GRANTfinder Special Feature

Legal Structures for Charitable Organisations

*Article submitted by the Idox Information Solutions VCSE Team**

Introduction

Deciding on the correct legal structure for your organisation will affect the governance, fundraising and even the impact of your organisation and must be researched thoroughly. Each structure varies greatly in its requirements, effectiveness and purpose and must be meticulously researched before one is chosen.

There are now several legal forms for charitable organisations to take, meaning groups have greater operating flexibility and choice than before. With the seismic changes we have seen recently in the funding landscape, the time has never been better to re-look at your organisation and see what changes could be made.

In this feature we have identified some of the most common legal forms available to organisations and identified their advantages, disadvantages and requirements, as well as their national bodies (where available) and some successful examples of each.

Traditional grant funding is no longer the only financial option for charitable organisations. With the new focus on sustainable income generation and the need for charities to start becoming involved in the delivery of

public services, it is time for groups to assess their needs and objectives and design an organisational plan that is appropriate, responsive and effective.

1. Charity

Definition:

A charity is an organisation that is set up for the exclusive purpose of carrying out charitable purposes that benefit the public.

Advantages:

Becoming a registered charity offers the following advantages:

- Tax breaks and exemptions.
- Paying no more than 20% of normal business rates on premises.
- Ability to raise funds more easily than non charitable bodies.

Requirements:

To become a registered charity, an organisation must:

- Be set up for public benefit and not for individuals.
- Be set up for a charitable purpose which fits one of the 13 purposes recognised by British law through the Charities Act 2006. These include the prevention or relief of poverty, advancement of education, religion, health or the saving of lives.
- Register with the Charity Commission for England and Wales if:
  - i. It is set up in England and/or Wales.
  - ii. It has a total income of more than £5,000 a year. (If annual income is less than £5,000, it can register as a charity with HM Revenue and Customs for tax purposes only.)
  - iii. The majority of charity trustees live in England and Wales.
  - iv. It is set up in England and/or Wales.
  - v. The majority of the assets are in England and Wales.
  - vi. It is registered as a company in England and Wales.
- Have trustees who cannot be paid by, or gain financially from, the charity.
- Operate within the limits set out by its governing document, which depending on the nature of the charity may be a constitution, trust deed or memorandum and articles of association.

(Note: requirements may vary for the Charity Commission in Northern Ireland and the Office of the Scottish Charity Regulator.)

National body?

The Charities Aid Foundation, a registered charity, works to create greater value for charities and social enterprise. It does this by transforming the way donations are made and the way charitable funds are managed. It also helps shape the charitable sector through its research and events.

2. Charitable Trust or Foundation

Definition:

A trust or foundation is a legal categorisation of non-profit organisation that may provide support to other organisations or provide funding for their own charitable activities.

A charitable trust or foundation is one that has been created exclusively for charitable purposes solely for public benefit.

There are different types and sizes of trusts and foundations. They can be set up, for example, by commercial companies that want a vehicle to support charitable giving or by individuals who want a means of directing their assets or income to a charitable purpose that they can control.

Advantages:

Becoming a charitable trust/ foundation offers the following advantages:

- Tax relief and benefits.
- Control of where money is being directed.

Requirements:

To set up a charitable trust/foundation, an organisation or individual must:

- Draw up a formal document (trust deed, constitution, articles of association, etc) that defines the trust's charitable purposes, how the trustees must operate, as well as its approach to investment.
- Appoint trustees who are responsible for the control and management of the charity's administration.
- Fund the trust, either by transferring assets or by soliciting donations.
- Apply for charitable status, if the trust's annual income exceeds £5,000, by registering with the Charity Commission.
- Upon registration, publish a formal annual report and accounts.

National Body?

The Association of Charitable Foundations (ACF) is the leading membership association for trusts and foundations in the UK with over 300 members ranging in size from small and local grant-makers to some of the world's largest foundations.

3. Industrial and Provident Societies

Definition:

An industrial and provident society (IPS) is an organisation conducting an industry, business or trade, either as a co-operative or for the benefit of the community, that is registered with the Financial Services Authority (FSA) under the Industrial and Provident Societies Act 1965 (I&P Act 1965). IPSs fall under the following two categories:

- Bonafide co-operative society - the conduct of the business is for the mutual benefit of the members, with control of the society being vested in the members equally under the principle of 'one man, one vote'. Interest on any capital cannot exceed a rate necessary to carry out the society's objectives and any profits must be distributed amongst members in relation to the extent that they have taken part in the society's business.
- Benefit of the community - the business must be run primarily for the benefit of the community at large, not for members of the society, and profits must be ploughed back into the business, not distributed to the members. The organisation must have special reasons for not registering as a company.

Advantages:

Becoming an IPS offers the following advantages:

- Incorporated organisations can hold property and take legal action in their own name.
- Committee members are protected from personal liability under contracts and can generally only be personally liable if they act fraudulently or in breach of trust, or continue to run the organisation when they ought to know that it has no reasonable chance of avoiding insolvent liquidation.

Disadvantages:

The potential disadvantages of being an IPS are as follows:

- If the organisation does not use model rules, registration can be a lengthy, expensive process.
- Annual returns, accounts and an annual fee must be

submitted to the FSA.

- Registers of members and officers must be kept and be available for public inspection.
- An IPS cannot register with the Charity Commission; therefore, it will not receive a registered charity number.
- A charity IPS should submit its constitution to the Inland Revenue as charitable; otherwise it will not be able to claim tax advantages of charitable status and may have to pay corporation tax.

Examples of IPSs include: retail, agricultural and housing co-operatives, working men's clubs, allotment societies, sports clubs, community associations, housing associations, registered social landlords and credit unions.

