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DOCUMENT

Title: **CASC – Setting up a Trading Subsidiary**

The NGCAA has put together a package for clubs to assist them in setting up a trading subsidiary so they can continue to comply with the CASC regulations in place.

Revision: 1

Date: 24 July 2015

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VAT No: 598 3758 66 | Company Number: 8904597 Registered in England

CASC – Trading through a wholly owned company

If a club or company is a CASC (or intends to be) and may be foreseeably at risk of exceeding the £100k p.a. income threshold (thus putting its CASC status or eligibility at risk) consideration should be given to generating trading income and/or property income in a separate wholly owned trading company.

The Finance Act 2014 includes provisions extending corporate gift aid to donations made by companies to CASCs – allowing them to claim corporation tax relief on qualifying donations they make after 1 April 2014. This enables a company to donate its distributable profits to the parent CASC in the same way as charities are able to do.(*See NGCAA Guidance Note – Monitoring Compliance with CASC Regulations and accounting procedures).*

For a golf club which is (or intends to become) registered as a CASC the establishment of a trading subsidiary, in the case of an incorporated club, or of a company which is wholly owned by trustees for an unincorporated club beneficially, is straightforward and the NGCAA legal team has developed a package which members can access either to facilitate this for themselves or, on a bespoke basis, to achieve it for them.

The steps to be taken, once the Club management committee or board has decided upon this course, broadly involves the following:

1. Incorporation of a new private company – limited by shares; with
2. Articles of association appropriate for a wholly owned and controlled entity; and
3. Directors nominated by the club; whose
4. Shares will be issued to and registered either in the name of the Club (if itself incorporated) or trustees for the Club if not; and
5. An agreement entered into between the Club and the new company providing for the provision of or access to facilities, equipment and/or premises in exchange for the commitment to donate all distributable profits to the Club.
6.

Before deciding to proceed on this basis however, Clubs are advised to seek advice from their accountants as to the adequacy of their accounting and point of sale systems to be able to keep a discreet record of transactions which will comprise the trading which must be accounted for in and by the new company – such that they would withstand audit and scrutiny in the event of any challenge by HMRC. (S*ee NGCAA Guidance Note – Operating a CASC trading subsidiary – accounting and administration).*

If members are willing to take the above steps for themselves, following the guidance and draft documentation which can be provided by the NGCAA legal team, the cost of the package will be £500 plus VAT including the cost of the new company incorporation fees and Companies House charges.

If members wish to instruct the legal team to deal with the above steps on their behalf then the cost will be a minimum of £850 (plus VAT and incorporation costs – and assuming the NGCAA standard documentation is adopted without alteration), but could be more dependent upon any additional work or assistance the Club requests.

For further information please send your details to info@ngcaa.co.uk and you will then be put in touch with a member of the legal team to discuss your requirements.

Monitoring compliance with CASC regulations and accounting procedures

A golf club qualifying to be registered with HM Revenue and Customs as a Community Amateur Sports Club (CASC) enjoys potentially valuable tax benefits and also business rates relief.

The tax benefits are in summary….

- Exemption from Corporation Tax on trading profits arising from turnover of up to £50,000 from trading with non-members and £30,000 property income
- Exemption from Corporation tax on interest (with no limit)
- Exemption from Corporation Tax on chargeable gains
- Reclaiming basic rate tax on donations from individuals
- Donations from companies can are encouraged by the donor company being able to claim relief from corporation tax on its donation
- Donations from individuals as lifetime gifts and bequests are encouraged by Inheritance Tax exemption

The consequences of becoming a CASC but subsequently failing to meet the conditions for registration are potentially very serious. HMRC may remove a club from the register of CASCs if the club has not complied with the conditions of registration.

The effect of this is a deemed disposal of the clubs property at market value which can lead to a large capital gains tax liability if for example the club owns land with significant value.

A club that is registered as a CASC therefore needs to monitor compliance with all the conditions of registration. Monitoring compliance with certain conditions of registration requires accounting records and systems which will provide the relevant figures and an understanding of the way income needs to be analysed and recorded.

