

**Response by the Social Enterprise Coalition to the Proposed
Amendments to the Community Interest Companies Regulations
2005**

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The Social Enterprise Coalition's Response to proposed amendments to the Community Interest Companies Regulations 2005

1. The Social Enterprise Coalition (the 'Coalition') welcomes the opportunity to respond to the proposed amendments to the Community Interest Companies Regulations 2005.
2. The Coalition was established in 2002 as the national voice of social enterprise. Social enterprises are businesses with primarily social or environmental 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 owners. The Coalition represents a wide range of social enterprises, umbrella bodies and networks, with a combined membership of over 10,500 social enterprises. These include co-operatives and mutuals, housing associations, leisure and football supporters' trusts and Social Firms, as well as CICs themselves.. Social enterprises in the UK generate more than £27 billion in turnover, and contribute more than £8 billion to GDP per year.
3. In creating this response the Coalition has consulted widely with its members
4. Community Interest Companies are a new legal form of limited company to be set up for those wishing to operate for the benefit of the community rather than private owners. The 'asset lock' and cap on the distribution of profits protects the value to the company for the community and as such makes it a legal form particularly useful for social enterprises.
5. The Coalition, as the national umbrella body for social enterprise, was intimately involved in the development of the CIC legal form. Since its launch we have been monitoring its uptake, liaising with the regulator, facilitating forums and gathering evidence to understand how the legal form is working and any issues that have arisen.
6. From this process over the last 3 years the Coalition has gained an insight into the need for regulatory changes in the CIC.
7. The Coalition is aware that this consultation is the first step in a broader consultation programme for development of the CIC. The Coalition would like to share its information and work with BERR to develop the regulatory framework to meet these needs and ensure the legal form fulfils its function efficiently.

Q1. Do you agree with the draft amendments to recognise the asset lock form of community benefit society?

8. Community benefit societies are a type of Industrial and Provident Society, a longstanding part of the social enterprise movement. For a considerable amount of time this legal form has been used to operate services and hold assets on behalf of communities.
9. Previously the asset lock form of community benefit society did not exist, and therefore offered less protection for assets for community interest. The Coalition approved of limiting the ability of CICs to transfer assets to community benefit society because of this discrepancy in the level of protection for the community interest.
10. With the regulatory changes to allow for asset locks to be instituted in community benefit societies this discrepancy has been removed. The Coalition therefore agrees with the amendment to recognise the asset lock form of community benefit society and to subsequently allow asset transfer to these organisations.

Q2. Do you agree with the proposed amendments to allow a Scottish charitable company to convert to a CIC?

11. The Coalition agrees with the amendment to allow a Scottish charitable company to convert to a CIC.

Q3 Do you agree that adding a reasonable persons test to Regulation 5 will help to clarify the purpose of the community interest test? If so, will it help ensure it excludes those for whom the form was not designed?

12. The purpose of the community interest test is to ensure the CIC is serving the needs and interest of the community. The Coalition recognises that Regulations 4 and 5 are purposefully broad to ensure that there is no exclusion of good causes in definitions of 'benefit for the community' and 'section of community'.
13. Although recognising the need to keep the definition as broad as possible, the Coalition agrees that regulation 5 is loose and could allow arbitrary inclusion of beneficiaries who share very little with the 'community'.
14. Reasonable person tests are acknowledged as a more selective approach to identifying communities, without prejudicing the breadth of potential activities for CICs to engage with. This is because the need for an 'average' person to recognise the 'community' is already contained within the regulations so the reasonable person test is merely a process to clarify the interpretation of the 'section of the community'. As a result the Coalition agrees with the amendment to Regulation 5 to include a reasonable persons test.

Q4. Do you agree that the Regulator should take account of the impact of a prospective CIC's activities on the wider community and public policy considerations? Will the proposed amendment help the Regulator to interpret more clearly the meaning of community interest?

15. It is a reasonable conclusion that the activities of some CICs will come to be considered a detriment to the wider community or public policy considerations. An example of such an activity is a CIC used as a vehicle for a community owned wind farm that is objected to by members of the wider community on the basis of the wind turbines ruining the scenic beauty of an area or detrimentally affecting wildlife habitats.
16. The Coalition recognises that the community interest test does not take into account these potential conflicts of interest between differing sections of the community. Regulation 5 itself is not prescriptive but allows for 'sections of the community' in the broadest sense to ensure there is no predetermination of what a 'community' is.
17. Conflicts of interest between different parties, such as between, or within, communities over ownership of assets or detriment caused by activities, are not unknown and are not restricted to community interest companies, but apply to all organisational legal forms. At present these conflicts are decided ultimately by the arbitration role of the civil courts of the UK.
18. Equally, communities also offer solutions and activities that do run counter to public policy, through failure of infrastructure and services to differing degrees for those communities. Although on occasion this has led to legal action, a fundamental role of community based activities is to deliver services and activities for the benefit of communities that have been failed by public policy solutions.

