A Guide to Legal Structures for Social Enterprise

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Introduction

There is no agreed definition of what is a social enterprise and it is not the purpose of this Guide to consider the arguments about whether or not any particular purpose is or is not a social purpose or object. We aim to provide some guidance on the available legal structures and to consider some of the principal advantages or disadvantages and limitations of those structures which may influence which structure is more suited to you.

The DTI define social enterprise (‘*Social Enterprise - A strategy for success*’ - 2002) as ‘***a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owner***’.

From this it is clear that a social enterprise is not defined by its legal structure but by its purpose and, more importantly, by its effect. Accordingly the structure that should be adopted reflects the specific needs of the enterprise and it is important to give proper consideration to those needs.

This Guide does not provide a comprehensive statement of the law as it applies to the different structures and we do not include any advice or recommendation on tax or financial issues. Advice should be taken on your particular requirements at an early stage in your considering setting up a social enterprise.

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Wrigleys Solicitors LLP is a specialist charity law firm and considered one of the top 20 law firms advising charities in the UK by the Caritas Data publication Top 3000 Charities 2011/12. The Legal 500 consider Wrigleys the leading charity law firm of the North East and Chambers give the firm premier ranking.

The Charities and Social Economy Team consists of 17 lawyers working almost exclusively with clients in the charities and the wider social economy, with experience across charity, company and commercial, intellectual property, tax, property, employment, banking and financial services. Other members of the firm may advise charities, and those involved in their management, in their specialist areas. We seek to provide a full legal service to our clients, although this does not include litigation matters where we will liaise with external specialist lawyers on our client's behalf.

Further information about Wrigleys and members of our Charities and Social Economy Team can be found on our website at www.wrigleys.co.uk

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A General overview

Legal structures are generally divided in to two distinct groups, those which are unincorporated and those which are incorporated.

Unincorporated	***Incorporated***
Associations (or Clubs)	Companies
Trusts	Industrial and Provident Societies
Partnerships	Community Interest Companies
	Community Interest Societies
	Limited Liability Partnerships
	Charitable Incorporated Organisation

Some Common Features

Legal Status

The principal distinction between these two groups is that the former, the unincorporated organisation, has no separate "legal personality" or identity from those involved in its membership or management. Those involved in an unincorporated association carry potential personal liability for debts and liabilities which arise in the course of that organisation's activities. Individuals who manage the organisation, or who are appointed to represent it for that purpose, should be contracting on behalf of the organisation, for example agree a lease, buy equipment or enter into a service delivery agreement since it has no legal personality. Such individuals will usually have a right to be re-imbursed by the organisation and may, depending upon the circumstances, have the

right to be re-imbursed by other individuals who manage or are members. However they remain personally at risk, particularly if the funds of the organisation are not sufficient to cover its liabilities.

From this it will be seen that risk (and the benefit of limited liability) is one of the principal reasons why an unincorporated organisation may seek to incorporate or that incorporation is sought from the start.

Risk may arise through any of the activities of an organisation but those who carry the risk of liability should be particularly concerned, and take appropriate advice in any of the following situations:

- large or unusual contract;
- loans or other funds which may require re-payment e.g. claw back in service contracts;
- employing others; or
- leasing or buying property, especially if it is subject to any borrowings e.g. mortgage.

However there are other reasons which will help in determining which legal structure is more appropriate to an organisation such as:

- the level of regulation, including disclosure;
- the stage of development of the organisation, where there is perhaps little likelihood of personal liability in the early stages;
- tax advantages, which fall outside the remit of this Guide; or
- status or perhaps more likely the perception and requirements of others, such as funders and potential investors.

Limited Liability

It is likely that you have heard about 'limited liability', but what does this mean? As already noted an organisation with legal status can contract in its own name and has its

own assets and liabilities. This means that, generally, any liability is the liability of the organisation and not of the individuals involved. Limited liability gives the directors, employees and members protection in the event that the organisation goes into liquidation and from other claims made against it, provided they act in accordance with the relevant governing documents (its Rules or Memorandum and Articles of Association) and also act in accordance with any duties imposed on them which includes acting in the best interests of the organisation. One example is where the directors continue to operate where there are no reasonable prospects of the organisation being able to pay its debts as they fall due, known as fraudulent, wrongful or insolvent trading. Personal liability is also imposed on directors or employees by specific laws, such as those protecting the environment or the health and safety of employees.

Members' liability is limited, in a guarantee company to the financial contribution they have agreed to put in and in a share company to the price payable for the shares. This is explained further below. It is rare for any further liability to be imposed on members but this could exist where a member fails to follow the rules set out in the organisation's constitution or acts contrary to the law.