The main financial restriction in the CASC legislation is the 'income condition' which restricts a club's receipts from trading with non-members and property income to £100,000 per annum.

To monitor compliance with this condition receipts need to be analysed and recorded as either from trading with non-members or non-trading.

Based on their detailed guidance notes HMRC treat all income including bar income from members as non-trading income even though it could be argued that the bar income is trading income. This appears to be a HMRC concession to get around the fact that technically a CASC cannot treat bar income from members as non-taxable on the basis that it is 'mutual trading' income. Bar profits of a members club would not normally be taxable on the basis on being from a 'mutual trade' .A CASC cannot meet the conditions for tax free 'mutual trading' as any trading surplus cannot be returned to the members (a condition of registration as a CASC).

Therefore it is necessary to have a method of recording all forms of income including bar receipts as being from members and from non-members. A modern till can be set up to do this but staff need to be trained to use it and to identify and differentiate sales to members and non-members.

The income figures from members and non-members recorded through the till or any other records of income (invoices, cash books etc.) should be posted into the nominal ledger of the clubs accounting system so cumulative totals in the accounting period can be seen separately.

HMRC are aware of the possibility of the non-member income restrictions being circumvented by clubs granting temporary membership or membership with limited rights to visitors or people who use the club bar as social members. Income can only be treated as non-trading income from members if the member has similar rights to a full member in terms of voting rights, participation in club activities and general control over the club. Short term members or adult members without full voting rights are unlikely to be accepted as members for the purposes of the income condition.

Property income needs to be recorded separately although it makes no difference whether property income comes from members or non-members. Rental of a room with services provided is a potential grey area and the prudent thing to do may be to record as property income counting towards the £30,000 corporation tax exemption limit even when received from a member.

Although it is the £100,000 turnover from trading with non-members plus property income limit that determines if a club is entitled to be registered as a CASC, the club also should monitor the turnover from trading with non-members and property income in relation to the £50,000 corporation tax exemption limit for trading and £30,000 property income corporation tax exemption. This is because exceeding these turnover limits even by a small amount makes all the resulting profit taxable potentially costing the club thousands of pounds in corporation tax.

A possible solution for a club with income which is on course to exceed the £100,000 turnover limit or the income thresholds for corporation tax exempt trading and/or property income is to form a separate company to be owned and controlled by the club to carry on the taxable trading and property business activities (a ‘trading subsidiary).

In this scenario a trading subsidiary would be the entity which contracts with non-members and any persons renting land or buildings and receives the income. In this case the turnover will not count towards turnover in the CASC for the test of whether the £100,000 income condition is breached nor will this turnover count in assessing if the profit exemption limits have been exceeded.

Trading and property income in a trading subsidiary would be in the first instance liable to corporation tax at 20% but to the extent that it is donated to the CASC within the conditions for charitable donations relief, corporation tax relief will be available.

Formation of a subsidiary to carry on trading activities and receive property income followed by donation of all profits to the CASC appears on the face of it to allow unrestricted amounts of profit to be generated without corporation tax. Although this arrangement is one that was contemplated by HMRC and other parties involved in the consultation before the recent changes to legislation and regulations and it is mentioned as a possible course of action in HMRC’s guidance notes, such arrangements will have to be implemented with care. It is possible to foresee that in an extreme situation where for example a company is formed and all that happens is money is routed through the new company bank account HMRC may challenge the arrangements. HMRC are also fearful that an essentially commercial enterprise might try to use a CASC as a way of sheltering profits from tax. There are various ways in which HMRC could seek to deny tax relief in such circumstances. A separate document follows which addresses the accounting and administration of a trading subsidiary.

