

Mixed Sponsorship and Donation Income: An Update to VAT Guidance

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HMRC has updated its guidance, "How VAT affects charities", to recommend how a charity can distinguish between funds that are a mix of sponsorship and donations if the money is received as a mixed payment in relation to VAT.

This is a key issue to consider for any charity being sponsored by or entering into a 'partnership' arrangement with a business, and the update from HMRC is a helpful refresher on how to properly protect your charity's position.

VAT Treatment of Donations and Sponsorship Income

Donations to charities, including by a business, are usually outside the scope of VAT as long as the donation is made freely and without the donor receiving anything in return.

By way of contrast 'sponsorship income' is generated when a charity receives money, goods or services from sponsors, such as retailers or other large corporate organisations, as part of a reciprocal arrangement where the sponsor also receives a direct benefit from the relationship.

If the charity is obliged to provide the sponsor with a significant benefit in return for sponsorship, then the trading income received as a result is taxable at the standard rate as it will be considered a business activity. What is 'significant' is a matter of degree – however the HMRC guidance notes that a significant benefit would not include, for example, giving out flags or stickers to a donor or naming a donor in a list of supporters.

The key risk is that if donation money cannot be clearly distinguished from sponsorship income it will become taxable and the charity will be liable to VAT on the entire amount. As a charity would, typically, only provide a benefit to further its purposes or, otherwise, in return for a like benefit of fair value, HMRC will treat the donation as the payment in return unless there is a separate fee accounting for the benefit provided.

We note that many instances of 'sponsorship' understood in this sense involve a form of promotional benefit, which may include a licence of the charity's branding for marketing purposes. The charity providing a significant benefit, such as a licence of trademarks, must also be alive to the risk of the income received in return constituting 'taxable trading' which, if it does not fall within certain exemptions, can create an additional corporation tax charge.

For this reason many charities used wholly owned 'trading subsidiaries' to provide benefits in return for sponsorship income – to ensure any potential tax liability is ring-fenced in an entity separate from the charity itself.

VAT Treatment of Mixed Sponsorship and Donations

If a charity receives sponsorship income and donations at the same time from the same partner, the money that consists of a donation will only fall outside the scope of VAT if it is entirely separate from the sponsorship income or the sponsorship agreement makes it clear what money is payment for services and what is a donation.

It is important to be clear that any benefit the charity is giving to the sponsor is not conditional on the sponsor making the donation to the charity.

To achieve an accurate and helpful 'split' the HMRC's updated guidance suggests that it is good practice for a charity to enter into two separate agreements with corporate sponsors.

For example, one agreement would be between the charity's trading subsidiary and the sponsor and provides for the charity to grant publicity and any other rights to the sponsor. The second agreement would be between the main charity and the sponsor for the sponsor to make a donation to the charity.

However the crucial reminder is for your charity to agree and document the terms of any partnership, whether in one document or several, to ensure all arrangements are in its best interests and the tax position has been considered upfront.

If you have any questions on managing a partnership with a business or how VAT applies to your charity, please get in touch with a member of the Charity team.

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