Detailed consideration of the duties of a director (who may also be called a "trustee" or a "member of the management committee" depending upon the particular organisational form) is outside the purpose of this Guide. These duties arise through decided case law and the principal director duties have recently been codified as part of the Companies Act 2006, which has come into force in stages with the last stage on 1st October 2009.

Regulation

Incorporation brings with it certain obligations. An incorporated organisation must use its full name, and give details of its registered number and address, on all formal papers. This doesn't stop you adopting a trading name, but certain formalities do need to be followed. Also, each year the incorporated organisation must file an annual return, which will give details of its directors and secretary, and accounts which must contain certain required information. However the burden of disclosure and the formalities involved do

differ depending upon which particular structure you use and whether or not you are registered as a charity.

Funding

This Guide does not seek to discuss particular sources of funds for a social enterprise. Here we set out some of the common features.

Grants: Each of the structures can receive grants. However some organisations, including some large grant-making charities, will only give grants to a charity or more particularly to a registered charity. Gifts to a charity can also benefit from tax relief (for example Gift Aid) for both the giver if they are a UK tax payer and the charity receiving payment.

Equity: Some structures can raise funds through equity investment. In this Guide we use the term equity for money invested in an organisation, usually for some kind of profit or return based on the organisation's performance rather than for a pre-determined rate of return as would be the case with interest on a loan. The return is usually financial (a dividend), but some investors may look for a social return, promoting the good works of an organisation with no, or a limited, expectation of any profit. For example there may be no return, or one that is low but over time accumulates to satisfy the investor; or shares that increase in value or allow the investor to sell without making a loss. A focus on social return may be referred to as 'social venture capital', or 'patient capital'.

Loans: Each of the structures can borrow money, and can give security against any assets it owns. Before borrowing money an organisation must ensure that it can pay the interest and repayments as they become due. Patient capital or social venture capital (see above) in loan finance includes low interest or extended repayment terms.

Trading and other income: Each of the structures can trade and make a profit on that trade. Only where the organisation is charitable will there be limits on what kind of, or how much (in value), trade may be undertaken and a requirement that 'profit' is applied towards the charitable objects. There is an expectation that any social enterprise will re-

invest any profits in its activities with only a limited return of its profits or surplus to individual stakeholders.

Asset Lock

This refers to the way in which assets are locked into the organisation and held in perpetuity for its objects. There are different ways assets may be locked such as

- rules which prohibit or limit the return on equity investment or rules which prevent the distribution of profits or assets;
- rules requiring a large majority of members to agree changes to particular rules, for example the rules which restrict distribution of assets for private benefit;
- legal requirements to obtain the consent of the Financial Conduct Authority (FCA), the CIC Regulator or Charity Commission to any change of rules.

There is sometimes confusion over what the asset lock actually means. It does not stop an organisation engaging in its ordinary business nor would an asset lock prevent a disposal (for example a gift or transfer at below value) to some other asset locked body, for example a charity. The asset lock, in its simplest form is intended to protect the assets of an organisation for its community or public purpose rather than for any private or personal gain of the members of the organisation.

It is usual in a social enterprise to find a prohibition on payments or other distributions of profit or assets to the directors and/or to members. However the "strength" of the asset lock differs depending on the structure used; some are easier to break than others. Consideration should be given to the value of the assets held by the organisation, how important it is to protect those assets and what measures any particular structure allows to protect those assets from distribution amongst the members.

Legal Structures

Company Limited by Guarantee ("CLG")

The CLG is the most common incorporated structure for a charity. It has traditionally been used by grant funded not for profit companies or social enterprise, so we shall discuss it first.

There are two principal types of company, each with limited liability. These are the CLG and the Company Limited by Shares (CLS) which we shall discuss below. Such companies may be incorporated easily and relatively inexpensively under the Companies Acts 2006.

A company is governed by two documents; the Memorandum of Association and the Articles of Association. Since 1st October 2009 for new companies, the Memorandum has become a simple statement of the company's main details, with the Articles containing what was formerly in both the Memorandum and Articles.

The company's Articles are its internal rulebook. They govern the company's internal proceedings such as the appointment of directors and the holding of members' meetings.

Together the Memorandum and Articles of Association form a contract between the company and its members.

While many commercial companies dispense with the practice of having an objects clause within the Articles, for charitable companies, and other social enterprise companies for which social branding is important, specific restrictions on the objects will be necessary either to secure charitable status, or to comply with the conditions of grant funding. For such companies the Article which contains the objects is perhaps the single most important provision. A company with defined objects cannot act outside of those objects and directors who fail to exercise control and management can be punished, including being held personally liable, for example where a director knows or should have known that any particular course of action was not permitted.

The principal advantage of establishing a social enterprise as a CLG is its ease and familiarity. The CLG provides a flexible structure which allows it to be shaped to satisfy the needs of any organisation. Its familiarity also extends to funders and potential partners who can gain great comfort from the ease of access to information concerning the organisation's objects, structure and appointed officers through the public register at Companies House.

