Law Commission
Reforming the law

Review of the Co-operative and Community Benefit Societies Act 2014

Consultation paper

Consultation Paper 264

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September 2024

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THE LAW COMMISSION – HOW WE CONSULT

About the Law Commission: The Law Commission was set up by section 1 of the Law Commissions Act 1965 for the purpose of promoting the reform of the law. The Law Commissioners are: Sir Peter Fraser, Chair, Professor Nicholas Hopkins, Professor Penney Lewis, and Professor Alison Young. Professor Sarah Green was also a Commissioner when this paper was approved for publication. The Chief Executives are Joanna Otterburn and Roshnee Patel.

Topic of this consultation: Proposals to reform the Co-operative and Community Benefit Societies Act 2014.

Geographical Scope: This consultation applies to the law of England and Wales.

Duration of the consultation: The consultation period is open until 23.59 on Tuesday 10 December 2024.

Responses to the consultation may be submitted using an online form at: https://consult.justice.gov.uk/law-commission/coops. Where possible, it would be helpful if this form was used.

Alternatively, comments may be sent:

By email to coops@lawcommission.gov.uk

OR

By post to Commercial and Common Law Team (Coops), Law Commission, 1st Floor, Tower, 52 Queen Anne's Gate, London, SW1H 9AG.

If you send your comments by post, it would be helpful if, whenever possible, you could also send them by email.

Availability of materials: This consultation paper is available on our website at https://lawcom.gov.uk/project/co-operatives-and-community-benefit-societies/.

We are committed to providing accessible publications. If you require this consultation paper to be made available in a different format, please email coops@lawcommission.gov.uk or call 020 3334 0200.

After the consultation: We will analyse the responses received and undertake further stakeholder engagement as appropriate. We will publish a report of our final recommendations for law reform. It will be for HM Treasury, along with other interested departments, to decide whether to implement any recommendations.

Consultation Principles: The Law Commission follows the Consultation Principles set out by the Cabinet Office, which provide guidance on type and scale of consultation, duration, timing, accessibility and transparency. The Principles are available on the Cabinet Office website at: https://www.gov.uk/government/publications/consultation-principles-guidance.

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ABBREVIATIONS

Adderley	I Adderley, *Co-operatives: linking theory and practice* (forthcoming)
Asset Lock Regulations	The Community Benefit Societies (Restriction on Use of Assets) Regulations 2006 (SI 2006 No 264)
CCBS Act	Co-operative and Community Benefit Societies Act 2014
CCBS Handbook	I Snaith (ed), *Handbook of Co-operative and Community Benefit Society Law* (2nd edn 2014)
FCA	Financial Conduct Authority
FCA Guide	Financial Conduct Authority, *Registration Function under the Co-operative and Community Benefit Societies Act 2014 Guide* (May 2023) https://www.handbook.fca.org.uk/handbook/RFCCBS.pdf
FSMA	Financial Services and Markets Act 2000
ICA	International Cooperative Alliance
ICA Guidance Notes	ICA, *Guidance Notes on the Co-operative Principles* (2015)
ILO	International Labour Organisation
OSCR	Office of the Scottish Charity Regulator
PECOL	G Fajardo and others, *Principles of European Cooperative Law* (2017)
PRA	Prudential Regulation Authority
Sensitive Words Regulations	Company, Limited Liability Partnership and Business Names (Sensitive Words and Expressions) Regulations 2014 (SI 2014 No 3140)
UN	United Nations

Chapter 1: Introduction

1.1 Co-operatives and community benefit societies are business associations. They are alternatives, for example, to companies and partnerships.

1.2 Co-operatives are associations of consumers, producers, workers, or a mixture (called multi-stakeholder). Part of their purpose is to harness economies of scale. For example, when producers or workers combine as members of a co-operative, the co-operative might command better prices in the market for the produce or labour. When consumers combine as members of a co-operative, the co-operative might access cheaper prices for goods or services. The co-operative can then pass on those better prices when selling to its consumers, buying from its producers, or paying its workers.

