Resolution to create a wholly owned subsidiary

Supporting Information

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Summary

Dartmouth Sailing Club (Holdings) Ltd is a Community Amateur Sports Club (CASC) registered with HMRC. In the financial year 2020-21, the club has materially exceeded the amount of income we are allowed to earn from non-members under the CASC rules. The club is also possibly deficient in meeting its main purpose obligations of being a watersports club first and foremost, due to the proportion of income from the sale of food and drink (59%) and the inability to demonstrate at least 50% member participation in sports twelve times per year.

Given the club's plans for outdoor seating and conversion of the middle floor to a holiday let, it is likely that this is not a one off occurrence and HMRC rules require us to take action to bring ourselves into compliance. Several options have been considered to achieve this including de-registration, conversion to charitable status, reducing non-compliant activity and putting trading activity into a wholly owned subsidiary.

The Committee is recommending setting up a wholly owned subsidiary. The new entity ("Newco") will have the non-member sales of food and drink and the property income, together with associated costs. The member activity will remain in Dartmouth Sailing Club (Holdings) Ltd. This will preserve the club's CASC status and benefits (worth £13,186 in 2020-21) and allow us to grow the club's finances from sales to non-members and increased property income.

Tax Status: CASC

Dartmouth Sailing Club (Holdings) Ltd trading as Dartmouth Yacht Club is registered with HMRC as a Community Amateur Sports Club (CASC). CASC status is a tax classification scheme introduced by HMRC in 2002 and the club registered for it in 2005. It is intended to be permanent and brings a number of tax reliefs, similar to a charity but without the charitable registration and oversight process.

A CASC is required to operate within the legislation's rules. A CASC must:

i) be open to the whole community

ii) be organised on an amateur basis
iii) have as its main purpose provision or promotion of participation in eligible sports
iv) not exceed the income limit
v) meet the management conditions
vi) meet the location condition

Detailed CASC guidance can be found here.

Conformance to CASC rules

DYC has been operating successfully within these rules to date however with the growth of the club it is clear that in the financial year 2020-21 we have exceeded the income limit and probably the main purpose criteria:

Income Limit

A CASC can earn up to £100,000 a year from *non-member* trading and property income. There is no limit on the amount of income that can be generated from members. Within the £100,000 limit the club can earn a maximum of £30,000 from property income.

For DYC's purposes, non-member trading is the sale of food, drink, regalia and any other services such as canoe taster sessions and private functions to non-members. The significant item is non-member sales of food and drink which is calculated by multiplying the member discount total (@20%) x 5 and subtracting that from total food and drink sales. In the financial year 2020-21, the club's non-member sales of food and drink was £127,632 vs. member sales of £86,306.

HMRC makes it clear that the sale of food and drink as a social benefit should be incidental to the sporting purposes of the club. They quote examples of incidental sales such as supplying drink to members of a club in the bar before, during and after games and training. Loosely translated that means the club should be a watersports club first and foremost rather than a social club with watersports on the side. In 2020-21, sales of food and drink comprised 59% of the club's turnover.

To date we have not breached the £30,000 property income limit, with rent in 2020-21 being £10,659.

Main purpose

To meet one of the main purpose tests, a club must ensure that at least 50% of members are 'participating members', meaning they are:

- participating in an eligible sport (sailing, paddling, motorboating etc.)

- officiating or coaching
- providing first aid
- preparing or maintaining facilities or equipment
- being an officer or committee member
- undertaking training

The club is required to keep records to demonstrate that at least 50% of members are participating at least 12 times per year. Over the years, it has proved to be very difficult for the club to come up with a robust mechanism for recording participation. We do have records of training courses, kayak and motor boat bookings, committee membership and we have an indication of interest areas in the Webcollect membership system. However, for example, we don't have a list of members with their own boats or kayaks who would be deemed participating.

With the growth in membership over recent years to ~1600, it would be very difficult to demonstrate to HMRC that we have achieved 50% participation. HMRC's solution is to restrict non-participating membership or encourage an increase in participation.

CASC Benefits

Tax Reliefs

The club is exempt from Corporation Tax on trading profits if the turnover from that trade is less than £50,000 a year. Member activity isn't deemed trading but non-member activity is, which makes for a complicated tax calculation. In 2020-21, the club made a surplus before taxation of £37,493. Without CASC status the club would be liable for corporation tax at 19% = £7,124. With CASC status and applying the member vs. non-member trading logic, the club has no Corporation Tax to pay.

It should be noted that 2020-21 was an exceptional year with profits inflated by the receipts of £59,222 in furlough (CJRS) and Business Support Grants. Previous years have shown a small loss so would not have incurred a tax liability.

Rates Relief

The club has an 80% business rates relief on its two rateable properties (the ground floor and middle floor are separate properties for business rates). In 2020-21 this equated to a benefit of £6,062.

Other benefits

The club could (but doesn't) benefit from Gift Aid. Donations by individuals to the club are tax free. Our CASC status has been very helpful in securing grants from, for example, Sport England.