Where other structures have an advantage is that the CLG is limited as a means of attracting outside investors. The CLG membership structure tends to attract those who directly or indirectly support the organisation's objects. The CLG does not have share capital and so cannot raise equity, including patient or social venture capital except by debt.

It is also usual to find that voting is democratic with "one member one vote", but the CLG structure is flexible and can allow for different classes of membership and different voting rights attaching to the different classes. The members' liability is limited to a requirement (the guarantee) to contribute a certain amount (usually £1 or £10 but it can be any sum) in the event of the company being wound up. This liability can arise at any time when that member is a member or within, usually, 12 months of them ceasing to be a member.

As already mentioned it is common for the rules of a social enterprise to contain a prohibition on payments or other distributions of profit or assets to the directors and members. This feature is established as part of the Articles of Association of the CLG by agreement between its members. That agreement can be changed by following a formal process which can remove any restrictions on such payments or distributions, effectively enabling assets to be paid to members. This is an example of how weak the "asset lock" is in a CLG and is often overlooked. There is currently no statutory "asset lock" which applies to the CLG but some protection exists where the CLG is a registered charity where amendments to the Articles of Association which deal with the Objects and member benefits are subject to Charity Commission consent. The Companies Act 2006 includes asset lock provisions for the CLG by permitting the 'entrenching' of provisions in the Articles, i.e. making it harder for members to change.

Setting up a CLG is relatively straightforward and inexpensive. The Memorandum and Articles of Association must be signed by the founder members and Company Form IN01 completed and sent, with the required fee, to Companies House. On that form a CLG may seek exemption from the need to use the word “limited”, although there are conditions which must be satisfied. Provided all is in order incorporation/registration will follow usually in less than a week and can be completed on line for as little as £15 with postal applications costing £20. There is a fee payable on filing the annual return and further fees as proscribed (e.g. registering a charge on assets costs £10) and late filing fees of up to £1000 if your annual accounts are overdue.

Up to date information on incorporation of a company and recurring costs is readily available from Companies House at www.companieshouse.gov.uk.

Company Limited by Shares ("CLS")

The second type of company is the CLS, which is perhaps seen as (and may suffer the perception of) being a pure commercial venture. However, as we have previously noted the DTI definition of a social enterprise does not provide for any specific structure and the CLS is sufficiently flexible to incorporate the defined objects and restrictions on

director and member benefits that will be found in a social enterprise incorporated as a CLG, including a restriction on distribution to members in the event of a winding up. It is possible to establish a charity which is incorporated as a CLS. Modifying the CLS structure to allow for such use is not common and there would need to be some strong and specific reason for seeking to incorporate a social enterprise as a CLS given the availability of alternatives which can offer the advantages of a share structure, such as the Industrial and Provident Society ("IPS") and the Community Interest Company ("CIC"), both discussed below.

Similar to the CLG, the CLS is governed by its Memorandum and Articles of Association and offers its directors and members' limited liability, this time limited to the nominal price payable for their shares. A distinction exists between a share's nominal (face) value (often £1) and its market value. A share may be issued as partly paid, meaning that for example only 50 pence is payable when it is first issued allowing the company to 'call' for the balance at some later time. For social enterprises this is rarely an issue, but it is important to recognise the flexible nature of a company's shares. Different classes of membership can be created, through different classes of shares and different rights attaching to those shares, such as extra voting rights, enhanced or preferential payments through dividends or other distributions.

The CLS has an advantage over the CLG in the flexibility of the CLS share structure which makes this particular legal form a very convenient vehicle for raising money through equity (shares) and loan capital. However the CLS is restricted in that by law it may not offer its shares for purchase by the public. There are complex rules which apply and specialist legal advice is necessary. This requirement has the effect of restricting the potential pool of investors to a few large investors who can be approached individually.

The principal advantage of the CLS is the existence of share capital which can attract additional funds. In particular a social enterprise may be able to attract patient capital, investment from those who seek a social return through promoting the work of or through association with the organisation.

A disadvantage is that the CLS is the principal legal structure used for commercial enterprise and this may be seen to taint its use for social purposes.

However it remains the case that the CLS is a popular vehicle as a wholly or partially owned trading subsidiary for charities and for other social enterprises. In the case of charities a CLS subsidiary can gift aid trading surpluses in a tax efficient manner. The flexibility of the company structure and the simplicity of its share structure make the CLS a very convenient structure for joint ventures and other partnership working.

The formalities and costs involved in incorporating the CLS are the same as for the CLG save that the Memorandum and Articles of Association will identify the structure as a CLS and include corresponding provisions about share classes and the rights attaching to those shares.

