2015

Local Healthwatch Legal Entities

A decision making tool to support local Healthwatch determine the most appropriate legal entity for their social enterprise

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Talking Health Taking Action
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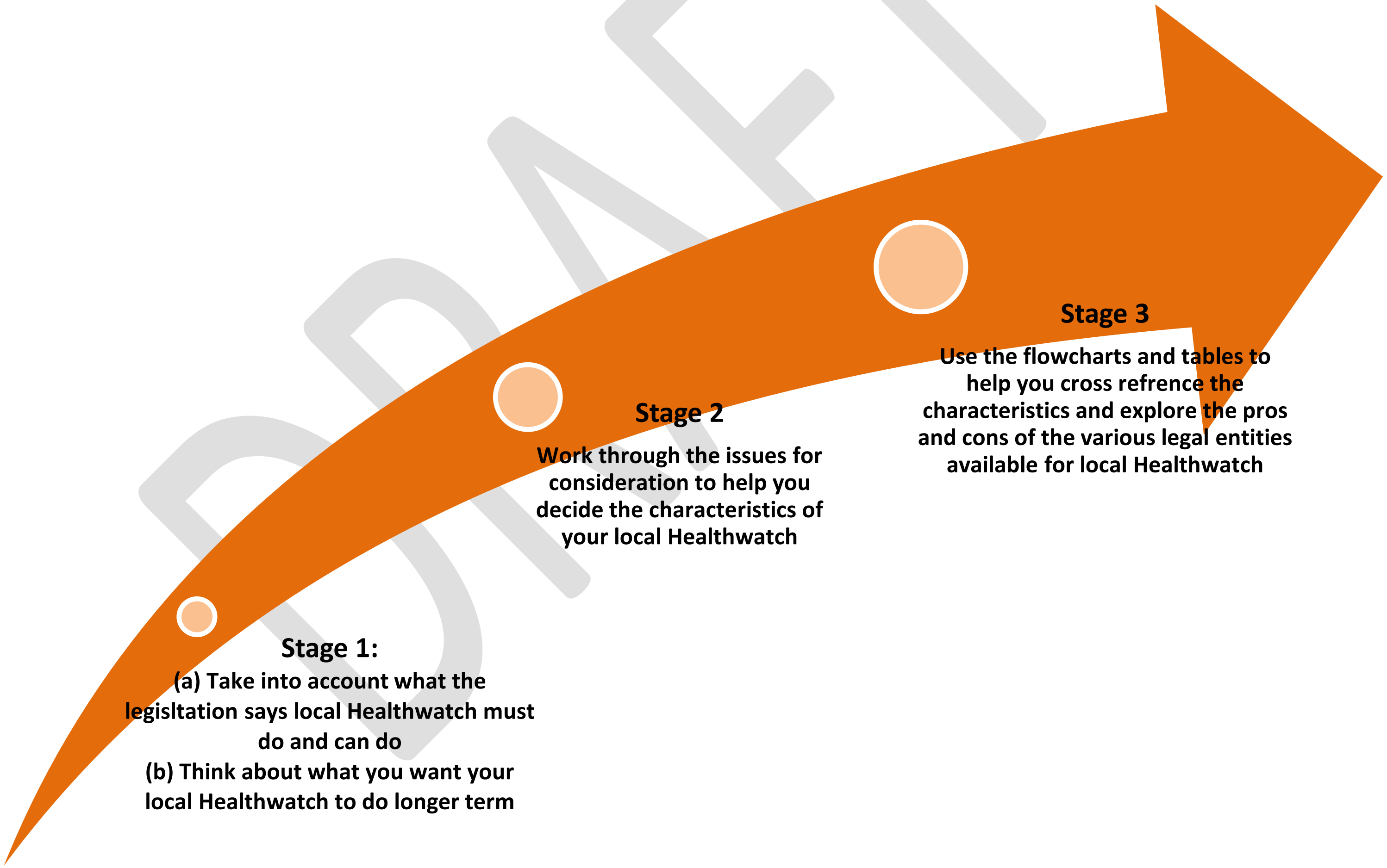
How to use this decision making tool

This decision making tool has been designed to support local Healthwatch thinking of changing their legal structure determine the most appropriate legal entity for their organisation. It will do this by supporting you through three stages (see below) during which you will have the opportunity to think through what you want your organisation to achieve now and in the longer term, and then use that knowledge to consider the pros and cons of the different legal structures available to you. This will help you make a decision about which legal structure is best suited for your local Healthwatch.



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Disclaimer

This tool gives you a general overview of some of the major considerations when choosing the legal structure for your enterprise. It is not intended as a form of legal advice. You should always seek professional advice, including legal advice if you are not certain as to what legal structure is appropriate for your local Healthwatch. This is important to get right from the beginning, since it can be both complex and expensive to change from some legal forms to another later down the road.[1]

[1] https://unltd.org.uk/socialentrepreneurshiptoolkit/

Glossary

Term	Definition
Articles of Association or "The Articles"	The rules of a company which set out the internal management structure and procedures, such as the role of members and directors, procedures for appointment and removal, conduct of meetings and so on.
Asset Lock	Rules about the way in which the assets of the company can be distributed.
Board of Directors/Trustees	People responsible for determining policy, supervising the management of the company's business and exercising the powers of the company. Directors/Trustees generally carry out these functions collectively as a board.
Body corporate	A legal entity entirely separate from the individuals comprising its membership.
Business Rates	A tax on the occupation of non-domestic property.
Capital Gains Tax	A tax levied on profit from the sale of property or an investment.
Charity Commission	The body that registers and regulates charities in England and Wales.
Companies Act	The Companies Act 2006.
Companies House	The registry for companies in England and Wales.
Constitution	A contract setting out how the company/body will run i.e. the rules.
Corporation Tax	A tax levied on companies' profits.
Guarantors	The members of a company limited by guarantee whose liability is limited to a specified amount.
Dividends	The distribution of a portion of the company's assets (usually cash) to its members.
HMRC	HM Revenue and Customs.
Management Committee	People responsible for determining policy, supervising the management of the company's business and exercising the powers of the society.
Members	The company's owners.