1.3 Co-operatives UK represents co-operatives and community benefit societies. It reports that there are more than 7000 co-operatives in the UK, with around 14 million members, contributing about £40 billion to the economy.[1] A visible example on the high street is the Co-op chain of supermarkets.

1.4 A community benefit society carries on business for the benefit of the community. They can engage in a range of activities, from owning a local pub, through publishing a newspaper or developing a local renewable energy network, to providing social housing.

1.5 Co-operative and community benefit societies register under the Co-operative and Community Benefit Societies Act 2014 (CCBS Act), and are listed on the Mutuals Public Register. The registrar is the Financial Conduct Authority (FCA).

1.6 We have been asked to review the CCBS Act, to ensure that the governing law is fitting to the nature and needs of these societies, and that their regulation is proportionate and effective. The CCBS Act itself consolidated the law, but in some areas that law is over a century old. Stakeholders have repeatedly told us that modernisation of society law is long overdue, and this is a view which has been repeated in Parliament.

1.7 In this consultation paper, we explain the current legal framework and make provisional proposals for ways that the law could be improved. We ask consultees for their views on these proposals. We have also published a shorter summary document, available on our website.[2]

ABOUT THIS PROJECT

1.8 In June 2023, we were asked by HM Treasury to review the CCBS Act. Our full terms of reference are set out in Appendix 1. They include the following.

> The aim of the project is to identify changes to the legislative framework for co-operatives and community benefit societies which would modernise the law,

1 https://www.uk.coop/understanding-co-ops/what-co-op/quick-facts-about-co-ops.

2 https://lawcom.gov.uk/project/co-operatives-and-community-benefit-societies/.

proportionally reduce barriers/costs to operation for these societies, and support a more proportionate and effective regulatory environment – aligning as appropriate with relevant Acts which have updated in more recent years.

In particular, the Law Commission is to consider whether reform is warranted to ensure that:

(1) the governing law is fitting to the nature and needs of co-operatives and community benefit societies, identifying necessary updates to the legislation based on other modernisations; and

(2) the regulation is proportionate and effective.

1.9 We began this project in September 2023. We have spoken with a range of stakeholders, listed in Appendix 2, to hear what reform they think is needed. We have carried out our own research and analysis, and we now publish this consultation paper which sets out provisional proposals for law reform. The consultation period will be open until 23.59 on Tuesday 10 December 2024.

1.10 Once the consultation period has closed, we will consider all responses, and carry out further research and analysis as necessary. We will then publish our final report, which will include our final recommendations for law reform. It is for Government to decide whether to accept our recommendations.

1.11 We are also carrying out a separate review of friendly societies under the Friendly Societies Acts 1974 and 1992.[3]

TERRITORIAL EXTENT

1.12 The CCBS Act extends[4] to England and Wales, and to Scotland – but with different provision in those two jurisdictions in the matter of floating charges,[5] and mortgages.[6] Matters governed by the CCBS Act are reserved to Westminster; they are not devolved to the Welsh Senedd,[7] or the Scottish Parliament.[8]

1.13 The CCBS Act also extends to Northern Ireland, but only in the following respects. First, societies registered in Northern Ireland can choose to register under the CCBS

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3 For more information see the project page at https://lawcom.gov.uk/project/friendly-societies/.

4 CCBS Act, s 153.

5 CCBS Act, Pt 5.

6 CCBS Act, ss 71 to 73.

7 Under the Government of Wales Act 2006, an Act of the Senedd is not law if outside its legislative competence. Reserved matters are outside its competence: s 108A. Reserved matters include the creation, operation, regulation and dissolution of types of business association: sch 7A § C1.

8 Under the Scotland Act 1998, reserved matters are outside the legislative competence of the Scottish Parliament: s 29(2). Reserved matters include the creation, operation, regulation and dissolution of types of business association: Scotland Act 1998, s 30, sch 5 s C1. “Business association” means any person (other than an individual) established for the purpose of carrying on any kind of business, whether or not for profit; and “business” includes the provision of benefits to the members of an association. All this is with the exception of charities.