Public Limited Company ("PLC")

No structure is outside the realms of being suitable for a social enterprise. An example of such a social enterprise is Cafédirect plc, a leading fair-trade enterprise which adopted the PLC structure (having previously existed as a CLS) as part of a major fundraising project attracting more than £5 million from principally private investors (many of them customers and other supporters of fair-trade). See www.cafedirect.co.uk. Another example is The Ethical Property Company PLC which buys properties and develops them as centres that bring charities, co-operatives, community and campaign groups together under one roof where they can share skills and ideas and benefit from reasonable rents, flexible tenancy terms and office space and facilities designed to meet their needs. See www.ethicalproperty.co.uk. However, in 2010, it gave up its PLC status and became a private company again because it was becoming too expensive to make public share issues.

The PLC is similar to and based upon the CLS save that the PLC can offer its shares to the general public, although again specific legal advice is required as the rules are complex. The CLS is referred to as a private company, in contrast to the public nature of the PLC.

Many, but by no means all, PLC's will be members of a recognised stock market (e.g. FTSE or Dow Jones as international or primary markets; or AIM or PLUS (formerly

known as OFEX) as secondary UK share markets) where their shares are 'listed' or 'quoted' and can be more easily traded. The stock markets have their own rules which govern aspects of its members' behaviour, particularly governance but many of these rules can be voluntarily adopted by 'non-quoted' companies.

The formalities involved in incorporating the PLC are the same as for the CLS, although there is a minimum requirement of £50,000 share capital subscribed for on incorporation. In place of the word "limited" in its name the PLC must have "Public Limited Company" or "PLC". The costs of preparing the Memorandum and the Articles of Association are likely to be more expensive although there is little advantage to any 'standard' PLC and bespoke governing documents would be usual with costs specific to the particular circumstances. Seeking a listing will incur very substantial one off and recurring costs and is outside of the purpose of this Guide.

Industrial and Provident Societies ("IPS")

There are two types of IPS, the "bona fide co-operative" and the "society for the benefit of the community". The main difference between the two is that the co-operative will conduct its business for the mutual benefit of its members, while the benefit of the community society (also referred as a BenCom) must operate for the benefit of persons other than its own members and act in the interests of the community.

It is possible for a BenCom to have charitable status by seeking that status from HM Revenue and Customs, although currently an IPS is not required to register as a charity. This will change when proposals contained in the Charities Act 2006 come into effect. Charitable IPS with income in excess of £100,000 will have to register with the Charity Commission except where the IPS is a registered social landlord or regulated by some other body (this could be, for example, the Homes and /Communities Agency or the Financial Conduct Authority). The Charity Commission has not yet brought these provisions into effect. A charitable BenCom can receive all the tax advantages of a registered charity, for example tax relief on profits and will be treated as charitable by funders or by local

authorities giving rate relief. Some local authorities will also give a BenCom discretionary rate relief even if it is not a charity.

The BenCom is common amongst housing associations, credit unions, community development finance institutions and community shops and will be appropriate for any democratic, community focussed non-profit distributing organisation.

An IPS registered as a co-operative will adhere to the International Co-operative Alliance principles of one member one vote, limited return on capital, and open membership.

The IPS is governed by its Rules which form a contract between the IPS and its members. The Rules set out the objects of the IPS, its powers, and amongst the key clauses are those providing for the rights and duties of the members, the admission and withdrawal of members, appointment and removal of directors and for decision-making.

An advantage of the IPS structure over a company (CLG or CLS) is that although it is still necessary to maintain records, the administrative and statutory requirements are far less strict than those of companies. The incorporation costs are comparable to those of a CIC.

The IPS has share capital and is therefore similar to the CLS. However, the restriction that applies to the CLS in offering shares to the public and the requirement to issue a formal share offer prospectus may not apply to the IPS provided that certain conditions, and certain exemptions in the Prospectus Regulations, are satisfied. Consideration of those exceptions is outside the scope of this Guide and specialist advice available from Wrigleys, is required. However the exemptions, if they apply, will give substantial cost and time advantages and allow the IPS a means of raising substantial capital from investors which is unavailable to other legal structures. Such investors may seek social as opposed to financial reward. This feature of the IPS has been used to great advantage by many community development finance institutions, as well as commercial social enterprises such as Baywind Energy Cooperative Limited (see www.baywind.co.uk). However, this exemption only applies to withdrawable and non-transferable share capital in an IPS which, because of its non-transferable nature, limits its appeal to purely private investors. Further discussion of the different types of shares available in the IPS or any of the other legal structures is outside the scope of this Guide.

Interest (similar to and sometimes referred to as dividends) can be paid on shares which may also attract tax incentives, for example under Community Investment Tax Relief or the Enterprise Investment Scheme provided they are for qualifying purposes (which generally exclude affordable housing) and/or in qualifying locations; there may be other conditions to be satisfied as well. Detailed consideration of such incentives falls outside the remit of this guidance. There is a statutory limit on the amount an individual may invest (£20,000) although another IPS may invest a higher amount. On 6 January 2012 this limit was abolished in respect of transferable share capital of an IPS but the £20,000 limit on withdrawable share capital was not increased. It is proposed that the limit will be raised to £100,000 during 2014.