Memorandum of Association	A constitutional document comprising the subscriber clauses required for the incorporation of company
PAYE	Pay As You Earn and is a scheme that HMRC use to collect income tax and national insurance contributions from employees as they earn it.
Profit	A financial benefit that is realised when the amount of revenue gained from a business activity exceeds the expenses, costs and taxes needed to sustain the activity.
Registrar of Companies	The official responsible for maintaining the company records filed under the requirements of the Companies Act
CIC Regulator	The Community Interest Company Regulator.
Shareholders	A person or body owning a unit(s) of the company.
Social enterprise	In respect of local Healthwatch an organisation is considered to be a social enterprise if a person might reasonably consider that it acts for the benefit of the community in England; [2] and it satisfies the criteria in the local Healthwatch regulations, including that lay people and volunteers are involved in governance.
Value Added Tax (VAT)	An indirect tax on the domestic consumption of goods and services, except those that are zero-rated

[2] Section 222 (2) and (8) of The Local Government and Public Involvement in Health Act 2007 (as amended by Section 184 Health and Social Care Act 2012).

Stage 1: Local Healthwatch and the Legislative Framework

The Local Government and Public Involvement in Health Act (2007) requires local Healthwatch to undertake certain activities. It also provides local Healthwatch with the power to undertake other activities at its own discretion.

A full overview of the legal requirements of local Healthwatch has been produced by Healthwatch England.[3]

A brief summary of the mandatory and discretionary activities are as follows:

What does the legislation say local Healthwatch must do?:[4]

1. Promoting and supporting the involvement of local people in the commissioning, the provision and scrutiny of local care services
2. Enabling local people to monitor the standard of provision of local care services and whether and how local care services could and ought to be improved
3. Obtaining the views of local people regarding their needs for, and experiences of, local care services and importantly to make these views known
4. Making reports and recommendations about how local care services could or ought to be improved. These should be directed to commissioners and providers of care services, and people responsible for managing or scrutinising local care services and shared with Healthwatch England
5. Providing advice and information about access to local care services so choices can be made about local care services
6. Formulating views on the standard of provision and whether and how the local care services could and ought to be improved; and sharing these views with Healtwatch England
7. Making recommendations to Healthwatch England to advise the Care Quality Commission to conduct special reviews or investigations (or, where the circumstances justify doing so, making such recommendations direct to the CQC); and to make recommendations to Healthwatch England to publish reports about particular issues
8. Providing Healthwatch England with the intelligence and insight it needs to enable it to perform effectively.

[3] Healthwatch England. Understanding the Legislation: An overview of the legal requirements for local Healthwatch. Revised August 2013.
[4] Section 221 (2) of The Local Government and Public Involvement in Health Act 2007

What does the legislation say local Healthwatch can do?

1. May involve persons or organisations (other than the local authority) to help carry out some (but not all) of its activities[5]
2. Ask providers for information which they must make available[6]
3. Refer matters relating to social care services to an overview and scrutiny committee of a local authority[7]
4. Enter and View providers' places of work so it can observe matters relating to health and social care services (these powers do not extend to services relating to local authorities' social service's functions for people under the age of 18).[8]

Action:
Take into account what the legislation says local Healthwatch must do and can do, and use this to inform your discussions about what you want your local Healthwatch to do in the longer term.

[5] Section 222 of The Local Government and Public Involvement in Health Act 2007
[6] Section 224 of The Local Government and Public Involvement in Health Act 2007
[7] Section 226 of The Local Government and Public Involvement in Health Act 2007
[8] The Local Authorities (Public Health Functions and entry to Premises by Local Healthwatch Representatives) Regulations 2013 (18 February 2013). The arrangements to be made by Relevant Bodies in respect of Local Healthwatch Regulation 2013 (28 March 2013).

Stage 2: Issues for Consideration

According to government regulations a local Healthwatch must be ***a body corporate which is a social enterprise***. Although there is no legal definition for what constitutes a social enterprise, for the purposes of section 222(8)(b) of the 2007 Act (Local Healthwatch: social enterprises) the criteria prescribed are that the constitution of the body must—

a) state, or contain provisions which ensure, that not less than 50 per cent of its distributable profits in each financial year will be used or applied for the purpose of the activities of that body;
b) contain a statement or condition that the body is carrying on its activities for the benefit of the community in England; and
c) where appropriate, contain provisions relating to the distribution of assets which take effect when that body is dissolved or wound up, as follows:
    - require that the residual assets of the body be distributed to those members of the body (if any) who are entitled to share in any distribution of assets on the dissolution or winding up of that body according to those members' rights and interests in that body;
    - in the case of a company not limited by guarantee and registered as a charity in England and Wales, provide that no member shall receive an amount which exceeds the paid up value of the shares which the member holds in the company; and
    - designate another social enterprise (within the meaning of section 222(8) of the 2007 Act) to which any remaining residual assets of the body will be distributed after any distribution to members of the body.

Form Follows Function

The phrase of "form follows function" generally refers to the design principle that the shape of a building or structure should be determined by its function or purpose. When applied to the design or composition of organisations, the term states in essence that an organisation's function (its primary purpose, goals, strategy) should determine its form or structure.[9] So before moving onto decide the "form" of your local Healthwatch it would be prudent to consider its "function". While there is considerable scope for choosing from a number of different legal forms, there are ***two fundamental principles*** used to determine whether or not an organisation is seen as a social enterprise:

1. It is not the legal structure that makes an organisation a social enterprise – it is its activities
2. The structures you choose can have a major impact on how you are able to respond to immediate and future funding and income generating opportunities.[10]

The rest of this stage will support you to think about these fundamental principles as applied to local Healthwatch.

[9] http://www.strategicleadershipinstitute.net/news/let-form-follow-function-for-more-effective-change1/
[10] https://unltd.org.uk/socialentrepreneurshiptoolkit/

Your Activities - how do you want the organisation to be managed and run?

Governance

As we have seen the activities that local Healthwatch must do and can do are determined by legislation. Within this context the decisions you make about how your organisation is managed and run will determine what activities your local Healthwatch engages in.