Future Trading Plans

Middle Floor

Members may recall from the previous AGM that plans to convert the middle floor to a holiday let would result in property income greater than £30,000 after year 1 of operation. That would breach the CASC property threshold limit and require us to take action such as putting the property portfolio through a separate legal entity which does not enjoy the CASC benefits. That project has planning permission but has been deferred to 2022-23 due to cost increases and building supply issues.

Outdoor seating

The temporary outdoor seating has been a huge success over the last two summers and made a significant contribution to the club's turnover. However, it has exacerbated our CASC challenge as a lot of that income was from non-members. That aside, the club is seeking a three year outdoor pavement license (renewable) as it is such a good contributor to the club's income and financial security.

Options

De-registration

HMRC makes it very clear that an organisation which breaches the CASC rules must take action to comply or risk de-registration from the scheme. De-registration would entail loss of reliefs which would be back dated to the point of non-compliance. De-registration would also be a chargeable event for tax purposes which would land the club with a hefty bill for the property as that was revalued in 2018 to £1,150,000.

A club cannot apply to de-register.

Become a charity

A charity doesn't have the same restrictions on income as a CASC, has different tax reliefs and enjoys more favourable VAT treatment but must register with the Charities Commission and be subject to its oversight. A CASC cannot apply to be recognised as a charity, it must wind up the club and transfer the assets and activities to a charity. In doing so a tax charge may apply in regard to the property (as above) because HMRC deem the property to be disposed of and reacquired at the market value on date of de-registration.

Reduce non-compliant activity

As a club we could decide to reduce our non-member activity and also not convert the Middle Floor to a holiday let. We have a rule which lets visitors use the club up to 5 times per year which we could rigorously enforce. We could choose not to have the outdoor seating or restrict it to members and guests. That would bring our non-member hospitality sales below the threshold. Not converting the middle floor would ensure we stay under the £30,000 property limit.

However, doing that would hinder growth and risk the long term financial security of the club. Even with non-member income we have made a small loss in previous years and with a significant reduction in non-member income we would not be able to afford the staffing levels in the club. Both the outdoor seating and middle floor plans are intended to provide a long term boost to the club's finances which are needed to build our cash reserves; at some stage in the future we'll have a major capital project such as replacing the roof.

The membership secretary reports that the outdoor seating is a great recruitment tool.

Put trading activity into a trading subsidiary

This is an option put forward by HMRC for clubs with high levels of non-member trading income and/or property income. Any income generated by the trading subsidiary doesn't count towards the club's income threshold, preserving the club's CASC benefits and avoiding the threat of de-registration. The subsidiary should be owned and controlled by the club, is liable for tax on profits and pays VAT as any other normal entity. The subsidiary can benefit from corporate Gift Aid on donations made to the CASC to reduce the profits chargeable to Corporation Tax. This is the option recommended by the Committee.

"Newco" Trading Subsidiary

Structure

Newco will be a wholly owned subsidiary of Dartmouth Sailing Club (Holdings)

Ltd. It will:

- be a company limited by guarantee (rather than by shares)
- be managed by the elected officers of the club and the directors will be the Flag Officers and Treasurer
- have its own, new, articles of association as the current club articles are very dated
- be registered with HMRC for tax and VAT
- have the same financial year and produce annual accounts at the AGM
- have its own bank account

Costs to set up Newco are estimated at £1500.

Business Mix

Newco will have the revenues and direct costs for non-member sales of food and drink and property rent for the middle and top floors.

Non-member income such as the ground rent from the rear apartments and kayak taster sessions may not be large enough to justify putting through Newco.

Fixed assets will remain in Dartmouth Sailing Club (Holdings) Ltd but a charge for their use may be made to Newco.

Overheads will be apportioned periodically based on a ratio of member : non-member activity. Some overheads (e.g. affiliation fees, GoCardless fees) will remain 100% in the club as they relate to membership.

For further details see "Newco - Business mix and assumptions.pdf".

Operation

Operating Newco is intended to be transparent to the members and guests with the exception of the annual AGM meeting where two sets of accounts will be presented for approval.

When buying food and drink, both members and non-members will be transacting with Dartmouth Sailing Club (Holdings) Ltd, trading as Dartmouth Yacht Club. The Till Management System will not require changes. On a periodic basis, the ratio of member to non-member spend will be calculated and the revenues transferred to Newco in the accounts system and bank accounts. Direct costs will be transferred on the same basis.

Once converted to a holiday let, the middle floor property rental income and costs will transact directly with Newco. The upper apartment would transact direct with Newco at the next appropriate change of tenancy agreement.

Periodically, an applicable share of overheads will be calculated and charged to Newco. Similarly, a charge for the use of fixed assets will be made.

Quarterly, Newco will need to submit VAT returns.

Annually, accounts will need to be prepared, submitted at the AGM for approval and sent to Companies House.

Costs for operating Newco (extra bookkeeping, accountancy fees, new instance of the accounting system etc.) are estimated at approximately £5.5k per year.