Undervalue

An optimum saving is achieved if the donor sells to the charity for such a price as will involve him realising no gain and no loss for capital gains tax purposes. In the case of a higher rate taxpayer who has utilised his annual capital gains tax exemption and has sufficient income to utilise the QIDR relief, total relief will be at a rate of up to 80% of the value of the gift.

There will be no stamp duty or stamp duty reserve tax on a sale to the charity. The charity will have to consider whether it is proper for it to buy the assets at the suggested price.

There may be a question as to whether the assets are authorised investments.

If the charity acquires:

(a) shares in an open-ended investment company or

(b) an interest in an offshore fund

they will not constitute "qualifying investments" for the purposes of the qualifying expenditure rules unless, on a claim, the Board of Inland Revenue is satisfied that the investment was made for the benefit of the charity and not for the avoidance of tax (whether by the charity or any other person): para 9 Sch 20 TA 1988.

The general rule is that a charity's tax relief (in respect of income or capital gains) in any year is reduced by the smaller of:

(a) the shortfall of qualifying expenditure of that year (relevant income less qualifying expenditure); and

(b) the non-qualifying expenditure of that year.

Whose Benefit?

In the case of Gift Aid, 22% of the tax saving enures for the benefit of the charity and only up to 18% for the donor, whereas in the case of QIDR the whole of the saving of up to 80% enures for the benefit of the donor. So it is important the charity impress on the donor the true size of the gift he is making, both in terms of the real cost to him and of the benefit which will be conferred on the charity.

QIDR Reversing Old Restrictions on Income Tax Relief for Gift of Property to Charity

It was desired to restrict gift aid relief to gifts of cash, and to deny income tax relief for gifts of other assets. Without a specific anti-avoidance provision, a donor could easily obtain that relief. He would simply give money to the charity, which the charity then used to purchase the asset from the donor.[9] In this way, what is effectively a gift of an asset could qualify for income tax relief.

Statute therefore provides that gift aid relief does not apply if the gift is:

> "conditional on or associated with, or part of an arrangement involving, the acquisition of property by the charity, otherwise than by way of gift, from the donor or a person connected to him".

Section 25(2)(f), FA 1990.

This anti-avoidance provision did not entirely succeed in its aim. There were still various ways to obtain income tax relief on the gift of an asset to charity.[10]

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9 The sale would not give rise to capital gains tax if the sale price did not exceed the donor's base cost.

10 Suppose, for instance, that a donor wishes to give a picture to charity, but would like to qualify for income tax relief. The donor would sell the picture to the charity, and put the charity in funds in order to pay for the purchase in a manner which qualifies for tax relief. One method of doing this without infringing s.25(2)(f) is to arrange for the purchase to be made by a charity other than the charity to whom the gift is made; in principle, an inter-charity loan or grant should achieve this. Alternatively the purchase may be made by a related non-charitable body. Great care would need to be taken to avoid *Furniss v Dawson* because this would be tax avoidance, contrary to the "evident intention" of Parliament.

The new QIDR relief has no comparable restriction. So in this type of situation it should be more straightforward to obtain income tax relief for what is effectively a gift of assets which are not Qualifying Investments.

QIDR Reversing *St Dunstan v Major*

Suppose a person ("the beneficiary") has recently received a legacy or bequest under a will or intestacy. Such a person could in some limited circumstances make a gift to charity by means of a deed of variation which qualifies for both Gift Aid relief for the individual and inheritance tax relief for the estate.

The tax savings here are very substantial. The testator's estate receives Inheritance Tax relief at 40%; the charity reclaims income tax and the individual donor obtains income tax relief at the higher rate on the grossed up amount.

Great care is needed in the execution of these arrangements in particular to ensure that the gift takes the form of the payment of a sum of money.

The Revenue take the objection that Gift Aid relief may be lost because of s.25(2)(e) FA 1990. This provides that there is no relief if the donor receives a benefit in consequence of making the gift. It is said that the donor does receive a benefit, namely, the IHT relief under s.142 IHTA 1984. This was accepted by the Special Commissioners in *St Dunstan v Major* [1997] SCD 212, and should be assumed for practical purposes to represent the law until reviewed by a higher court, though some arguments could be raised if the matter ever came to the High Court.[11]

Where the donor is not (and is not connected[12] with) the residuary beneficiary under the will, no problem arises but that is a rare case. In other cases a possible solution before the FA 2000 was for the donor to ensure that the IHT benefit passes to charity or to a person connected to him, but this was not often done.

Now there is an easier course, to use Qualifying Investment Donation relief. This relief is restricted but not lost if the donor receives benefits. So called "double dip" arrangements, which were very popular before the *St. Dunstan* decision have therefore become viable again.

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11 See [1998] Charity Law & Planning Review, Vol 5, 143 (Robert Venables, QC).

12 Defined s.839 ICTA 1988: see FA 1990 s.25(11).

Example

T inherits an estate of £1m from a parent and wishes to give £100,000 to charity.

Route (1) Deed of Variation.
The IHT saving for the estate is £40,000.

Route (2) QIDR gift.
The income tax saving is (say) £40,000.[13]

Route (3) Deed of Variation and QIDR relief.
The IHT saving is £40,000. The income tax relief is:

Value of gift	£100,000
Less Benefit[14]	£ 40,000
	£ 60,000

The income tax saving may therefore amount to £24,000, sufficient to justify the work involved. If the assets give rise to potential chargeable gains, the tax saving may be much greater than this.

This puts the parties in a similar position as if the testator had made a QIDR gift to charity before his death, and should therefore be regarded as acceptable tax mitigation rather than unacceptable (to the Revenue) tax avoidance. But care must, of course, be taken to ensure that all the technical conditions for the tax reliefs are satisfied.

13 Assuming T has income taxable at the 40% rate. If his income is taxable at the Schedule F upper rate, for instance, the saving is less.

14 IHT saving, applying principle of *St. Dunstans v Major*.