All social enterprises need a person or group of people to set the strategy (long term plans), make sure that the strategy is put into action, and make sure that the organisation works within the law and meets its legal obligations. Depending on the legal structure chosen this role is carried out by either the:

- **Board of Directors/Trustees (company limited by shares/guarantee/registered charity which is a company limited by guarantee/CIC/CIO)** – a shareholder or guarantor is also known as a member. Members may or may not be directors of the company. Members have the right to elect directors to manage the company on their behalf. The directors are accountable to the members and can be removed by the members. Limited companies are only required to have one member and one director (who may be the same person). However, as most social enterprises claim to be operating for the good of stakeholders, the community or society in general it is good practice to have least three directors and five or more members.
- **Management Committee (industrial and provident society) -** can be all the members or a smaller management committee provided that the managers are appointed by the members and can also be removed by them.

Grant funders are more attracted to organisations with a wider membership. A greater number of board members will increase the level of oversight. However, the more board members the more difficult and time consuming the organisational decision making will be.

Action:
Think about the balance in terms of enabling a diversity of viewpoints whilst maintaining quick and decisive decision making. Think about the regulations in relation to local Healthwatch and in particular the need to involve lay people and volunteers in the governance of the organisation.[11] Each local authority will enter into bespoke arrangements with its own local Healthwatch and the issue of lay and volunteer involvement will be covered in these contracts.

[11] Regulation 38, The NHS Bodies and Local Authorities (Partnership Arrangements, Care Trusts, Public Health and Local Healthwatch) Regulations 2012

Future funding and income generation opportunities – things to consider

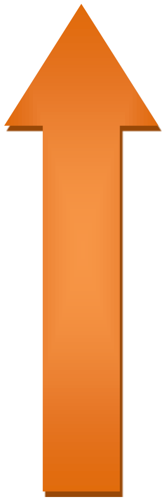
Personal liability

Legislation has determined that local Healthwatch ***must be corporate bodies*** (i.e. an independent legal entity) ***providing limited liability*** to the members/guarantors/owners.[12] Having a legal structure that separates the members/guarantors/owners from the enterprise will limit their personal liability if the enterprise suffers financial loss, or if financial loss is caused by the enterprise (this immunity is not valid if the members/guarantors/owners have acted negligently or fraudulently).[13]

Ownership – who do you want to be in ultimate control of the organisation?

Listed below are the ranges of legal entities available to social enterprises in order of structures that afford greater control to a smaller number of people, to those in which ownership is shared among the many.[14]

Ownership by few



- **Company limited by shares or Charitable Incorporated Organisation** – the shareholders have outright ownership of the company. The more shares you own the more votes and influence you have over the strategy, management and operation of the enterprise. Any profit made by the enterprise is usually distributed to the shareholders by means of a dividend. The founders will usually be the directors and are paid for their employment. The management board may be supplemented through the appointment of non executive directors. A community interest company may be limited by shares, but dividends are usually limited.
- **Company limited by guarantee or Charitable Incorporated Organisation** – there are no shareholders, instead the company has a number of guarantors. The liability of the guarantor is determined by the amount of the guarantee they have committed to. There is no legal minimum or maximum guarantee amount. If each person guarantees the same amount they will usually have one vote each. Profits can be distributed. Social enterprises with this structure may also embed within their constitution (Articles of Association) that profits will not be distributed but will be reinvested in the company, to charities of the community they serve. The Articles will also govern the distribution of assets if the company closes down. Assets may be distributed to other companies undertaking similar work, or to the guarantors.
- **Industrial & Provident Society (co-operative model)** – Ownership is shared with other members of the co-operative. In order to be considered a co-operative each member will usually have only one vote, however much they invest in the co-operative. The maximum investment by any one individual is restricted to £20,000. Investors may receive dividends.

Ownership by many

[12] Section 221 (2) of The Local Government and Public Involvement in Health Act 2007
[13] https://unltd.org.uk/socialentrepreneurshiptoolkit/
[14] https://unltd.org.uk/socialentrepreneurshiptoolkit/

Funding, both short and long term – how do you intend to generate income?

This is a question of crucial importance as the legal structure of the social enterprise will determine the kinds of funding that the company is able to access. Grant making trusts will only fund companies that do not distribute profits or their assets if they close down. However, choosing a structure that allows you to receive grants in the short term may prevent you from accessing investment when you want to scale up later down the line. There are a number of different Industrial and Provident Societies and most cannot access grant funding, the exception being a co-op established for the Benefit of the Community (which is also an unregistered charity). All types of social enterprises can access loans.[15]

If your organisation generates income through charging a fee for its services – classed as "trading" – this may affect your ability to benefit from charitable status. To be a registered charity, an organisation must be established for charitable purposes only, although some trading is permitted within these rules. If charities undertake trading activities, they need to take care that they stay within the rules on trading or set up appropriate forms for the trading activities.[16]

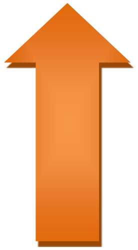
Action:
It would be wise to agree, in the first instance, what the most likely form of long term funding will be for your local Healthwatch and either choose a legal structure that enables you to access it, or have a strategy for adapting your legal structure as and when it becomes necessary. As local Healthwatch is required to be a social enterprise, there is some expectation that it will provide services in return for a fee.

Profit distribution – what will you do with any profits you make?

By definition a social enterprise should be generating "profits", or surpluses. How the profits are used is determined by the legal structure:

[15] https://unltd.org.uk/socialentrepreneurshiptoolkit/
[16] Sayer Vincent. Trading Issues made Simple. Charity Finance Director's Group & Sayer Vincent, 2008.