Whilst the IPS as a legal structure has been available for longer than the company it has not benefited from the same resources behind it as for companies. The IPS suffers from a lack of transparency since information relating to any particular IPS is slower and more expensive to obtain than for a company. Improvements have taken place in recent years to computerise the Register and it is expected further improvements will occur in future. However the IPS particularly suffers from a lack of awareness and familiarity amongst professional and other advisors.

The registration process for an IPS is simpler than that for a CIC. A completed application form, copies of the Rules, and the registration fee is sent to the FCA. Where the Society is for the benefit of the Community, the application must specify the 'special reasons' why incorporation as an IPS is sought rather than as a company. In practice this will usually be satisfied by demonstrating that the IPS will be conducted for community rather than for private benefit, with an appropriate restriction on a distribution of assets to members on a winding up.

The FCA acts as registrar and is not a regulator of IPSs. By this we mean that the FCA deals with registration of IPSs and holds information, on the Mutuals Register, relating to registered IPSs. It does not govern, or regulate, what IPSs do or the way in which an IPS manages its affairs, although it does have more powers than the Registrar of Companies and, for example, Rule changes must be approved by the FCA rather than just filed. Also it must be noted that many IPS's, for example credit unions, are either directly regulated by the

FCA or through its activities (which involve financial services) an IPS may become subject to FCA regulation e.g. debt advice agencies promoting mortgage or insurance products.

An IPS may adopt any Rules it wishes but it will be more expensive and time consuming to write all of the Rules specially. It is more common to use "Model Rules", e.g. those available for Housing Associations or Co-operatives, which are standardised governing documents that have previously been approved by the FCA as this can reduce time-scale and cost. These Model Rules are submitted via a sponsoring body and a fee will usually be payable to the sponsor for use of the Model Rules as well as to the FCA on incorporation.

The registration fee is £40 where the IPS adopts Model Rules without amendment, with the fee increasing where amendments to those Rules are sought. Sponsor fees for Model Rules will vary but may be expected to cost in the region of £300-£500, payable to the Sponsor. A stand alone registration with its own Rules will cost £950 to register. Periodic fees (annual) are charged calculated with reference to assets value but are generally £60 pa for an IPS with assets of less than £50,000, increasing to £350 pa for an IPS with assets of more than £1million.

Wrigleys have registered a Model Rules for a BenCom Community Interest Society which can be an easy starting point for most types of Ben Com.

Up to date information on incorporation and recurring costs is readily available from the FCA website at www.FCA.gov.uk/Pages/Doing/small_firms/MSR/index.shtml under the guidance for Small Firms.

Community Interest Company ("CIC")

The CIC is a new structure, introduced in July 2005 and designed specifically for those interested in establishing social enterprises. The CIC can have the structure of a CLS, CLG (which makes up the majority of CICs now registered) or PLC.

A CIC will have some extra features in order to ensure that assets and profits are used in the interest of the community. First, all CIC will have a compulsory statutory asset lock, so that the assets of the CIC may only be distributed to some other specified CIC or to

charity and not to its members or investors. Secondly, to register as a CIC a company must adopt a suitable constitution and must satisfy the community interest test. This test is to ensure that the CIC will not benefit an unduly restricted group of beneficiaries (specifically stated to exclude employee ownership as being too narrow a community of interest); it is intended to provide a community benefit. The Regulations governing CICs do specify certain activities that are not acceptable such as promoting or opposing changes to the law or government or support for a political party.

Organisations already registered as a company are able to convert into a CIC by adopting the relevant changes, such as the statutory asset lock, into its Articles of Association.

A CIC cannot be a charity and will not have the benefits of charitable status, such as charitable tax concessions. However there is emerging evidence that some local authorities are granting discretionary rate relief to CICs. Any social enterprise should consider carefully whether it will seek charitable status (more on this below).

The CIC can be established as a company limited by shares and this is seen as a positive encouragement of private investment in social enterprise. However to protect the CIC's assets dividends and other payments to shareholders are subject to a statutory cap as part of the asset lock. If a return to investors is not anticipated then the CIC limited by guarantee will be a more appropriate structure.

The statutory asset lock takes two principal forms:

- a requirement that the Articles of Association of the CIC contain rules that cap or limit any return to members; and
- a restriction on distribution of assets in the event that the CIC is wound up which require that such assets pass to some other organisation with a similar asset lock, such as another CIC or a charity and retain their community ownership rather than passing into private hands.