4. Community Interest Company

Definition:

Community interest companies (CICs) are established to trade for the good of the community rather than to make a profit for the owners. CICs are companies formed under the Companies Act 2006 and are subject to that Act and company law generally. Most CICs are companies limited by guarantee, however those that want to raise equity by issuing shares must be either a private company limited by shares or a PLC.

The two main features of a CIC are:

- Asset lock - this prevents profits being distributed to members or shareholders other than in certain circumstances as the assets and profits must be permanently retained within the CIC and used solely for community benefit, or transferred to another organisation which itself has an asset lock.
- Community Interest Statement and Report – CICs must register with Companies House and provide a statement that the CIC is pursuing the community interest which is assessed by the CIC Regulator. A community interest report must be filed each year, including details of the remuneration of directors, dividends paid on shares and interest paid on certain types of loans. It must also explain what it has done to benefit the community and how it has involved its members in its activities.

Advantages:

The advantages of becoming a CIC include:

- CICs have fewer regulations than charities and can be established for any lawful purpose, as long as it provides a benefit to the community.
- Directors can be paid and still maintain strategic control.
- CICs limited by shares can sell shares and pay dividends to individual shareholders, subject to a limit known as a cap.
- Other than applying for charitable status, setting up a CIC is the simplest way of ensuring that the organisation ' s assets and profits are used for the benefit of the community.

Disadvantages:

The potential disadvantages of being a CIC are that CICs lack many of the fundraising and tax benefits associated with charitable status, including relief from corporation tax, capital gains tax, stamp duty and inheritance tax, as well as benefiting from tax-effective giving, even if their purpose and activities are entirely charitable.

The CIC structure is particularly useful for:

- Organisations that are going to earn all or most of their income through trading, or those that hold property.
- Charities that operate a trading arm and wish to differentiate between their philanthropic work and the pursuit of profits for the social good.
- Unincorporated bodies running recreational, village and community facilities to protect their assets and those running them.
- Social entrepreneurs who establish trading concerns and want to maintain operational control.

5. Social Enterprises

Definition:

Social enterprises are businesses that trade for a social and environmental purpose. With no financial commitment to

investors, shareholders or owners, social enterprises are able to reinvest their surplus income to sustain and develop their goals.

Social enterprises contribute over £24 billion annually to the UK economy and employ approximately 800,000 people across almost every industry, including:

- Community enterprises.
- Credit unions.
- Trading arms of charities.
- Employee-owned businesses.
- Co-operatives.
- Development trusts.
- Housing associations.
- Social firms.
- Leisure trusts.

National body?

The UK's national body for social enterprises is the Social Enterprise Coalition, which was established in 2002 and represents over 10,000 social enterprises, umbrella bodies and networks. In February 2010, the Social Enterprise Coalition launched the Social Enterprise Mark, which aims to increase the visibility of socially motivated businesses and establish a recognisable niche for social enterprises in the business community.

Example:

One of the most high profile social enterprises in Britain is the restaurant 'Fifteen'. Established in 2002 by celebrity chef Jamie Oliver, the restaurant offers disadvantaged young people with problems including homelessness, unemployment and drug or alcohol addiction the opportunity to secure a 12 month work placement at the restaurant. The placement includes college learning and work experience as well as trips to farms, vineyards and fisheries.

The Jamie Oliver Foundation aims to build on existing restaurants in London, Cornwall and Amsterdam to turn Fifteen into a global social enterprise brand that will inspire young people all over the world.

6. Company Limited by Guarantee

Definition:

The Company Limited by Guarantee (CLG) model is the type of company normally chosen by voluntary organisations, charities, social enterprises and community groups that require a legal structure and:

- Have a substantial turnover.
- Employ staff.
- Own or occupy premises.

Types of organisation that often seek CLG status include:

- Clubs.
- Membership organisations, including students' unions and workers' co-operatives.
- Non-governmental organisations (NGOs).
- Charities.

Advantages:

The advantages of becoming a CLG include:

- The personal assets of the members are not usually at risk if the company becomes liable for any debts.
- The company is able to undertake all of its activities in its own right.
- It provides a democratic structure - the members elect the directors or management committee and have the right to remove them.
- The company framework is suitable for any size of organisation, so a small organisation can expand without being restricted by its structure.
- Owning and transferring property is simplified as no individuals have to be appointed as nominal owners.

A Company Limited by Guarantee can be formed by a group of people wishing to set up a new organisation, or by the committee of an existing, constituted organisation. Organisations seeking to become a CLG must submit a Constitution to Companies House, consisting of the following:

- Memorandum of Association - Setting out the objectives of the company, the powers the company has to pursue its objects and the extent of the liability of the members should the company wind up.
- Articles of Association - Stating the rules governing how the company is to be run, including procedures at meetings, voting procedures, accounting procedures and the method of electing the committee of management, usually referred to as the Board of Directors.

Although a Company Limited by Guarantee can have a social mission written into their Memorandum and Articles of Association, this is not regulated.

7. Charitable Incorporated Organisation

The CIO is a corporate structure for charities designed to protect trustees from financial penalties incurred by the organisation and enable the charity to legally conduct business in its own name and not that of its trustees.

Key features include:

- No minimum income registration threshold.
- All CIOs will be required to submit accounts and annual returns to the Commission regardless of income.
- CIOs will have to comply with the other additional responsibilities outlined in the Charities Act 2006 and the CIO Regulations.
- A CIO will officially exist once it is registered with the Commission.

The Charity Commission published its first guidance documents and model constitutions to support anyone interested in establishing a CIO to help them decide if the CIO structure is appropriate for them and also to familiarise themselves with the guidance and constitutions ahead of implementation.

For further information and to access the document you should refer to the Charity Commission website.

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