Charitable Remainder Gift: Transforming Charitable Giving

Presentation Charity Tax Forum

and

Submitted to HM Treasury Budget Representation

1.0 Introduction

The Charitable Remainder Gift coalition, led by Philanthropy Impact, is pleased to make this presentation to the Charity Tax Forum and a submission to HM Treasury.

We believe there are critical questions that should be addressed regarding:

i) How the existing taxation rules could be **simplified** to make them more accessible to individuals and their advisers.

ii) How we can encourage greater **innovation** around the existing reliefs to create new opportunities for individuals and their advisers to engage in philanthropic giving and social investment.

With reference to the latter we would like to discuss Charitable Remainder Gift. However, first described below are a series of taxation principles designed to encourage greater philanthropic giving and social investment.

2.0 Taxation principles: encouraging private assets to be used for public good

Underpinning our approach are the following principles.

2.1 Role of wealth in civil society

Since the financial crisis of 2008/2009 and the aftermath of austerity, the roles played by government, individuals and charities in civil society have been rebalancing. In the age of austerity, evidence suggests that the role of the charity sector is growing as the state rolls back in certain areas. At the same time, there is little evidence that wealthy individuals are stepping forward and stepping up the levels of personal giving.

According to Charity Commission data there were 168,354[1] charities in 2008 with annual gross income of £48.4 billion. In 2009, the number of charities fell by 5%, but has been climbing ever since. In 2017, there were 168,237 charities in the UK with annual gross income of £75.4 billion, 56%

[1] https://www.gov.uk/government/publications/charity-register-statistics/charity-register-statistics-for-previous-years-charity-commission

higher than a decade ago. These data suggest that the demands on charitable organisations are as great as they have ever been, and growing.

Yet, over the same period, giving by individuals has stagnated. The UK Giving Report by the Charities Aid Foundation (CAF) in 2008 showed giving by individuals in the year 2007/2008 at £10.6 billion[2]. In 2017, it was £10.3 billion[3].

Further research conducted by Scorpio Partnership indicates that among the UK's millionaire population, the median annual amount given is just £240-£500. In fact, only 5% of the UK's 400,000 millionaires give at a level that could be considered generous[4].

Data from CAF show that overall the UK is a generous nation, ranking 11th [5] globally in terms of charitable behaviour. Yet, of the £10.3 billion given last year in the UK, we estimate that less than £2 billion[6] of that total was made up of regular annual donations made by wealthy individuals in the UK (defined as individuals with liquid assets of more than £1 million).

A further £3 billion[7] was given by just 150 individuals in major gifts; however, individuals rarely have wealth levels that can sustain seven-figure gifts on an ongoing basis.

Taken together, these data show that we have a problem with our culture of giving in the UK. Put simply, wealthy people are not engaged in contributing to civil society at a significant level.

This problem is especially troubling at a time when wealth inequality in the UK remains stubbornly high[8] and our social sector faces mounting pressures.

As with all cultural and societal problems, there is no single cause for the lack of engagement in civil society by wealthy individuals in the UK. The rise of the welfare state in the 20th century, taxation policies, the decline of religious participation and the culture of fundraising in the third sector have all been blamed – as have a myriad of other reasons.

It is this combination of factors that has left us with a complex behavioural problem among the wealthy in the UK. Like all such challenges, there will be no single intervention that will change behaviour. Rather, it will require a sustained effort across many institutions in the private, public and third sectors to re-engage our wealthy citizens in civil society.

2.2 Tax reliefs are an invitation for individuals to participate in civil society

If we start from the premise that civil society flourishes when it is recognised as the shared responsibility of government, individuals and charitable organisations, then the purpose of charitable tax reliefs becomes clear: they are an invitation by government to individuals to step forward as partners in this shared civic duty.