Operating a CASC trading subsidiary- accounting and administration

Forming a trading subsidiary is a way of avoiding a CASC having to be taken off the register and losing the benefits of CASC status and creating a potential Capital Gains Tax liability, if it is on course to exceed the limit on CASC non-member trading and property income. It also offers the possibility of profits arising from turnover in excess of the CASC exemption limits being sheltered from corporation tax by means of donations from the trading subsidiary to the CASC.

To deliver these benefits the trading subsidiary needs to be properly constituted and administered. It is possible to imagine HMRC challenging a club which simply forms a company, opens a bank account and routes money through the subsidiary bank account. In an extreme case HMRC might argue that the company was a sham and lacked legal substance so all the income should be regarded as that of the CASC. All the usual formalities of forming a company and running a business through it need to be observed.

The first step towards operating a trading subsidiary is incorporation of a company limited by shares. The NGCAA legal team have put together a package of guidance and documentation to assist an unincorporated club or one that is incorporated, to go through this process.

The new trading subsidiary will be a separate legal entity to the CASC. It will need to have a separate bank account and a separate set of accounting records and accounting system. If a club currently uses accounting software such as Sage for a single business a second licence will need to be purchased.

Funds should be kept separate in general. It might be necessary to lend money from the CASC to the trading subsidiary or vice versa but such transactions will need to be recorded in the ledgers of the two legal entities so there are equal and opposite loan account balances recorded in each. The lending of funds needs to be identified separately from donations from the trading subsidiary to the CASC which is the basis for the tax relief the trading subsidiary will claim on its corporation tax return and also payments relating to shared expenses (more of which below).

Whenever and wherever income is generated consideration will need to be given to whether it is from members and non-taxable and whether it is taxable income from non-members. If it is the former generally it should be recorded as a receipt of the CASC and banked in the CASC bank account. If it is the latter it should be recorded in the records of the trading subsidiary and banked in the subsidiary’s bank account.

Cash also needs to be separated. If a single safe is used there should be a means of identifying the amount of cash belonging to the CASC and the trading subsidiary. This might involve a bar cashing up sheet that reconciled brought forward cash, takings and cash expenses of the CASC and trading subsidiary to cash at the end of the period, split into amounts belonging to the CASC and the subsidiary.

Where there is a contract rather than cash changing hands over the bar ,for example when a booking is made for a catered function, correspondence and agreements should be entered into in the name of the trading subsidiary. The company will need its own stationery and invoices.

In the case of bar takings, a club with a bar serving members and non-members may have two legal entities trading in the same location and at the same time. The principal way the sales of the CASC and the trading subsidiary would be differentiated in terms of who makes the sale, is where the money ends up. Separation is reliant on the bar staff identifying if the customer is a member or non-member and dealing with the money appropriately.

One approach to this issue might be to have two tills. If one till is used it would be necessary for that till to be programmed to record the sale as to a member or non-member and for the cash to be split on that basis when cash from the till is banked or put into the safe.

Similarly with credit card sales there would need to be two card machines or a way of analysing the credit cards receipts so a transfer could be made between the bank account into which payment went and the other entities account.

Purchases of bar stock would have to be recharged between the two entities based on the split of turnover and the overall gross profit margin. If a stock taker is used to check bar profit he will have to take account of the records of both entities. A stock taker 's report for the combined bar trading of the CASC and the subsidiary would be helpful in calculating recharges for bar stock.

Splitting bar income is perhaps the most difficult source of income to manage. It may be possible to leave all bar income in the CASC if there are other sources of income and profit which are more straightforward to transfer to the trading subsidiary and this alone would result in the CASC being comfortably below the income limit once this income is removed. For example if a club had £40k bar income from non-members and green fees from visiting non-members of £70k (per annual accounting period) CASC status could be maintained by the visitor green fees being charged and collected by the trading subsidiary without taking any action to split bar takings.