Profits distributed



- **A company limited by shares** will normally distribute the profits (pay a dividend) to the shareholders and so are attractive to investors
- **A CIC limited by shares** may distribute profits (pay a dividend) if agreed by a resolution of its members. Dividends payable to private shareholders (non asset locked bodies) will be subject to a dividend cap [17]
- **A company limited by guarantee** will tend to re-invest the profits within the company to grow the company and increase its social impact
- **Registered charities and co-ops** that are charitable in nature are not permitted to distribute profits so they usually re-invest them in the business

Profits re-invested

Implications for local Healthwatch:
If the local Healthwatch <u>is not</u> a company limited by guarantee and a registered charity, or <u>is not</u> a CIC registered as a company limited by guarantee, or <u>is not</u> a CIO then its constitution/memorandum and articles of association must contain a statement to the effect that the local Healthwatch is carrying on its activities for the benefit of the community in England. The constitution/memorandum and articles of association must also and ensure that not less than 50% of its distributable profits in each financial year will be used for the purpose of its activities and contain an ‘asset lock’.[18]

Taxation liability - what are the tax implications?[19]

One of the main benefits of charitable status is the tax relief available to charities. Organisations with charitable status are exempt from corporation tax, income tax and capital gains tax on income used for charitable purposes. They are entitled to 80% mandatory relief on business rates and a further 20% at the discretion of the local authority. They are also exempt from stamp duty on land transactions. For these reasons, most organisations engaged in activities which might fall under the definition “charitable” will be keen to obtain charitable status. Being a charity would be the default option, unless the organisation engages in substantial non-charitable trading activity, is primarily a campaigning organisation[20], or wishes to distribute its profits to shareholders.

[17] The cap is currently 20% of the paid up value of a share in the company and a maximum aggregated dividend of 35% of the distributable profits. Unused dividend capacity can be carried forwards for 5 years. There is also a cap on performance –related interest of 10% of the average amount of debtor the sum outstanding under debentures issued by the company. (Unltd tool kit)

[18] For a full explanation of the ‘asset lock’ see Healthwatch England ‘What are the requirements relating to being a social enterprise’ in Understanding the Legislation: An overview of the legal requirements for local Healthwatch. Revised August 2013.

[19] The following information about tax liabilities are based on current (March 15) legislation and case law which may change over time.

[20] See Regulation 36, The NHS Bodies and Local Authorities (Partnership Arrangements, Care Trusts, Public Health and Local Healthwatch) Regulations 2012

The table below provides a summary of the tax implications for the different forms of legal entity available to social enterprises.

Legal structure	Corporation Tax	Income Tax	Other taxes
Company Ltd by Guarantee	• Must register for Corporation Tax and complete an annual Corporation Tax return CT600 • Any surplus is liable to Corporation Tax, unless the organisation can prove the income was not generated through trading	• No reliefs available	CLGs pay: • VAT on purchases (but if they are doing something that qualifies as a VATable supply, they can offset this against the VAT they must charge) • Stamp duty • Capital gains tax • Tax on dividends from UK companies • Business rates
Registered Charity (company Ltd by guarantee)	• Income from charitable activities is exempt from Corporation Tax • Tax reliefs are not automatic. The charity must first apply to HMRC on form CHA1 for recognition as a charity for tax purposes.	• Can reclaim income tax on donations (Gift Aid), gifts of land or shares and bank interest.	Charities pay tax on: • Dividends from UK companies • Profits from developing land or property • Purchases (VAT) • Charities are exempt from capital gains tax, provided they apply the gains for charitable purposes • Charities can claim an 80% mandatory discount on business rates, plus 20% discretionary relief • Charities do not pay stamp duty if the building is purchased for charitable purposes
Company Ltd by Shares	• Must register for Corporation Tax and complete an annual Corporation Tax return CT600 • Any surplus is liable to Corporation Tax	• No reliefs available	Companies limited by shares pay: • VAT on purchases (but if they are doing something that qualifies as a VAT-able supply, they can offset this against the VAT they must charge) • Stamp duty • Capital gains tax • Tax on dividends from UK companies • Business rates
Industrial & Provident Society (Community Benefit)	• Charitable IPS community benefit societies (Bencom) are classed as exempt charities and do not pay Corporation Tax. • Community benefit I&Ps must	• Can reclaim income tax on donations (Gift Aid), gifts of land or shares and bank interest.	Pay tax on: ○ Dividends from UK companies ○ Profits from developing land or property ○ Purchases (VAT)

	register with the Charity Commission if they wish to receive charitable tax breaks.		• Exempt from capital gains tax, provided they apply the gains for charitable purposes • Can claim an 80% mandatory discount on business rates, plus 20% discretionary relief • Do not pay stamp duty if the building is purchased for charitable purposes
Community Interest Company (Limited by shares)	• Must register for Corporation Tax and complete an annual Corporation Tax return CT600 • Any surplus is liable to Corporation Tax	• No reliefs available	CICs limited by shares pay: • VAT on purchases (but if they are doing something that qualifies as a VAT-able supply, they can offset this against the VAT they must charge) • Stamp duty • Capital gains tax • Tax on dividends from UK companies • Business rates
Community Interest Company (Limited by Guarantee)	• Must register for Corporation Tax and complete an annual Corporation Tax return CT600 • Any surplus is liable to Corporation Tax	• No reliefs available	CICs limited by guarantee pay: • VAT on purchases (but if they are doing something that qualifies as a VAT-able supply, they can offset this against the VAT they must charge) • Stamp duty • Capital gains tax • Tax on dividends from UK companies • Business rates
Charitable Incorporated Organisation (CIO)	• Income from charitable activities is exempt from Corporation Tax • Tax reliefs are not automatic. The CIO must first apply to HMRC for recognition as a charitable organisation for tax purposes.	• Can reclaim income tax on donations (Gift Aid), gifts of land or shares and bank interest.	Pay tax on: ○ Dividends from UK companies ○ Profits from developing land or property ○ Purchases (VAT) • Exempt from capital gains tax, provided they apply the gains for charitable purposes • Can claim an 80% mandatory discount on business rates, plus 20% discretionary relief • Do not pay stamp duty if the building is purchased for charitable purposes

Summary of Issues for Consideration in relation to your chosen legal entity

Your chosen legal entity must:	Things that are for you to decide
Be a corporate body	Who owns the organisation
Be a social enterprise	How to generate income for the benefit of the community in England
Must have rules about how any profits are distributed (an asset lock)	Whether to take advantage of the tax relief that is available to registered charities
Must carry out activities for the benefit of the community in England	
Must include volunteers and lay people in the governance of the organisation	