---

[2] https://www.cafonline.org/docs/default-source/about-us-publications/ukgiving2008.pdf?sfvrsn=d415f440_4
[3] https://www.cafonline.org/docs/default-source/about-us-publications/caf-uk-giving-2018-report.pdf
[4] Philanthropy Collaborative, based on high-net-worthy survey data provided by Scorpio Partnership
[5] https://www.cafonline.org/docs/default-source/about-us-publications/cafworldgivingindex2017_2167a_web_210917.pdf?sfvrsn=ed1dac40_10
[6] Philanthropy Collaborative, based on high-net-worthy survey data provided by Scorpio Partnership
[7] https://www.civilsociety.co.uk/news/rich-gave-away-over-3-2bn-in-last-12-months-according-to-sunday-times-giving-list.html and https://www.cafonline.org/docs/default-source/personal-giving/the-sunday-times-giving-list-2017.pdf
[8] https://www.equalitytrust.org.uk/how-has-inequality-changed

Indeed, if government genuinely wants to promote "a shared society"[9], then tax reliefs must be regarded as a cornerstone in the strategy to engage all responsible citizens to give to the charities, institutions and organisations that underpin our civil society.

2.3 Tax reliefs are an important mechanism to encourage individual giving

By one measure, tax reliefs are working well to achieve this goal. Reliefs for individuals are currently worth £1.47 billion, which is equivalent to approximately 14% of the amount given to charity last year. In other words, an investment of £1.47 billion by the exchequer is a factor influencing the estimated £10.3 billion of private capital that was estimated to have been given by individuals last year, but clearly more can be done.

In order to increase that amount, it is important to note that there are many reasons that levels of personal giving have flatlined over the last decade. If we want to change the culture in the UK so that it becomes normal for individuals to give in a significant way for the public good, then we need to accept that multiple, interconnected actions will need to happen to influence the behaviours, beliefs and values that underpin our social norms.

No single mechanism, such as the tax system, in isolation will turn that trend around. But, that is not to say that tax reliefs are unimportant.

While individuals rarely give because of tax reliefs, when they do, it is important to them that they are giving as effectively and efficiently as possible. Tax reliefs therefore act as an encouragement for individuals who have made the choice to give. They also serve as a reminder to those who do not yet give at a significant level of the important contribution private wealth can make to civil society.

Tax reliefs are therefore an important lever in the context of our giving culture. To roll them back will undermine those who are already giving and send a signal to others that Government does not value the contribution of private individuals to our civil society.

2.4 Individuals should never be taxed on money they give away

Linked to this, there is another important principle at stake: whether an individual should ever be taxed on money they give away.

If one accepts that civil society is a shared responsibility between Government and citizens, then individuals should be able to contribute from their own private purse as Government does from the exchequer. Guided by public policy, Government can set the priorities for funding within our civil society and regulate accordingly. Within this framework, private giving can then act as a form of complementary capital: funding before, alongside or around our civil society priorities.

Thus, when individuals take up the invitation to deploy some of their wealth to support charitable causes, the transaction represents an act of citizenship undertaken by the individual and the charitable organisations they support. Government may have encouraged the transaction through tax reliefs; it may have even guided it through various mechanisms, but it is not a party to it.

[9] https://www.gov.uk/government/speeches/the-shared-society-article-by-theresa-may In her article to the nation in January 2017[9], the Prime Minister described her vision of a shared society: where our social values will focus "rather more on the responsibilities we have to one another; a society that respects the bonds of family, community, citizenship and strong institutions that we share as a union of people and nations; a society with a commitment to fairness at its heart."

In other words, the full gross value of the transaction should balance between the two transacting parties: the individual and the charity.

The gain to Government, where individuals use charitable tax reliefs, is a thriving civil society. Charitable tax reliefs therefore do not represent a “loss” to Government, but rather a gain to society.

2.5 Private philanthropic capital can invest in ways that the public and private sectors cannot or will not

Indeed, it is important to recognise that the unconstrained nature of charitable giving represents a form of capital that is not freely to be found in either the public or private sectors.

Where the Exchequer must be cautious with public funds, the private donor can test new ideas. Where the Exchequer must seek economies of scale, the private donor can support the specialist and the niche. And, where the private sector must maximise financial value, the philanthropist can champion social value.

Thus, money that is given by individuals, with no expectation of financial return, offers the opportunity to the charitable sector to be bold: to pilot new solutions to old or emerging social problems, or to fund important work that might never be commercialised or taken to scale.

Imagine if someone with a rare medical condition were unable to access respite care simply because their condition is not shared by many; or they were denied the hope of a future cure because research into the condition is considered economically non-viable.

Some have called private philanthropy the risk capital of society (as demonstrated in start-up support for social enterprises). However, it is more than that; it is the oxygen that allows our civil society to thrive.