Act.[9] Second, the CCBS Act gives HM Treasury power to amend legislation to assimilate some specified aspects of company law, and that power extends to amending equivalent Northern Ireland legislation as well.[10]

1.14 More generally, as the Law Commission of England and Wales, we can only recommend reform to the law of England and Wales. However, Government may decide that reform should extend to Scotland too. We encourage Scottish stakeholders to respond to our consultation paper. In particular, we ask whether there are any factors unique to Scotland which ought to be flagged and encourage consultees to reference any Scottish-specific points in their response to each question. We ask this question again at the end of this paper.

Channel Islands[11]

1.15 The following Acts extended to the Channel Islands: Industrial and Provident Societies Act 1965,[12] Industrial and Provident Societies Act 1975,[13] and Industrial and Provident Societies Act 1978.[14] The CCBS Act repealed these Acts,[15] except that the repeal only extended to the United Kingdom (that is, England, Wales, Scotland, and Northern Ireland, but not the Channel Islands).[16] We think that those Acts therefore continue in force in the Channel Islands. The CCBS Act provides that it may be extended by Order in Council to the Channel Islands,[17] but no such Order in Council has been made.

1.16 It may be fitting that any reform of society law be extended to the Channel Islands, but that is not something on which we could take a view. Again, we encourage stakeholders from the Channel Islands to respond to our consultation paper so that we can record views on this issue. In particular, we ask whether there are any factors unique to the Channel Islands which ought to be flagged. We ask this question again at the end of this paper.

Housing associations

1.17 Housing associations can register as societies under the CCBS Act. We note the following divergence of regimes.

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9 CCBS Act, s 142.

10 CCBS Act, ss 135, 136 and 147.

11 We gratefully acknowledge the assistance here of the Privy Council Office and the Crown Dependencies Team.

12 Industrial and Provident Societies Act 1965, s 78(2). The Act was modified in its application to the Channel Islands: s 75; Industrial and Provident Societies (Channel Islands) Order 1965 (SI 1965 No 2165).

13 Industrial and Provident Societies Act 1975, s 3(5).

14 Industrial and Provident Societies Act, s 3(4).

15 CCBS Act, s 151(4) and sch 7.

16 CCBS Act, s 153(5).

17 CCBS Act, s 152.

1.18 In England, societies can register with the Regulator of Social Housing.[18] Regulation is governed by the Housing and Regeneration Act 2008. Registration is optional, but many housing societies choose to register as a mark of quality assurance. In Wales, regulation is provided by Welsh Ministers' Housing Regulation Team,[19] under the Housing Act 1996. In Scotland, there is the Scottish Housing Regulator,[20] and the governing legislation is the Housing (Scotland) Act 2010.

HOW TO RESPOND TO THIS CONSULTATION

1.19 In this consultation paper, we set out all the possible reforms which we have identified or which have been suggested to us. We discuss each one, and make provisional proposals. Throughout, we ask consultees whether they agree with our proposals.

1.20 Our proposals are provisional. They can and do change depending on what we are told by consultees. Also, if there is any possible reform that is not included in this paper, which consultees think we should consider, please tell us. We will ask this question again at the end.

1.21 We would prefer if possible if consultees could complete the on-line return. It can be found here: https://consult.justice.gov.uk/law-commission/coops.

1.22 Alternatively, consultees can respond to this consultation by sending us an email at: coops@lawcommission.gov.uk, or by writing to us at: Commercial and Common Law Team (Coops), Law Commission, 1st Floor, Tower, 52 Queen Anne's Gate, London, SW1H 9AG.

1.23 The law of co-operatives and community benefit societies has not been reviewed in a very long time. As a result, there are many possible reforms to consider. Consultees do not have to answer every question – you can answer only those questions where you have a view. But we do encourage consultees to answer as many questions as possible.

1.24 It is also important for us to know how reform might affect consultees (positively or negatively). When answering a question, please tell us, where possible, what effect that specific reform might have on you. There will also be an overall question about impact at the end.

1.25 We encourage consultees to read this consultation paper before answering the consultation questions on-line. We have also published a summary of this paper, in English and in Welsh, available on our webpage at: https://lawcom.gov.uk/project/co-operatives-and-community-benefit-societies/.