19. This amendment would require the regulator, in considering potential detriment to the wider community, to make a pre-emptive judgement based on evidence from conflicting parties in a dispute. This will make the regulator, in some cases, act as an arbitrator of what projects and activities should go ahead. This will fundamentally change the role of the regulator to that of an arbitrator and is a different and inappropriate regulatory framework to that originally envisaged for CICs.
20. Consideration of any detrimental impact on public policy would equally place the Regulator as arbitrator of whether there is a detrimental action by the CIC, but the regulator would have to assess the potential positive and negative implications of the public policy to ensure the decision is fair and proportionately weighted.
21. The Coalition believes that this amendment will fundamentally change the basis by which the regulator acts from that of confirming community interest to defining what community interest should be within the alternative presented. This is not only best done through the civil courts, but will also drastically increase the required resources needed for specific decisions and is beyond the intended remit of the regulator. Therefore the Coalition disagrees with the need for this amendment.

Q5. Do you agree with the widening of the definition of governmental authority?

22. The Coalition believes that it is essential that the CIC is not used for political activity considered for the benefit of government authorities, political parties or political campaigning groups. This does not restrict members of CICs from describing, assessing or commenting on the public policy environment in terms of how it impacts upon CICs.
23. The proposed amendment for extending the definition of government authority to include several international authorities is proportionate and appropriate to ensure that the CIC form is not used as a vehicle for political activity. It does not change the present restrictions except to include government and supra-government authorities within the definition. The Coalition supports this amendment.

Q6. Do you agree with the aim of permitting relevant public authority or regulatory bodies to seek distribution of residual asset of a CIC subsidiary on winding up?

24. There is some evidence of developing relationships between public authorities and CICs set up to externalise services. This should involve investment from public authorities but is attractive because of the organisational independence of CICs to deliver services on behalf of communities
25. The Coalition believes that this amendment could lead to a changing relationship between public authorities and CICs, detrimentally affecting the contractual conditions placed on CICs delivering public services and subsequently how CICs operate as independent organizations. The Coalition would like to see a greater level of detail on how this would be managed and assessed, and on the potential implications, before deciding whether to support this amendment.
26. The Coalition is willing to work with the CIC regulator and BERR to develop a regulatory framework that ensures the independence CICs, while encouraging positive investment and relationships with public authorities.

Q7. Do you consider the current provisions create inconsistency? If so, how would you propose we should deal with this.

27. The identified inconsistency occurs is when the assets of a CIC are being transferred at less than full consideration. If transferred to a non-asset locked body then the regulator needs to give prior consent, and therefore is intervening in the winding up of the CIC (clause 15b). If assets are transferred to an asset locked body then the regulator does not need to give prior consent, and there is no intervention by the regulator (clause 15a).
28. The need for a company form that has provisions to ensure it operates for the benefit of the community is a tacit recognition of a need for a more interventionist approach than present company regulation. Therefore the limited interventionist provisions within the CIC regulations are not an inconsistency with a light touch regulator, considering the CIC is there to ensure protections for the interest of communities.
29. The amendment would remove the requirement for the regulator to agree the director's decisions ensuring good value for assets that are being removed from asset lock. There is no provision for how these assets would be returned, or the value recompensed, should the regulator disagree with the director's decisions post-transfer.
30. There is evidence where asset stripping has been undertaken by directors in traditional company forms prior to transfer of the asset to communities, such as with football clubs. There is little test case evidence of how it would be possible to return the asset post-transfer. Therefore the CIC would not be offering any more protections against determined attempts at obtaining assets in any other company form.
31. The Coalition disagrees with the proposed amendment to follow 15(a) and remove the regulators consent prior to transfer of assts to a non asset locked body, as this would undermine the protections afforded in the CIC form.

Q8. Do you agree with the proposal to remove the provisions on appointment and removal of directors?

32. The Coalition recognizes the need for flexible management for companies to ensure sustainability but we are unsure whether this provision will strengthen the potential to innovate at a cost of weakening links with members and communities. Therefore we would like further detail and evidence on what the need for this amendment is, and what the likely effects would be.

Q9. Do you agree with our intention to leave the provision on alternate directors on the basis it does not impose any requirement on CICs

33. The Coalition agrees that these provisions do not add any further requirements on CICs so the provisions should remain as they stand.

Q10. Do you agree with the proposal to remove the provision on a casting vote?

34. The Coalition proposes to agree with this amendment to bring it in line with company law and promote equivalent management practice between social enterprise and traditional businesses