Business Rates Relief and Trading Subsidiaries

Introduction
Charity shops have always benefitted from tax concessions in the UK under tax law. This is primarily because all funds raised by a charity shop go to fund the work of the charity, which provides a clear public benefit.

One of the most crucial of these benefits has been a mandatory 80 per cent relief in business rates for charity shops. This must be applied for through the relevant local authority.

There are two key factors which a local authority will use when determining whether a property should receive mandatory relief – who owns (or leases) the property and what the property is used for.

Although many local authorities are flexible in the way they operate this relief, it has occasionally been the case that this relief has been refused in the case of shops run through a trading subsidiary. This brief is intended to clarify the legal situation regarding mandatory rate relief for CRA members.

The Law
Many charities prefer to operate through a trading subsidiary (read our pros and cons guide here). Trading subsidiaries are seen by many charities as an efficient means of ring-fencing and managing risk and for carrying out taxable trading by tax-efficient means.

Likewise, charity trustees are not always retail experts and many prefer to delegate this responsibility to a suitably skilled board of directors on the subsidiary.

The system of rate reliefs was established through the Local Government Finance Act 1988. Guidance relating to this Act from the Office of the Deputy Prime Minister (read here) and the Charity Finance Group (read here) make it clear that to qualify for rates relief, a charity shop must fulfil the following conditions:
1) It must be wholly or mainly used for the sale of goods donated to a charity
2) The proceeds of sale of the goods (after any deduction of expenses) must be applied for the purpose of a charity

The Act makes no allowance for a subsidiary to be the ratepayer and does not consider a trading subsidiary to be a charity. Specifically, it states that the ratepayer must be “a charity or trustees for a charity” (s.43(6)).

Therefore, local authorities may be within their rights to deny this relief in such circumstances.

Understanding the problem
If your local authority takes a strict position on this, there is unfortunately no quick fix which charities can quickly adopt and thereafter be able to run their shops through a subsidiary and still get at least 80 per cent relief.

However, advice has been offered by various organisations in the sector. The Charity Finance Group report states: “Some advisors believe that [the law] allows the sale of donated goods to be taken through the subsidiary and that the shops should be run through the subsidiary but it should be noted that the goods must be donated to a charity – in which case the proceeds should be recognised by the charity.”

In response to this theory, we know that some charities adopt a structure whereby the charity owns or leases the shop and is therefore the ratepayer entitled to relief. The charity accounts for income and related expenditure on the sale of donated goods and the subsidiary accounts for income and costs on bought-in goods.

Hospice UK outline this process in more detail in their report Charity shops - interaction with rates relief (read more here), but to summarise:

- the charity owns or leases the property
- the charity then grants the trading subsidiary a licence to use the premises, at a commercial rate (the licence must not grant the subsidiary exclusive possession of security of tenure)
- the charity uses the property as well, perhaps by sorting a variety of donated goods or promoting its cause on the premises
- the charity keeps all responsibilities for the lease, including for issues such as insurance and health and safety

It is worth noting that the ring fencing of risk cannot be achieved when the charity maintains all responsibilities for the property under the lease.
Conclusion

The advantages and disadvantages of the potential work-around to maintain a subsidiary mean that each charity will have to come to their own conclusions about what will work best in their circumstances, and remember that the money saved though business rates relief is not the only factor to consider.

Given the complexity of these arrangements we would therefore strongly advise any member to seek independent legal advice before making any changes to their structure, and also to consult with the local authority in question to clarify that such changes will be acceptable to them.