There are however potentially negative VAT implications which could result in green fees for visitors being collected by a VAT registered subsidiary. The fees would be standard rated when charged by the trading company unless the trading subsidiary qualifies as an 'eligible body' ,whereas they are exempt when charged by a non for profit club (following the outcome of the Bridport Golf Club case). The term 'eligible body' is defined in the VAT legislation (the notes to group 10 of schedule 9) and a trading subsidiary may qualify if all its profits are distributed to a non-profit making body and it is free from 'commercial influence'. In view of the possible VAT cost arising from visitor green fees being charged by a trading subsidiary, before a decision were made to charge green fees through the company a calculation of the possible increased VAT costs versus the tax savings from maintaining CASC status would be advisable. A ruling from HMRC could be applied for on the question of whether the subsidiary qualifies as an 'eligible body'.

If visitors green fees were charged by the trading subsidiary it would be appropriate for the subsidiary to pay a share of the costs of course maintenance and management of the course. In circumstances where visitors green fees are within a club with mutual trading income (non-taxable for a club that is not a CASC) the costs to be allocated in calculating the taxable profit would normally be based on the number of rounds played by visitors as a proportion of the number of rounds played by both members and visitors. This is the method suggested in HMRC guidance based on the case of The Carlisle and Siloth Golf Club v Smith.

The procedure for the treatment of invoices for expenses to be shared by the CASC and the trading subsidiary needs careful consideration. Some expenses may be attributable entirely to income of the CASC or the trading subsidiary and in this case the invoice received and the payment should be made out to and come from the entity receiving the income.

If the CASC were to pay an expense which related to income of the trading subsidiary it could result in some of its otherwise tax exempt income being liable to corporation tax because of the rules on 'non-qualifying expenditure' (such payments would be incurred for the trade of the subsidiary rather than directly for the purposes of the CASC). On the other side of this the trading subsidiary would have a profit higher that a commercial organisation would show trading on an arm's length basis (as the CASC would be paying some of its expenses). HMRC could potentially resist the trading company's claim for tax relief on the donation on the basis that the company has received benefits (tax relief on donations to charities being denied where to donor receives associated benefits).

If the Trading subsidiary were to pay an invoice that properly relates to income of the CASC it will not get corporation tax relief for the payment as it would not qualify as wholly and exclusively incurred for the purpose of the trading subsidiary's trade.

The shared expenses need to be split in a reasonably accurate and realistic way to avoid potential loss of tax exemption or relief for the same reasons. If there is a single invoice for an expense that relates to income in both the CASC and the trading subsidiary the question arises who should it be addressed to and who should pay it.

The best approach may be for the trading subsidiary to be invoiced and pay the invoice if it will ultimately bear a significant proportion of the expense. It can then invoice the CASC for the CASC's share of the expense. In this way the trading subsidiary will show the commercial profit on its trading without potentially disallowable expenses of the CASC in its profit and loss account. It will usually not pay tax on the increased profit in any case by making a donation to the CASC.

If the CASC were to be invoiced for and pay all of a shared expense it would have to invoice the trading subsidiary for its share of the expenses if it is not to have 'unallowable expenditure' which would limit the exemption from corporation tax on its income. The payment it would receive having invoiced the trading subsidiary might however be viewed by HMRC as trading income from non-members and counting towards the £100k income limit in the CASC.

If the Trading subsidiary is invoiced for, pays the shared expenses and recharges a proportion to the CASC a further reason for the amount recharged being accurately calculated and charged at actual cost, is the restriction of charitable donations relief for a company making a donation to a CASC where there is 'inflated member-related' expenditure. This is a provision in the legislation which seeks to prevent a trading subsidiary of a CASC reducing its profits and benefiting members of the CASC by paying higher than commercial rate wages or an arm's length price for goods and services.

It may assist in dealing with any enquiries from HMRC if there are written documents giving the trading subsidiary the right to use the CASCs facilities in consideration for covering its share of the expenses calculated by a reasonable method. This would support the argument the trading subsidiary is a separate entity trading in its own right.

There are potential VAT implications of invoices between a CASC and its trading subsidiary. The VAT position can potentially be simplified by registering both entities within a group registration. If there were a VAT group registered there would need to be a partial exemption calculation done for the group as a whole.