2.6 Tax reliefs targeting wealthy individuals can unlock significant private capital for civil society

So, if the purpose of charitable tax reliefs is to stimulate engagement in civil society by individuals, there are two important secondary questions: who to prioritise when targeting reliefs and how to maximise the likelihood of these individuals giving more.

When considering who to target with tax reliefs, emerging evidence clearly suggests that more could be done to encourage those who have the most capital to give: the UK’s high-net-worth population.

Supporting regular, lifetime giving among the wealthy represents the best opportunity for significantly strengthening our nation’s civil institutions.

When considering how much additional capital might be generated by tax incentives for the UK’s wealthy population, the £2 billion of regular annual giving by wealthy individuals needs to be set in the context of the total £1.7 trillion[10] of liquid assets controlled by UK millionaires (the top 0.85% of the population). That is equivalent to 20% [11] of the liquid wealth held by households in Britain today.

[10] Philanthropy Collaborative, based on high-net-worth survey data provided by Scorpio Partnership
[11] https://www.ons.gov.uk/peoplepopulationandcommunity/personalandhouseholdfinances/incomeandwealth/bulletins/wealthingreatbritainwave5/2014to2016#total-wealth

Yet, the average amount given in total by the wealthiest individuals in the UK annually is currently just 0.18% of the liquid wealth they control – and this figure is inflated significantly by the generosity of a few.

Tax reliefs targeted at the top 1% would therefore seem likely to present the strongest opportunity for encouraging greater giving among individuals in the UK, and a target to double the amount of giving from this group should not be inconceivable.

2.7 Innovative tax effective giving structures can harness the professional advisory sector

Current tax reliefs already provide a good framework for encouraging greater giving by wealthy individuals, but there is significant potential for much greater innovation particularly in the form of tax effective giving schemes (such as Charitable Remainder Gift, the Cultural Gift Scheme, Pension-Release Schemes and Hybrid-Endowments).

Indeed, tax reliefs could be used in many different ways to unlock assets for the public good. Such innovation is important because it presents a vital opportunity to engage individuals in civil society – through their wealth advisers.

Currently, fewer than 20% [12] of wealth advisers raise the subject of philanthropic giving with their private clients; yet they are almost always the first port of call for individuals when considering major investments or transactions. The UK's 16,000 advisory firms therefore represent a critical nexus to extend the invitation from government to those individuals who can most afford to give.

The paucity of tax effective giving schemes is a major factor in the low incidence of philanthropy advice offered by professional advisory firms – hindering the commercialisation of the offering and the training of frontline teams.

2.8 Tax reliefs and tax effective giving schemes should engage living donors

Specifically, if tax efficient giving schemes could be developed to support clients at all stages of their wealth journey – through wealth accumulation and decumulation – it would enable professional advisers to talk to their clients about charitable giving as part of their normal practice.

This would increase the frequency of these interactions with clients, thereby helping to normalise charitable giving as an aspect of wealth and wealth management.

Equally importantly, such mechanisms create the opportunity to engage individuals in giving throughout their lifetimes. While donor engagement is a relatively new field of research, American insight suggests fully-engaged donors double [13] their commitment to the organisations they support.

The UK is considerably less developed than the US in terms of philanthropic giving, yet the irrefutable fact is that only living donors can increase their commitment to charitable causes. Therefore, it should be a core principle that tax reliefs and tax effective giving schemes should engage living donors through every stage of life, through mechanisms such as Charitable Remainder Gift. This engagement leads to a habit of giving which translates into greater legacies on death.

[12] http://www.philanthropy-impact.org/article/learning-give-lessons-advisers-and-would-be-philanthropists
[13] http://news.gallup.com/businessjournal/192689/charitable-giving-donors-focus-one-two-organizations.aspx

2.9 Simplification, consultation and innovation will promote the effective and proper use of tax reliefs

Complexity in tax reliefs can lead to artificial schemes and abuse, which damage the credibility of the sector and the philanthropists that properly claim tax relief as intended by Parliament. The fact that Gift Aid and marginal tax relief is not fully utilised or artificial avoidance schemes are constructed may be, in part, because of the complexity of the system. Ways to simplify the scheme need to be examined and clear explanations of how major donors and recipient organisations can benefit from reliefs disseminated.