As a statutory asset lock members cannot simply agree to change the rules to allow distribution, unlike with the CLG. One of the key advantages of the CIC is that the members, financial backers, customers and others can be sure that the organisation is intended for the benefit of the community and not for private gain. Also if the company

ceases to be a CIC, the remaining assets will be preserved for the community rather than being divided up between the members.

The CIC does not share the same advantages as the IPS in offering its shares to the public. A more costly and time consuming process must be followed, again with the benefit of specialist legal advice. However the CIC can still raise substantial equity or social capital from a more restricted community (a limited pool of individual investors) and is not subject to the same statutory maximum investment per individual as the IPS.

The currently applicable cap on dividends (from April 2010) is 20% with an aggregate cap on all dividends at no more than 35% of allowable profit.

The CIC is registered with Companies House in the same way as an ordinary company (CLG and CLS), but a community interest statement (identifying how the CIC will benefit the community) must be filed with the Memorandum and the Articles of Association, Form IN01 and registration fee. Before incorporation/registration is complete the application will be referred to the CIC Regulator who will consider the statement and whether the statutory CIC requirements are satisfied. The rules governing CIC's require that specific provisions are contained in the Articles of Association of the CIC - such as the asset lock (including a dividend cap for the CIC limited by shares) and the manner of appointment and removal of directors.

In addition to the accounts, financial audit and annual return (all similar to the CLS and CLG), the CIC will be required to produce an annual community interest statement and report for the public record. The report must demonstrate what the CIC has done to pursue the community interest during the year. The report must also include details of payments to directors.

On going costs will be similar to the CLG. The community interest statement is likely to incur additional costs although this is unlikely to be significant as many organisations will already include something to this effect in their annual report and accounts or reports to key funders.

Up to date information on incorporation and recurring costs is readily available from Companies House website at www.companieshouse.gov.uk and from the CIC Regulator's website at www.cicregulator.gov.uk

Community Interest Society

The Co-operative and Community Benefit Societies Act 2003 introduced, for the first time, a provision that allows the assets of an IPS registered as a society for the benefit of the community to be locked, so that the members of an IPS which has such a rule cannot vote to wind up and distribute the assets among themselves without the consent of the FCA for a Rule change. This is an effective asset lock (see above) but easier than the one for the CIC and may make the IPS more attractive to investors and funders who have some assurance that their money will be held, and continue to be held, for that community benefit. Wrigleys have registered Model Rules for a Community Interest Society which have been available from July 2013. These will be particularly useful for community share issues by Ben Coms, regardless of whether an asset lock is required or not and can be adapted to become a charitable Ben Com.

Charitable Incorporated Organisation ("CIO")

The Charities Act 2006 proposed a new corporate form, the CIO, specifically for charities which became available from December 2012. CIO's have a separate legal identity from the members of the organisation. Therefore members will have limited liability in the same way that they have under the CLG. The CIO will be registered by the Charity Commission, so there will be no requirement to separately register with Companies House. This will assist in avoiding the cost of duplicate filing - for example, it will no longer be necessary to complete two annual returns or file two sets of accounts. However it remains to be seen whether the filing requirement, for example in relation to changes in directors, will be as rigorous as the companies regime, where such information is required to be filed within 28 days of any relevant change, or if it will be a case of ensuring that such information is updated only through filing of an annual return.

It is envisaged that the CIO will be most appropriate for new charities which will not engage in trading where a mortgage may be required and for existing charitable trusts and unincorporated associations who wish to convert in order to benefit from limited liability. Such latter organisations will already be subject to Charity Commission regulation and the CIO is likely to be subject to less regulation that the CLG which would be the alternative limited liability structure for such organisations. It is unlikely that existing charitable companies and IPSs will find any advantage in conversions, may also wish to convert. There are some disadvantages to converting to a CIO, including the cost of transferring assets and liabilities. Concern should be taken particularly if the existing organisation has a defined benefit pension scheme as a transfer to a CIO may trigger a requirement to make payments towards any pension deficit that may exist.

Unincorporated Association

The unincorporated association is the most common form of organisation within the voluntary and community sector. It is essentially a group of people who are bound together to pursue a common purpose. The relationship between the members is often uncertain but generally will be governed by a contract (the constitution or rules) which details the objects, powers and rules of the Association. These Rules will contain the management provisions, and may provide for a division of rights and responsibilities between a managing committee and a general meeting of the members of the Association. Such a committee (which may be referred to as the board or council) should comprise a small number of members who are responsible for the management of the Association.

It will only be a charitable association if, under the governing document, the Association's property is to be devoted to wholly and exclusively charitable purposes. Often the constitution will state that the Association's assets do not belong to the committee or the members in order to ensure they cannot be treated as having a beneficial interest in such assets. This in itself is not a strong asset lock as the rules will usually include a procedure for amendment. However, where the Association is registered as a charity, Charity

Commission consent would be required to any rule change which allowed for members to benefit.