STRUCTURE OF THIS PAPER

1.26 This consultation paper comprises nine further chapters.

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18 https://www.gov.uk/government/organisations/regulator-of-social-housing.

19 https://www.gov.wales/sites/default/files/publications/2022-01/regulatory-framework-for-housing-associations-registered-in-wales.pdf.

20 https://www.scottishhousingregulator.gov.uk/.

(1) Chapter 2 introduces co-operative and community benefit societies and their legislative framework.

(2) Chapter 3 discusses whether there should be a new statutory definition of a co-operative. We provisionally propose that there should be a new definition with the following ingredients: a society for carrying on any business mainly for the benefit of its members through transactions with its members; membership is voluntary and open to all, with one vote per member.

(3) Chapter 4 discusses whether there should be a new statutory definition of a community benefit society. We provisionally propose that there should be a new definition with the following ingredients: a society for carrying on any business solely for the benefit of the community; membership is voluntary and open to all, with one vote per member. We also propose that charitable community benefit societies should cease to be exempt charities.

(4) Chapter 5 considers society shares. We conclude that the CCBS Act allows societies to issue shares which are withdrawable, non-withdrawable, transferable, and non-transferable, to user members and to non-user investors, with different rates of return if desired. We provisionally propose new rules to regulate withdrawal and transfer of shares, changes to class rights, and writing down shares. We provisionally propose that any rate of interest paid on shares should be no more than is necessary to obtain funding, and even then no more than a reasonable rate. We discuss whether any new type of share is needed.

(5) Chapter 6 is concerned with officers of a society. We provisionally propose that the Mutuals Public Register should have a list of society officers, and that a society must notify the registrar of any updates. We discuss what information should be published on a society's list of members and officers. We provisionally propose that the CCBS Act adopt for society officers the duties owed in company law by company directors.

(6) Chapter 7 discusses all those other suggestions by stakeholders where we provisionally propose reform. This is a long chapter – which is not surprising, given the long passage of time since society law was last reviewed. Topics include: a right to appeal decisions of the registrar; suspension and cancellation of a society's registration; entrenchment of society rules; asset locks; conversion, amalgamation, and transfer of engagements; powers of the registrar; audits; executing documents; society names; online meetings; changes to society rules; and indivisible reserves.

(7) Chapter 8 discusses all the remaining suggestions so far received from stakeholders where we do not currently propose any reform.

(8) Chapter 9 contains a few final questions for consultees, including those questions relating to Scotland and the Channel Islands mentioned in this chapter.

(9) Chapter 10 gathers together in one place all the consultation questions asked throughout this paper.

1.27 This consultation paper also has the following appendices.

(1) Appendix 1 sets out our Terms of Reference.

(2) Appendix 2 lists all the stakeholders we have spoken with prior to publishing this consultation paper.

(3) Appendix 3 reproduces historic guidance issued by the Registry of Friendly Societies (as discussed in Chapter 3).

(4) Appendix 4 sets out passages from historic legislation which concern shares in societies (as discussed in Chapter 5).

(5) Appendix 5 sets out the duties owed by company directors under the Companies Act 2006 (as discussed in Chapter 6).

PROJECT TEAM

1.28 The following members of the Commercial and Common Law team have contributed to this report: Laura Burgoyne (team manager), Nathan Tamblyn (lawyer), Matthew Parish (research assistant).

Chapter 2: An introduction to societies

2.1 In this chapter, we introduce co-operatives and community benefit societies. We provide a summary of the legislative framework, and we introduce the role of the registrar. We also introduce other forms of organisation whose law is a source of comparison throughout this paper: companies, charities, partnerships, and unincorporated associations. This chapter does not contain any proposals for law reform.

ABOUT CO-OPERATIVES

2.2 The earliest documented co-operative is perhaps the Fenwick Weavers' Society. Its foundation charter, now in the National Library of Scotland,[21] was signed in 1761. It sought to provide its members with mutual support, and to obtain a fair price for their work. Later it sold food, ran a library, and made loans.