Consideration would need to be given to whether staff employed by the CASC should transfer to the CASC. Staff cost should be recharged where they relate to both and there are similar VAT considerations as in the case of other costs recharged between the CASC and the subsidiary if they are not in a VAT group.

The result of setting up and running a trading subsidiary should be an accumulation of profit in the bank account of the trading subsidiary reflecting the profit shown in the company's accounting records. Periodically and certainly around the end of the company's accounting period consideration should be given to the amount to be donated from the trading subsidiary to the CASC. To eliminate any liability to corporation tax in the subsidiary the amount of the donation has to precisely match the profit in the company's accounts. The legislation on company charitable donations(a CASC is a charity for these purposes) takes account of the practical difficulties in matching donations to profit by allowing wholly owned subsidiaries of charities to treat a donation made shortly (up to 9 months) after the end of the corporation tax accounting period as being made before the end of the period of account so it qualifies as a deduction in that period.

There is potentially a limit to the amount of profit that can be generated in a trading subsidiary and sheltered from corporation tax in this way. The limit on the use of this strategy is the requirement that the donation be applied for 'qualifying purposes' by the CASC. That means the donated money has to be used in providing facilities for and promoting community sport. If the level of donations is more than the club needs or can spend in promoting its sport there will be a build-up of funds in the CASC and possible denial of corporation tax relief on the donations received. The accumulation of money in the CASC should not be a problem is it is being saved up for a capital project or other planned expenditure. If there is a build-up of funds budgets and/or a club development plan might be of use in satisfying HMRC that tax is not being avoided.   The CASC can make donations of surplus funds to anther CASC to satisfy the 'applied for a qualifying purpose test'.

A CASC generally only prepares a tax return and submits accounts to HMRC if it is required to do so by HMRC or if it has income not covered by tax exemptions. A trading subsidiary will however have to prepare its accounts in the statutory format and submit them with a tax return in the format required by HMRC (iXBRL) following the end of every accounting period.

A non-tax benefit of carrying on commercial trading activities through a trading subsidiary is the protection that officers and members of the club through limited liability. There are limitations to this protection and in particular directors may be liable to creditors if the company is guilty of wrongful trading. This means carrying on trading when the company cannot pay its debts. If a company has accounting records that show the results of trading and the assets and liabilities of the company the risk of slipping into a position where wrongful trading is potentially in point is reduced.

Summary of accounting and administrative recommendations and requirements

Prepare projections based on budgets to assess the potential overall tax savings and what trading activities to transfer to a trading subsidiary.

Form a company, appoint directors (and shareholders if shares will be held by trustees on behalf of an unincorporated club).

Put in place procedures for the board of directors to manage the company (governed by articles of association –model document can be provided by NGCAA Legal team)

Adopt suitable Articles of Association

Set accounting date to coincide with CASC and inform Companies House and HMRC(HMRC issue Unique Tax Payer reference(UTR) to company and set up tax record expecting to receive a return based on the first period of account).

Register for HMRC online services.

Open trading subsidiary bank account.

Set up separate accounting system and records

Complete VAT registration if turnover in excess of registration and consider Group Registration.

Consider new contracts for staff/transfer CASC contracts to trading subsidiary

Register PAYE scheme.

Put in place procedures for separation of cash balances.

Prepare trading company letterhead and invoices.

Open accounts with suppliers in the name of the trading subsidiary where appropriate.

Agree and document arrangements for trading subsidiaries use of CASC facilities and basis for payments for use and recharges.

Where expenses are shared decide who should pay for the expense (normally this will be the trading subsidiary) and put in place a routine for recharging expenses to the other entity.

Prepare company accounts in statutory format after the end of the accounting period.

Agree and document the amount of the donation from the trading subsidiary to the CASC (all directors meetings should be minuted and written records of resolutions retained).

Prepare and submit corporation tax return.

Pay corporation tax 9 months after the end of the corporation tax accounting period if not all profits donated to CASC.