The rules will need to provide for how committee members are appointed and discharged. They should also make provisions regarding membership. Is membership restricted to individuals or can organisations become members too? Are there different classes of membership? What are the responsibilities and powers of the general meeting?

An unincorporated association is not a distinct legal entity; it has no legal status separate from its members, so the legal title to any property cannot be vested in the association itself. Usually assets will be vested in just a few members, either members of the committee or designated trustees. These trustees hold the Association's assets but are subject to the committee's directions.

The contractual liability of the individual members of the committee should also be made clear if they are to limit their personal liability. The committee can either contract as agents and on behalf of all of the members or in their own name with a right of indemnity from the members. It is important that members of the committee are aware of the extent of, and therefore in particular any limitation of, their powers, which should be expressly provided in the rules.

There are no formal requirements to set up an association. However there is likely to be some need to regulate the relationship between the stakeholders and some basic rules will need to be established. The cost of establishing a set of rules will vary depending upon the complexity of the particular circumstances. Costs from £500 should be anticipated.

If an unincorporated association is or may be a charity then it should now consider becoming a charitable incorporated organisation.

The Trust

A trust is traditionally created by a settlor (often though a will) who transfers property or funds to, usually named individual, trustees upon trust for specific purposes. Where those purposes are exclusively charitable the trust must be registered with the Charity Commission.

A trust is an unincorporated body and is governed by a trust deed (for example the will) which will identify its purposes along with any powers of the trustees. There are certain restrictions on trustees' activities and these can be found in the Trustee Act 1925, Trustee Act 2000 and various other enactments.

As an unincorporated body the trustees will not have the benefit of limited liability, although it may be possible in appropriate circumstances to either incorporate the trust (involving a legal transfer of the assets held in trust from the unincorporated trust to an appropriate incorporated vehicle such as a CLG) or alternatively to appoint corporate trustees to act, i.e. rather than the trustees should be individuals (usually at least two) a company (usually a CLG whose objects are specifically structured to act as a trustee) is appointed as sole trustee. The directors of a corporate trustee would have the benefit of limited liability.

A trust is a more appropriate structure for a charity which already has sufficient capital and intends to give out grants, rather than carrying out charitable activities itself. As such the activities would be considered to be low risk, removing one of the principal factors that influence incorporation. A further advantage of the trust is that it is the only charitable structure that can be created by a will.

As an unincorporated organisation there are no formal requirements other than an intention to create the trust and to impose an obligation on the trustees to carry out a particular purpose. However it is more usual to find that a trust deed is used. Costs will be specific to the complexity of the trust and the manner in which it is established and will again depend upon whether a charitable trust is established which will require registration with the Charity Commission

Partnership

A partnership is automatically created where two or more persons come together to carry on a business in common with a view of profit. It would be unusual for a social enterprise to be specifically structured as a partnership given its focus on 'profit'. However those unaware of how easy it is for a partnership to come into existence may

find that they unintentionally move beyond collaborative working into developing a legal partnership. Organisations should consider using alternative such as the CLS as a joint working structure or one of the other legal structures.

The law on partnerships is old (it is still governed by the Partnership Act of 1890) and in many ways vague and it is, therefore, important to have a detailed partnership agreement providing for such things as partners' roles, financial input, timing of and means of calculating payments to be made to the partners, asset ownership, decision-making, retirement and expulsion. Typically, partners have the right to be involved in making business decisions, to share profits and losses and to examine the accounts of the business.

One of the main advantages of a partnership over a company is this lack of formality. Partnerships do not have filing or disclosure requirements. A partnership agreement is a private document, and not generally available for public scrutiny. However, a partnership does not have a separate legal identity and nor does it benefit from limited liability. The partners must contract in their own names and are each fully liable to the full extent of their assets (including their family home) on any contracts and for losses incurred by the individual, the partnership (called a firm), and losses incurred by any other partner in the course of the partnership business. The traditional advice that 'you must choose your partners carefully' continues to apply.

The cost of establishing a partnership will depend upon the degree of formality required. No formal registration is required but costs from £500 for a relatively straight forward partnership agreement should be anticipated.

Limited Liability Partnership ("LLP")

In contrast the LLP is relevant to social enterprise and represents a new means of working which, as yet, remains relatively unexplored.

This is a relatively new structure introduced by the Limited Liability Partnerships Act 2000 from April 2001. In truth it is more of a form of company than a traditional partnership and the Partnership Act 1890 does not apply. However members of the LLP

are taxed as partners. In return for the benefit of limited liability this structure has certain reporting and disclosure obligations.