2.3 The Rochdale Equitable Pioneers Society was founded in 1844.[22] Members pooled their funds with the society, which bought food at bulk prices. It could then re-sell the food to members, passing on those affordable prices. The group agreed a set of principles to govern their organisation. These principles became the blueprint for the modern co-operative movement (see below).

2.4 Today, co-operatives tend to be associations of consumers, producers, workers, or a mixture (called multi-stakeholder).[23] Part of their purpose is to harness economies of scale. For example, when producers or workers combine as members of a co-operative, the co-operative might command better prices in the market for the produce or labour. When consumers combine as members of a co-operative, the co-operative might access cheaper prices for goods or services. The co-operative can then pass on those better prices when selling to its consumers, buying from its producers, or paying its workers.

2.5 At the end of a year, if the co-operative has a trading surplus, that might be re-invested in the co-operative, or distributed to members as a dividend in proportion to their transactions with the co-operative. This is not a share of profits, but a price adjustment. In effect, for consumers, it is a refund, and for producers and workers, it is a final balance, on what were provisional charges or payments.[24] In contrast, for example, a private company would usually seek to make a profit on its transactions, with that profit taken out of the business to reward investors in the form of dividends.

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21 https://www.nls.uk/learning-zone/politics-and-society/labour-history/fenwick-weavers/.

22 There were several co-operatives founded in Rochdale, following a scandal whereby "a certain Savings Bank manager died in high reputation, taking with him the guilty secret that he had purloined [£]71,717 of the funds of the Rochdale Savings Bank, of which he had been actuary": E W Brabrook, *The Law Relating to Industrial and Provident Societies* (1869) p xiii.

23 For example, see: ILO, *Measuring Cooperatives* (2022) p 12; PECOL, r 1.1.

24 For example, see: ICA, *The Capital Conundrum for Co-operatives* (2017) pp 15, 26; PECOL, p 85; Community Shares Handbook, para 8.2.

2.6 Co-operatives might provide other benefits too. For example, in a worker co-operative, the workers are employees of the co-operative, which might confer advantages over being self-employed, such as sick pay or annual leave. Also, in creating a co-operative, members have a say in shaping the environment or moral ethos in which they work or produce or consume.

2.7 A distinction is sometimes drawn between primary and secondary co-operatives. Primary co-operatives usually have members who are individuals; secondary co-operatives have members who are co-operatives. In this way, secondary co-operatives are like federations of co-operatives.[25] For example, housing co-operatives might create a secondary co-operative to provide shared maintenance services; agricultural co-operatives might create a secondary co-operative to buy fertiliser.

2.8 Some secondary co-operatives are trade bodies that advocate on behalf of the sector. Co-operatives UK is a secondary co-operative: it is the representative body for co-operatives in the UK, representing and assisting British co-operatives. It also represents community benefit societies (we introduce community benefit societies below).

2.9 According to Co-operatives UK, there are more than 7000 co-operatives in the UK, with around 14 million members, contributing about £40 billion to the economy.[26] It reports that co-operatives can be resilient, with 72% of co-operatives in the UK surviving the first five years of business, compared to 42% of companies.[27] It reports that, during Covid in 2020, 1.5% of co-operatives were dissolved compared to 6.5% of businesses generally, while the number of independent co-operatives grew, and turnover for all co-operatives increased.[28] During a downturn, co-operatives may be more likely to focus on preserving jobs than other businesses.[29]

2.10 The International Cooperative Alliance (ICA) is a global body that represents and assists co-operatives worldwide. It has more than 310 member organisations (including Co-operatives UK) from 107 countries.[30] It was founded in London in 1895 and is now headquartered in Brussels. It reports that there are around 3 million co-operatives worldwide, with around 1 billion members, employing around 10% of the

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25 Hagen, H, *Guidelines for Cooperative Legislation* (3rd ed 2012) p 100.

26 https://www.uk.coop/understanding-co-ops/what-co-op/quick-facts-about-co-ops.