On occasions commentators, journalists and politicians have erroneously conflated the use of charitable tax reliefs with tax avoidance or evasion. This alienates philanthropists and casts them as social villains. Tax relief on charitable donations is not tax avoidance. To obtain tax relief an individual has to gives 2.5 times the amount of tax that would otherwise have been paid (at a marginal tax rate of 40%) so no donor should ever benefit financially from giving money to charity. If the giver does gain significant financial benefit it is the regulatory regime which should ensure that charitable gifts can only be used for charitable purposes that is failing.

3.0 Charitable Remainder Gift

3.1 A summary overview

Proposals to introduce Charitable Remainder Gift to the UK have been under discussion for a number of years. Recently, the proposal has gained considerable support from the professional services industry. More than 60 delegates gathered at the Royal Society of Arts in London on 1 November 2017 to discuss and explore this topic. Many of the delegates represented a number of professional organisations, including law firms, banks, and other professional advisers, philanthropists, as well as charities, both large and small.

Speakers emphasised the popularity and success of Charitable Remainder Trusts ('CRTs') in the United States, which is the vehicle used for Charitable Remainder Gift. They highlighted that the scheme creates a more dynamic relationship between donors and charities.

When making a Charitable Remainder Gift the donor makes an irrevocable commitment to give to charity. The sum is put into a suitable vehicle from which the donor receives an income during their lifetime. This income is subject to Income Tax. However, the initial investment is deemed to be a gift to charity for the purposes of Capital Gains Tax and Inheritance Tax. The donor also benefits from a one-off calculation of Income Tax relief for backward or forward offset. The benefits for charities are that it creates supporter engagement with a living person and the charity is guaranteed future income which is not the case with a legacy pledge made in a Will. The donor benefits as he or she has financial security for life whilst having made a gift to charity.

3.2 Charitable Remainder Gift – the benefits

By introducing Charitable Remainder Gift, we estimate that there is a possibility of an extra £400 million in assets and income that could be generated every year for charities.

This is experience borne out in the US where they have had a system of Charitable Remainder Gift in place for over 40 years - charities in the US benefit annually from $7bn ($4.5bn in assets and $2.5bn in income).

Potential Income from Charitable Remainder Gift in 2018

Total target group in UK (UK higher rate and additional rate tax payers)	4.7 million[14]
Average trust value (a quarter of US average trust value)	£145,000
Total number of Charitable Remainder Gift by 2020 (0.1 % anticipated take up)	3,340
Total trust value by 2020	£484 million
Total asset value from new donors by 2020 (80% of donations from new donors as opposed to those who would have already given in their will)	£387 million
Total increase to charity by 2020 (in both income and assets)	£398 million

Research suggests that an individual's concern for their financial security, particularly later in life, discourages many from giving more in their lifetime. If, however, an individual had the option to make a substantial tax-effective gift in their lifetime, and this individual was to receive a regular, but modest, income from this gift for the remainder of their life, then estimates show that they would give significantly more to charity. Note, Charitable Remainder Gift are distinct from legacies and it is expect that this approach will not dilute these gifts.

Boosting the money available to charities through a Charitable Remainder Gift provides them with a guaranteed gift of significant value and a secure basis for future planning. This means that they can plan and invest with more accuracy securing their long-term stability and future. With regular giving having declined, this is of increased importance.

There is also greater certainty for the charities because legacies in Wills can be revoked, whereas Charitable Remainder Gift cannot. It also avoids the chances of disputes arising.

It will also improve the relationship between donors and charities, putting it on a longer-term footing.

For the donors themselves and their families, a Charitable Remainder Gift provides the pleasure of making a substantial gift in their lifetime and connecting with the organisation they have chosen to support. On death, a Charitable Remainder Gift is treated like any other gift made to charity in a will and its value is not counted as part of the donor's estate for inheritance tax purposes.

3.3 Charitable Remainder Gift – the proposed model

Our suggestion is that the government adopts the best aspects of the US Charitable Remainder Trust' mechanism, whilst ensuring that it is simple, secure and easy to access without the need to employ

[14] In 2018-19, an estimated 4.3 million individuals (13.8%) are HR taxpayers and 393 thousand (1.3%) are AR taxpayers
https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/710866/Income_Tax_Liabilities_Statistics_May_2018.pdf

professional advice for the donor. Our proposed model is also inexpensive to administer, contains a clear benefit for the charity and allows the government to regulate it simply, to prevent abuse.