Stage 3: Possible Legal Structures

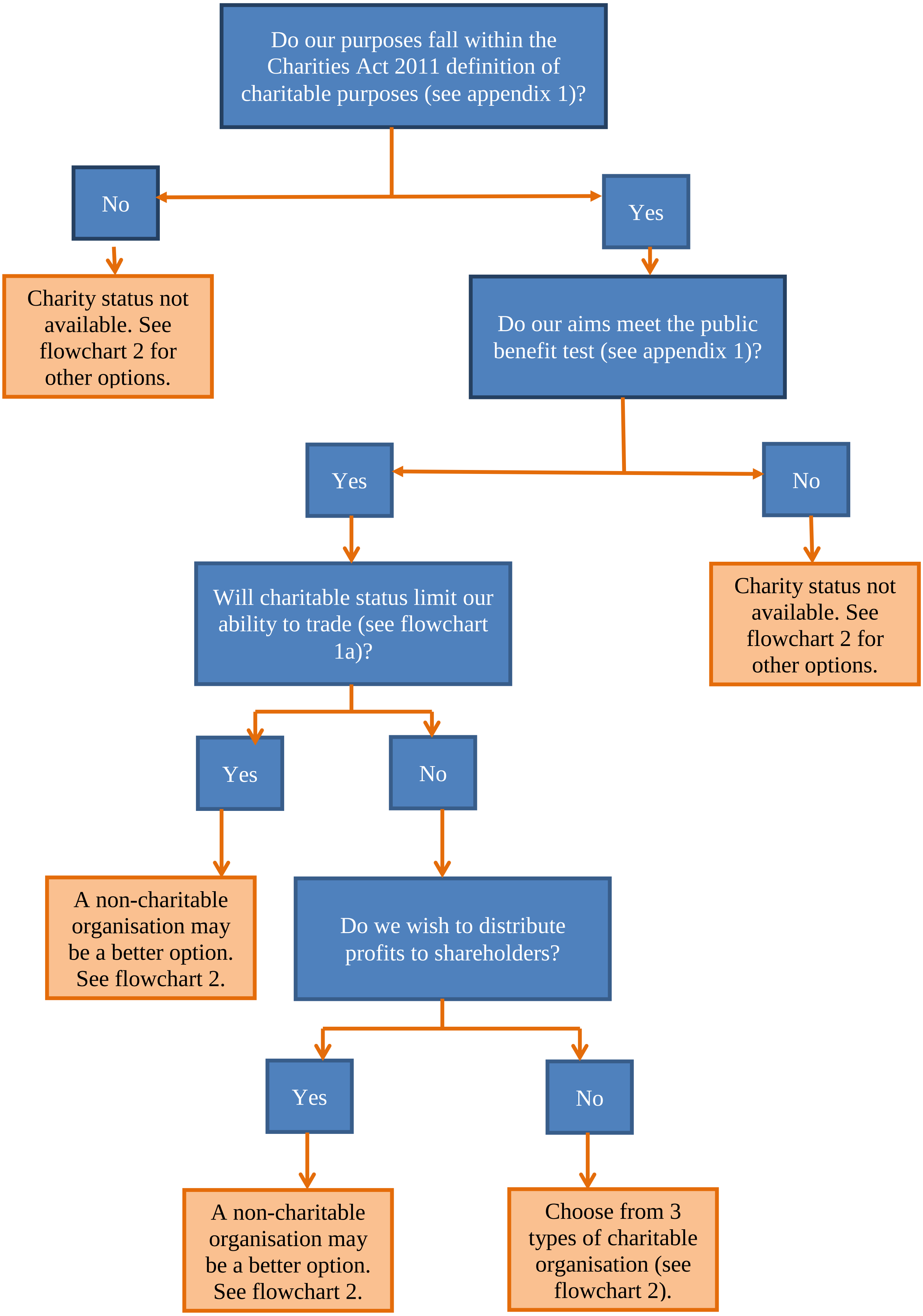
Having thought about the “function” of your local Healthwatch you are now, hopefully, in a better position to think about the appropriate legal entity, or “form” of your local Healthwatch.

The following flowcharts will help you consider the next three main questions before you can decide on an appropriate legal form.

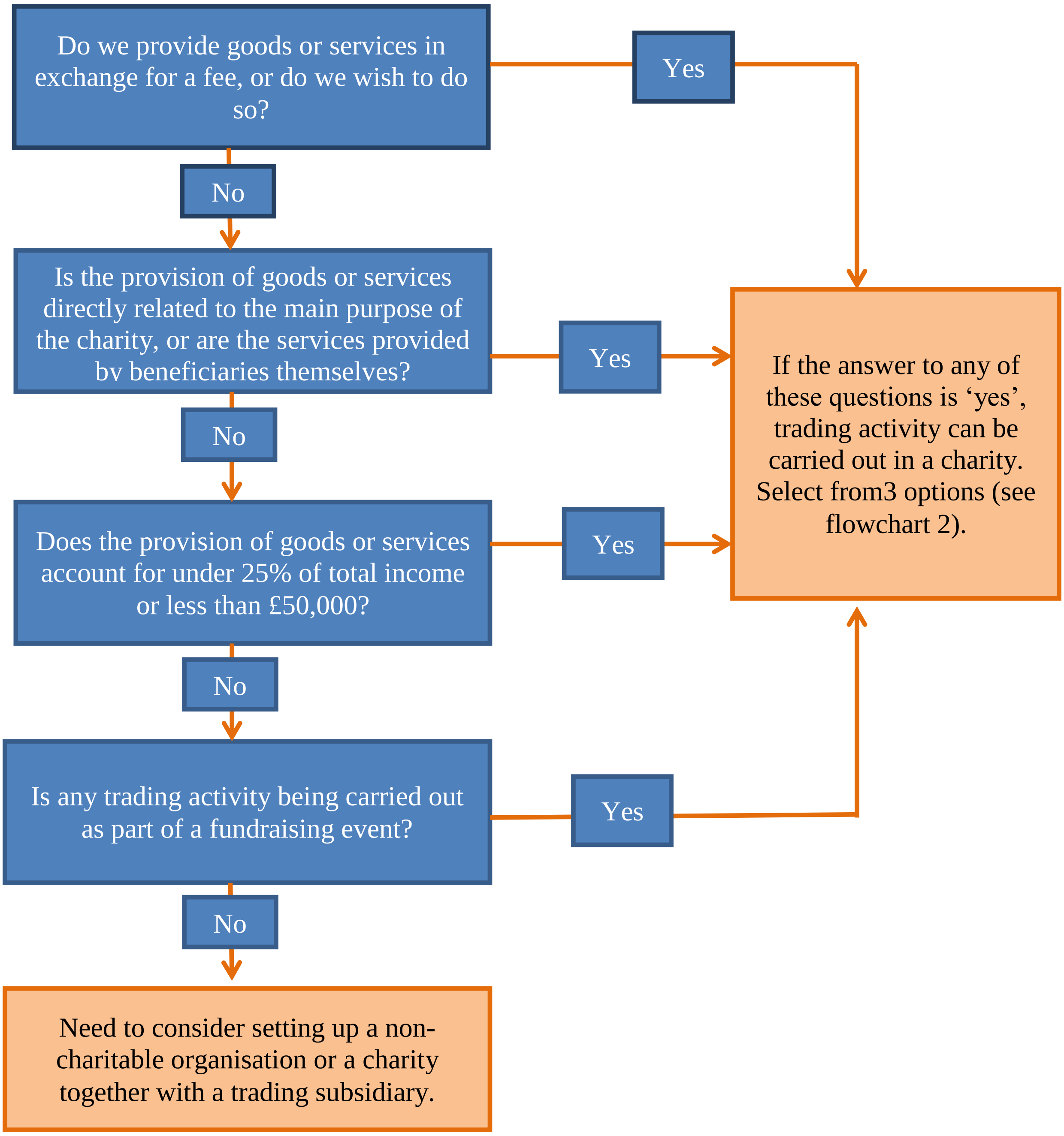
They are:

- Decision 1: Should we seek charitable status? (see flowchart 1)
- Decision 2: Can we carry out any trading activity within a charity? (see flowchart 1a)
- Decision 3: What is the best legal form for our organisation? (see flowchart 2)

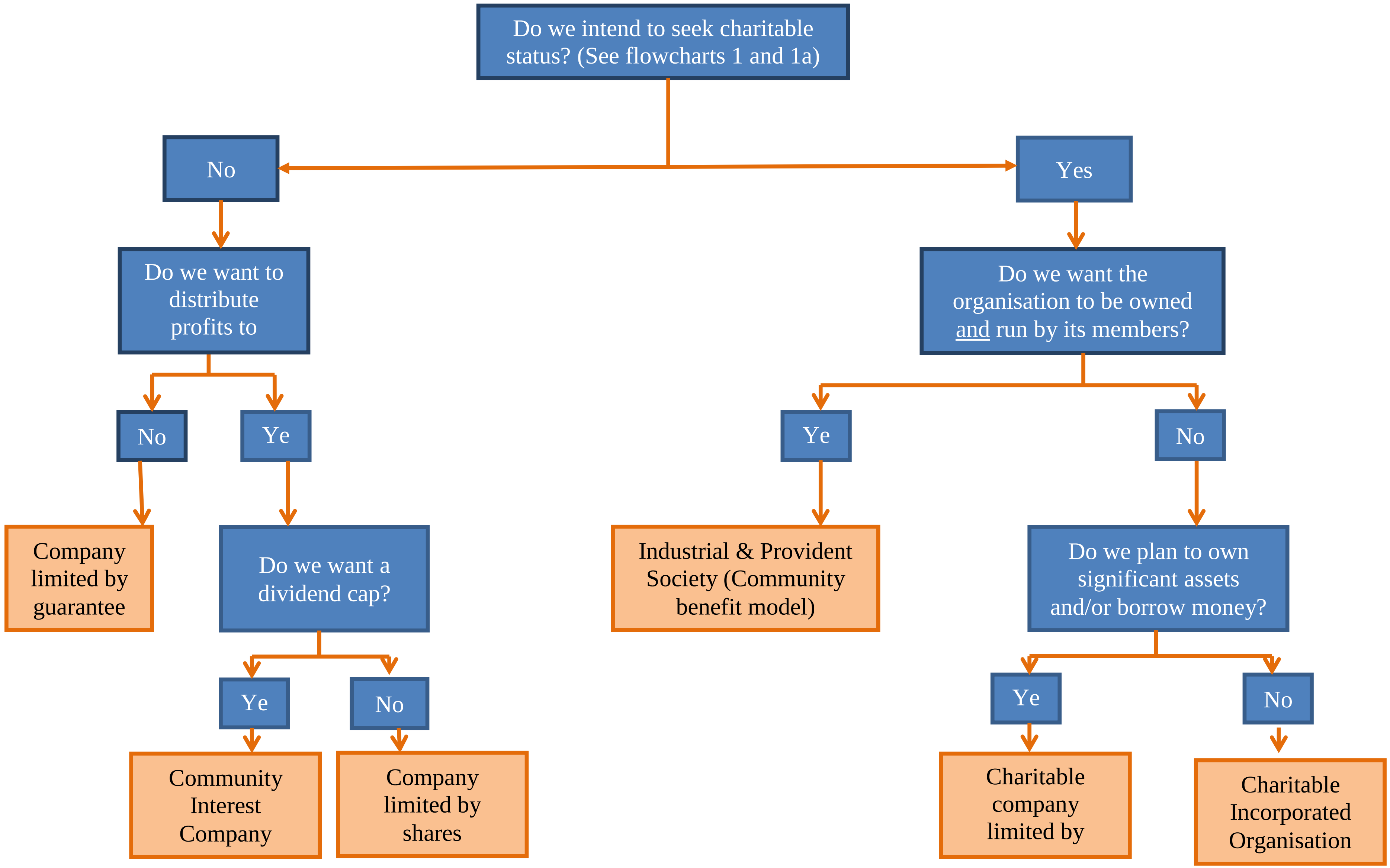
Flowchart 1: Should we seek charitable status?



Flowchart 1a: Can we carry out trading activity within a charity?



Flowchart 2: What is the best legal form for our organisation?



Legal Structures for Social Enterprises

Hopefully you will now be at a point where you have narrowed down your options. The following table provides a summary of the key features of the range of legal structures available to social enterprises. It also summarises the "pros" and "cons" of those entities with particular reference to local Healthwatch.

