



EDUCATION BULLETIN

## WHY **EDUCATION INSTITUTIONS** SHOULD MAKE (EVEN MORE) USE OF ASSOCIATED CORPORATE BODIES

It has long been accepted that non-primary purpose trading activities should be carried on by a non-charitable company which is wholly owned by the charitable parent institution.

This avoids tax and other complications which might arise if these activities are carried on by the institution itself.

The profit generated in the "subsidiary" can be gift aided to the parent, thereby reducing or eliminating any tax payable on those profits.

HMRC accept that this is a legitimate form of tax avoidance.

Where the trading subsidiary is wholly owned it has nine months from the end of an accounting period to decide how much it will pay to its parent by way of gift aid. It has time to calculate its otherwise taxable profit and decide how much of it to pay to its parent and whether it needs to retain some for working capital needs.

With the coming into force of the Charities Act 2006 there is increased uncertainty as to whether certain activities, previously carried on within the charitable parent, meet the "public benefit" test.

There was, of course, a presumption that education and training were charitable activities. That is no longer the case and charities have to demonstrate that what they

do is for "the public benefit". So, for example, certain "closed courses" may not satisfy the public benefit test because they are delivered to a limited group of people.

The advice must be that, if in doubt, non-core or potentially non-core activities should be carried on in a wholly owned subsidiary company.

However, there may well be other, longer term, advantages in using companies to carry on trading activities.

There is some pressure, at least in the FE sector, for consolidation by using collaborations between FEC's rather than through mergers.

A limited liability company provides an ideal structure for bringing in other partners and/or attracting external finance.

There will be many cases where a "corporate joint venture" is preferable to contractual or other forms of joint venture.

Companies have great flexibility in the ways that they can be structured to represent the differing interests and contributions of those involved.

It is relatively easy to provide for the bringing in of new partners and the departure of others, depending, of course, on the ongoing needs of the business.





Companies limited by shares are able to raise finance in their own right and there is increasing interest from financiers in investing in the public sector.

So, if you think that parts of your business could benefit from external finance, or from the introduction of other partners, you should consider putting that business in a subsidiary at an early stage.

If, subsequently, you do want to bring in others then you already have the business carried on by a suitable vehicle. You will not need to transfer it out of your institution with all the attendant difficulties, including under TUPE.

Gift aiding part of the profits of a company which is not wholly owned by a charity may still be possible but there are potential

pitfalls. Advice needs to be taken before the point at which a subsidiary ceases to be wholly owned so that it can be structured in a way which maximises gift aiding opportunities.

Another possible vehicle for carrying on business activities, separately from the main education institution, is a limited liability partnership ("LLP").

This is a separate and distinct legal entity, like a company, but it borrows some characteristics from traditional partnerships.

Unlike a company limited by shares, an LLP does not have a share capital and cannot build up a "capital base". This can be a disadvantage in some circumstances.

However, an LLP may be a suitable vehicle for some forms of joint venturing.

An LLP is "tax transparent". This means that it does not pay tax on its profits. They are attributable directly to its members in the proportions agreed by them.

There is therefore no need, or indeed no opportunity, for an LLP to make use of gift aid.

Where one of the members is a charity, it would be normal to interpose a non-charitable company between the LLP and the parent charity. The intermediate company receives the appropriate share of profit and then gift aids it to the charity.

In the case of a non-charitable member, it receives its agreed allocation of profit and pays tax on it in the usual way.

So, there are many advantages in putting non-core activities in either a company or an LLP. Which vehicle to choose will depend upon the nature of these activities and future hopes and aspirations for the business.

Much may depend on whether the venture is a "one off", and for the short term, or whether it is anticipated that, after some growth, a sale to a third party might be contemplated.

**This bulletin contain summaries of complicated issues and should not be relied upon in relation to specific matters. You are advised to take legal advice on particular problems and we will be happy to assist.**

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