To meet these objectives the following model is proposed:

- The donor gives a sum of cash, marketable securities or land to a trustee using a standard trust who must be a charitable donor-advised fund (DAF) or an equivalent organisation which is accepted by the relevant independent charity regulator (e.g. the Charity Commission) to administer Charitable Remainder Gift.
- The donor and the trustee agree the annuity rate within an approved range, the term and the charity beneficiary.
- The DAF's (or an equivalent organisation) auditors include a separate report on Charitable Remainder Gift in standard form within their annual report filed with the relevant independent charity regulator.
- Each year (or more frequently) the DAF (or the equivalent organisation) pays the donor the agreed annuity amount, on which the donor pays income tax.
- At the end of the term or on the donor's death the designated charity receives the Living Legacy from the DAF (or the equivalent organisation).
- The donor may specify if the fund is for the charity's general purposes or specific purposes (that is, unrestricted or restricted capital).
- In the first instance, cash only will be used but it is envisaged that all assets that are at any stage eligible for Income Tax reliefs on gifts for charity such as quoted shares and land will become eligible for Charitable Remainder Gift.

3.4 Charitable Remainder Gift – the tax implications

- The gift into the trust would be treated as a gift to charity for the purposes of Capital Gains Tax and Inheritance tax.
- The present value of the charity's future receipt (based on standard actuarial calculation) is used to calculate the donor's income tax relief on making the gift. In essence, that value is deductible, against the donor's income before calculating his or her tax liability, just as the value of quoted shares would be if they were given outright to the charity.
- Deductibility can be applied backwards for one year, and can be applied forwards.
- The donor is liable for income tax on income he or she receives from the trust.
- The charity receives the fund on the donor's death or at the termination of the trust (free of tax).

Over time, the government could consider the level of tax relief provided. For example, in the US no restrictions are placed on the type of property that can be put into a Living Legacy. So there are future adjustments that can be made which will also ensure that Charitable Remainder Gift are seen an option for greater numbers of the mass affluent and (U)HNWI.

3.5 Overall

Charitable Remainder Gift offers the prospect of expanding the donor base of charities and transforming the culture of giving in the UK at a time when a boost is needed.

At the fore-mentioned conference the then Chair of the Charity Commission expressed his support in principle of Charitable Remainder Gift.

As the *Giving USA 2017: The Annual Report on Philanthropy for the Year 2016* shows, charitable giving continues to rise to new heights and Charitable Remainder Gift play an important role in this success. They stimulate new giving rather than replacing traditional giving. Charitable Remainder Gift, in effect, add to the 'basket of giving incentives'.

The establishment of Charitable Remainder Gift can mark a sea-change in the way that giving is viewed – from often being a 'gift' on death to a thriving and valued lifetime relationship with a charity.

In summary the introduction of charitable remainder trusts to the UK by statute should result in the biggest step change to charitable giving yet to be witnessed because evidence, based on the US experience, suggests that it will unlock substantial resources unharvested by the existing reliefs such as gift aid on cash gifts and income tax reliefs on gifts of quoted securities and land. The remarkable aspect of such a change is that it would require a relatively small statutory provision in the form of clauses in a Finance Act, extending the existing quoted securities and land reliefs but modifying them to ensure that the value of the donor's reservation of benefit would be discounted against the open market value of the asset gifted when calculating their income tax relief.

4.0 About Philanthropy Impact

Philanthropy Impact (www.philanthropy-impact.org) is a charitable organisation whose mission is to increase philanthropic giving and social investment – more and better giving. We work with professional advisers to (U)HNWI to grow and enhance the quality of the support they give to their clients, the UK's wealthiest individuals, around philanthropy and social investment.

We are a membership organisation for private client advisers, wealth management, private banking, independent financial advice, tax and legal sectors; as well as individual philanthropists and social investors, trusts and foundations, and charities.

We act as a knowledge hub and centre of excellence offering events, specialist knowledge sharing, training, voluntary standards and sector and government liaison.

We represent over 200 members, including professional services firms and individual members, and we have outreach to and multiple contacts with a further 9,100 individuals and 3,584 organisations.