Legal structure	Regulator	Ownership	Governance	Profit distribution	Pros (including in relation to local Healthwatch)	Cons (including in relation to local Healthwatch)
Company Ltd by Guarantee	Companies House	Members (a company limited by guarantee can have a single member)	Board of Directors	Yes	• This is the most popular form of incorporated legal entity among social enterprises and is easily recognisable to funders and partners • Limited liability for members • Directors can be paid • Can apply for grant funding (if profits not distributed to members) • Can apply for loans, hold contracts and own property • Members of the Company (with voting rights) can be few in number or many • Offers flexibility for local Healthwatch to trade (for example, by offering consultancy on a fee paying basis) and retain profits within the organisation	• May be difficult to raise investment (if profits not distributed) • Assets are not protected with an asset lock • If the company does not also have charitable status, it may be difficult for a local Healthwatch to access some forms of funding. • The organisation may be in danger of being neither a commercial entity nor a charity, reaping the benefits of neither.
Registered Charity (company Ltd by guarantee)	Companies House and Charity Commission. The activities must fall within one or more of 12 pre-	Members	Board of Trustees (must be volunteers)	No	• Limited liability for Members • Volunteers are central to the governance of the organisation • Can make it easier to raise funds from trusts and companies • Can own property and hold contracts • May quality for a number of tax benefits • A good choice for a Healthwatch	• More active regulation in return for tax benefits • Must comply with both Companies House regulations and Charity Commission guidelines and administrative requirements • Trustees cannot be paid • Charitable rules may impact on entrepreneurial aims. For example, if a local Healthwatch wishes to

Legal structure	Regulator	Ownership	Governance	Profit distribution	Pros (including in relation to local Healthwatch)	Cons (including in relation to local Healthwatch)
	defined charitable objects which are of benefit to the community.				whose income will come primarily from charitable activities, with little income from trading	ensure its future sustainability by issuing community shares and/or developing products and activities which can be sold for a fee, then being a charity may not be the best option.
Company Ltd by Shares	Companies House	Shareholders (can have a single member/shareholder)	Board of Directors	Yes - unlimited	• Limited liability for shareholders/Directors • Good model for attracting private investors • Embeds entrepreneurial drive as shareholders benefit from the company's success • Directors can be paid • Can own property and enter into contracts in its own right • Suitable for a Healthwatch that wishes to operate as an entirely commercial entity	• Not attractive to grant funders/philanthropic donations so need to be entirely self-financing or financed through private investment • Assets are not protected with an asset lock • Probably not suitable for most local Healthwatch organisations, whose core activities could be classed as charitable and whose income is most likely to come from funders rather than investors seeking a return.
Industrial & Provident Society (co-operative model)	Financial Services Authority (FSA). The aims of the Society and governance must comply with FSA conditions.	Co-operatives are run and owned by their members, operating for the benefit of the community as well as the members. Must have at least three members.	Management Committee	No profit distribution	• Limited liability for Members • Good model for promoting democratic ownership and control and wide community of benefit • Can own property, enter into contracts, issue shares and take out loans • Attractive for a local Healthwatch that has a wide and active membership base	• Not attractive to grant funders, which may mean options for raising income are limited • FSA regulation entails a wide range of administrative requirements, which may be onerous for a smaller local Healthwatch
Community Interest Company	Companies House and CIC	Owned by the shareholders/members They can adopt the co-	Board of Directors	Yes – related to ownership	• Distinct brand for social enterprises • Combines freedom of	• CIC (limited by shares) not attractive to grant makers, therefore it may be difficult for a

Legal structure	Regulator	Ownership	Governance	Profit distribution	Pros (including in relation to local Healthwatch)	Cons (including in relation to local Healthwatch)
(CIC)	Regulator Must satisfy community interest test[21] Must adopt certain clauses in its constitution [22] Must deliver annual report	operative, not for profit or general commercial model.		structure. Can be company limited by shares or by guarantee[23]	entrepreneurial activity with protection of asset lock • Directors can be paid • Light touch CIC regulator • Can own property and enter into contracts in its own right	Healthwatch to raise philanthropic donations and grant aid • Dual regulation (Companies House and CIC Regulator) may be time consuming • Cap on dividends (asset lock) could depress demand from investors • Most suitable for a local Healthwatch that will have substantial fee income – for example from consultancy contracts – and members who are willing to invest
Charitable Incorporated Organisation (CIO)	Charity Commission	Two types: 'Foundation' style CIO, where trustees are the only members and 'Association' style, where there is a body of members	Board of Trustees	CIOs will not be allowed to distribute profits and will have their assets 'locked' (as with CICs)	• Main purpose is to reduce the burden of regulation by enabling an organisation that is both charitable and incorporated to be regulated by the Charity Commission alone	• It is slightly more difficult for a CIO than for a company limited by guarantee with charitable status to enter into contracts for substantial sums or to borrow money. This is because loan charges can be registered with Companies House for limited companies. • Only available to organisations that meet the criteria for charitable status. • A good option for a local Healthwatch that has charitable aims and will not undertake substantial trading or borrowing.

Sources of useful information and support

[21] Looks at what the underlying motivation of the company in terms of what it will do, who it will help and how, if it makes a profit, or surplus, what the company will do with it.
[22] Relating to the asset lock and preventing the CIC falling under control of non members
[23] A CIC limited by shares may pay a dividend, if agreed by a resolution of its members but dividends payable to private shareholders (non-asset locked bodies) will be subject to a dividend cap. A CIC limited by guarantee cannot distribute profits.