An incorporation document (similar to a company's Memorandum of Association) is filed with the Registrar of Companies containing certain required information including the name and address of each member. The LLP is also required to file accounts and notify changes to the members (note the LLP doesn't have partners but members!). An LLP has members but no shareholders and as such has complete flexibility as to the internal structure which it wishes to adopt. There is no requirement to register any governing document or members' agreement (similar to the Articles of Association), although it is recommended that one is drafted as a private document between the members (as such it does not have to be filed and so does not form part of any public record) to ensure some certainty about each member's role and involvement. Like a company, however, an LLP must maintain accounting records, prepare and deliver audited annual accounts to the Registrar of Companies, and submit an annual return.

The principal advantage of the LLP is that a member's liability is limited to the contribution they have agreed to put in to the business. In this sense it is similar to the CLG but the contribution is usually substantially greater. Members remain liable for their own actions, but no longer share any personal liability for any default of any other member. The LLP has a separate legal identity so again (like a company) it can own assets in its own name. However the LLP's tax treatment is unique in that the income (and profits) of the LLP are treated and taxed as the direct income of the member, in the shares agreed in the incorporation document, rather than as the income of the LLP.

The LLP offers an opportunity unmatched by any other legal structure for several parties to work together with limited liability in an otherwise transparent structure. It allows parties to contribute capital in unequal amounts and in different forms (for example, cash, assets or in kind contributions of time and personnel) and take account of such different contributions through the profit share.

A fee of £20 is payable on registration of the Memorandum with Companies House. The annual return fee is £30. Other filing fees, similar to those of the CLG are payable.

Up to date information on incorporation of an LLP and recurring costs is readily available from Companies House at www.companieshouse.gov.uk

Other Structures

There are other legal structures which may be relevant to any particular circumstances but which are unlikely to be common and expert advice should be sought. These include:

Commonhold Association - deals specifically with land ownership in relation to common parts of a building or estate.

Friendly Societies - mutual insurance organisations providing benefits for their members such as sickness, accident, retirement, childbirth, or death benefits. May also provide social benefits and includes Benevolent Societies "for any benevolent or charitable purpose"; Working Men's Clubs and Old People's Home Societies. It has not been possible to register a new society (other than an insurance society) since February 1993

Societas Europeae - the European Company, for organisations which operate in two or more EU member states.

European Co-operative Society - for co-operatives which operate in two or more EU member states.

Other Considerations

Charitable Status

A charity in itself is not a legal structure but a recognised status and a charity can be, or charitable activities can be carried out by any of the legal structures identified above. The only exception is that the CIC cannot and IPS with an asset lock cannot register as a charity.

For charitable status to exist, the organisation must have exclusively charitable objects and exist for the public benefit. Particular attention must be given to the preparation of

the organisation's Objects clause, closely following available Charity Commission guidance, unless the proposed charity is prepared for a long dialogue/discussion with the Commission and for the costs associated with the relevant expert legal advice and support

Not all charities are required to register with the Charities Commission. Some are exempt such as the IPS (although this will change as the Charities Act 2006 is implemented) and others are under the threshold which requires a charity to register (that is its income is less than £5000 per annum). Non-registered charities may still register with the HM Revenue and Customs in order to gain tax concessions.

The charitable status of an organisation means that the extent to which a charity trustee (in a company structure this is the same as a director) may be paid, or receive any personal benefit, is restricted considerably although there is current debate in the sector over the issue of payments to trustees. A charity will be subject to greater regulation, since it will need to satisfy the rules that apply to its particular structure (e.g. the CLG) as well as the rules applicable to charities.

One of the principal advantages of charitable status is the substantial tax advantages available to charities which includes tax relief on profits, rate relief and tax relief on donations from individuals (inheritance, capital gains and income tax) and companies (and other organisations) which pay corporation tax. Often grants may only be available to charities, and some are only available to registered charities

A disadvantage, and one of the areas which causes great confusion to charities, is that it is only trade in furtherance of the charity's core charitable objects which benefits from tax relief. Where trade falls out of this primary purpose then, save for some limited (de-minimis) financial limits, the relief is lost. Where non-primary purpose trade may arise this may be overcome by the charity setting up a wholly owned trading subsidiary to conduct the trade with any profits donated (usually via gift aid) so that both the charity and the trading subsidiary receive the benefit of tax relief. The Charity Commission has issued some guidance on the relationship between a charity and a subsidiary.

New guidance issued by the Charity Commission on 6 January 2012 recognises that IPS community benefit society charities may pay a social investment interest on their share capital to investors. This is not possible for company limited by share charities who are limited to paying capped dividends to charity investors.

A registered charity is required to file annual returns and accounts with the Charity Commission, similar and often identical to the information the charity will have to file elsewhere, e.g. which the CLG files at Companies House.

A great deal of guidance is available to charities, much of which guidance forms good practice for non-registered charitable organisations and social enterprises, at the Commission website at www.charitycommission.gov.uk.