Social Enterprises UK
The national body for social enterprise supporting its members and helping to grow the social enterprise movement.
http://www.socialenterprise.org.uk

UnLtd.
A Comprehensive Guide to Developing Your Social Enterprise. This toolkit offers practical guidance and working models for every stage of social entrepreneurship from initial idea, setup and piloting, on to longer term sustainability, growth and replication. The toolkit is not meant to be a formal textbook; instead it aims to present the authors' experiences of supporting social entrepreneurs and the challenges and opportunities of social entrepreneurship in a structured way. The toolkit is divided into sections, each focusing on one stage of this journey. There are 3 different ways to view the toolkit, each designed to help you find what you need fast.
https://unltd.org.uk/socialentrepreneurshiptoolkit/

Co-operatives UK
The national body that campaigns for co-operation and works to promote, develop and unite co-operative enterprises.
http://www.uk.coop/

Charity Commission for England and Wales
The Charity Commission for England and Wales is the non-ministerial government department that regulates registered charities in England and Wales.
https://www.gov.uk/government/organisations/charity-commission

Guide to legal forms for social enterprise
https://www.gov.uk/government/publications/legal-forms-for-social-enterprise-a-guide

Trading Issues Made Simple
http://www.sayervincent.co.uk/Asp/uploadedFiles/File/Publications/MadeSimpleGuides/Trading_Issues_Made_Simple.pdf

Keeping it Legal – legal forms for social enterprises
https://unltd.org.uk/wp-content/uploads/2012/11/keeping-it-Legal.pdf

Appendix One: Charitable status summary of issues for consideration

If an organisation has a turnover of more than £5,000 per year and meets the criteria for charitable status, it is **obliged** to register with the Charity Commission. This does not apply to ‘exempt’ and ‘excepted’ organisations. Exempt charities are organisations that have charitable purposes, but are considered to be adequately regulated by some other body. Examples include some universities, other educational institutions and national museums. Excepted charities are those which do not have to register with the Charity Commission, for example because their income is too low, but whose activities would otherwise fall under the jurisdiction of the Commission.

To qualify for charitable status, an organisation must have a charitable purpose or ‘aims’ that are for the public benefit. Charitable purposes (or aims) are those that fall within the various descriptions of charitable purposes in the Charities Act 2006, summarised below:

- the prevention or relief of poverty
- the advancement of education
- the advancement of religion
- the advancement of health or the saving of lives
- the advancement of citizenship or community development
- the advancement of the arts, culture, heritage or science
- the advancement of amateur sport
- the advancement of human rights, conflict resolution or reconciliation or the promotion of religious or racial harmony or equality and diversity
- the advancement of environmental protection or improvement
- the relief of those in need, by reason of youth, age, ill-health, disability, financial hardship or other disadvantage
- the advancement of animal welfare
- the promotion of the efficiency of the armed forces of the Crown, or of the efficiency of the police, fire and rescue services or ambulance services
- other purposes currently recognised as charitable and any new charitable purposes which are similar to another charitable purpose.

From 1 April 2008, all organisations wishing to be recognised as charities must demonstrate, explicitly, that their aims are for the public benefit. Previously the law presumed this to be the case for charities that advance education or religion or relieve poverty. There are two key principles of public benefit and, within each principle there are some important factors that must be considered in all cases. These are:

Principle 1: There must be an identifiable benefit or benefits

- Principle 1a: it must be clear what the benefits are
- Principle 1b: the benefits must be related to the aims
- Principle 1c: benefits must be balanced against any detriment or harm

Principle 2: Benefit must be to the public, or to a section of the public

- Principle 2a: the beneficiaries must be appropriate to the aims
- Principle 2b: where benefit is to a section of the public, the opportunity to benefit must not be unreasonably restricted:
    - by geographical or other restrictions; or
    - by ability to pay any fees charged
- Principle 2c: people in poverty must not be excluded from the opportunity to benefit
- Principle 2d: any private benefits must be incidental

The principles of public benefit apply to all charities, whatever their aims. Each charity must be able to demonstrate that its aims are for the public benefit. The Charity Commission will assess whether the aims of all organisations applying to register as charities are for the public benefit.

Advantages of being a charity

The principal advantages of being a registered charity are:

- Charities do not normally have to pay income/corporation tax (in the case of some types of income), capital gains tax, or stamp duty, and gifts to charities are free of inheritance tax.
- Charities pay no more than 20% of normal business rates on the buildings which they use and occupy to further their charitable aims.
- Charities can get special VAT treatment in some circumstances.
- Charities are usually able to raise funds from the public, grant-making trusts and local government more easily than non-charitable bodies.
- Charities can formally represent and help to meet the needs of the community.
- Charities are able to give the public the assurance that they are being monitored and advised by the Charity Commission

Possible disadvantages of being a charity

A charity must have exclusively charitable aims. Some organisations may carry out their aims by a range of activities, some of them charitable, some of them not. To become a charity, this type of organisation would have to stop its non-charitable activities. (The non-charitable activities can, of course, continue if carried on by a separate non-charitable organisation.) There are limits to the extent of political or campaigning activities which a charity can take on.

Trading by charities is restricted. While charities may trade more or less freely in pursuit of their charitable objectives, there are restrictions on engaging in trades when the objective is to generate funds for the charity. In particular, charities may not engage in such commercially-oriented trades where a significant risk to their assets would be involved. Where this is the case, trading it must be undertaken by a trading subsidiary.

Trustees are not allowed to receive financial benefits from the charity which they manage unless this is specifically authorised by the governing document of the charity or by the Charity Commission. Financial benefits include salaries, services, or the awarding of business contracts to a trustee's own business from the charity. This is sometimes a problem for charities that need to attract trustees with specific commercial experience.

Application process and estimated timescale

Broadly, the process of applying to become a charity is as follows[24]:

- An organisation needs at least three trustees to form a charity. The new trustees will need to agree the objects of the new organisation. It is a good idea to obtain specialist legal advice on the drafting of objects, since it is important, for example, that the wording does not unintentionally restrict the charity's activities or prevent it from being a charity altogether.
- A governing document will need to be drafted. This should include the objects of the organisation and its 'rules of engagement', for example on election of Board members. The type of governing document required will be determined by the proposed legal status of the new organisation; for example if the organisation's corporate status is to be company limited by guarantee, its governing document will be a memorandum and articles of association. The Charity Commission has model governing documents, which may be adapted to suit the needs of the organisation, but, again, legal advice is recommended.
- The trustees will need to complete an application for registration with the Charity Commission, available on the Commission's website, and submit this together with the governing document and evidence of income, for example a letter of intention to fund.

Typically, from receipt of application to registration takes around 40 days. The process will be quicker if the organisation uses a model governing document approved by the Charity Commission.

[24] For further detail see Charity Commission guidance document CC21 *Registering a Charity*