27 https://www.uk.coop/understanding-co-ops/what-co-op/quick-facts-about-co-ops. On resilience, see further: H Hagen, *Guidelines for Cooperative Legislation* (ILO, 3rd ed 2012) pp 22 to 24; J Birchall, *Resilience in a Downturn: The power of financial cooperatives* (ILO, 2013); J Birchall and L Hammond Ketilson, *Resilience of the Cooperative Business Model in Times of Crisis* (ILO, 2009).

28 https://www.uk.coop/get-involved/awareness-campaigns/co-op-economy.

29 V Perotin, *What do we really know about worker co-operatives?* (2018), available at: https://www.uk.coop/resources/what-do-we-really-know-about-worker-co-operatives.

30 https://www.ica.coop/en/about-us/our-members/global-cooperative-network.

global workforce.[31] The largest 300 co-operatives generate an annual turnover of over US$2 trillion.[32]

2.11 The International Labour Organisation (ILO) and the United Nations (UN) also promote support for co-operatives.

2.12 The ILO, now headquartered in Geneva, was created in 1919 as part of the Treaty of Versailles at the end of the First World War. It calls itself a tripartite organisation, bringing together representatives of governments, employers, and workers. Its Cooperatives Unit was set up in 1920, whose current activities are guided by its Promotion of Cooperatives Recommendation 2002 (No 193).[33] This calls on governments to create a policy and legal framework supportive of co-operatives. The ILO also produces guidelines on how to draft legislation to regulate co-operatives.[34]

2.13 In 2023, the UN's General Assembly adopted a resolution encouraging member nations to promote policies to encourage and support the social and solidarity economy as a model for sustainable economic and social development.[35] This followed an earlier resolution in 2022 which encouraged governments to strengthen and build the capacity of co-operatives as a form of sustainable and equitable business organisation.[36] The UN had previously declared 2012 as the International Year of Co-operatives. The International Day of Co-operatives is the first Saturday in July each year.

A note on terminology

2.14 Note that "co-operative" (with a hyphen) and "cooperative" (without a hyphen) are both in use. Throughout this paper, we use the word "co-operative", which is the word used in the CCBS Act – except that we use "cooperative" when that spelling is used in a name.

Co-operative identity

2.15 The ICA describes itself as the steward of the Statement on the Co-operative Identity.[37] The ICA is currently consulting on whether the Statement needs updating. For now, the Statement includes the following.

2.16 First, there is a definition of a co-operative:

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31 https://www.ica.coop/en/cooperatives/facts-and-figures.

32 World Cooperative Monitor 2022, p 13, available at: https://monitor.coop/en/media/library/research-and-reviews/world-cooperative-monitor-2022.

33 https://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO::P12100_ILO_CODE:R193.

34 https://www.ilo.org/empent/Publications/WCMS_195533/lang--en/index.htm.

35 A/77/L.60 (27 March 2023).

36 A/RES/67/135 (5 January 2022). See too the 2001 guidelines aimed at creating a supportive environment for the development of cooperatives: A/56/73.

37 https://www.ica.coop/en/whats-co-op/co-operative-identity-values-principles.

A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise.

2.17 Second, there are "Co-operative Values":

Co-operatives are based on the values of self-help, self-responsibility, democracy, equality, equity, and solidarity. In the tradition of their founders, co-operative members believe in the ethical values of honesty, openness, social responsibility and caring for others.

2.18 Third, there are "Co-operative Principles". These are "guidelines by which co-operatives put their values into practice", and come with additional and extensive guidance notes.[38] The Co-operative Principles are:

(1) **Voluntary and Open Membership**. Co-operatives[39] are voluntary organisations, open to all persons able to use their services and willing to accept the responsibilities of membership, without gender, social, racial, political or religious discrimination.

(2) **Democratic Member Control**. Co-operatives are democratic organisations controlled by their members, who actively participate in setting their policies and making decisions. Those serving as elected representatives are accountable to the membership. In primary co-operatives members have equal voting rights (one member, one vote) and co-operatives at other levels are also organised in a democratic manner.

(3) **Member Economic Participation**. Members contribute equitably to, and democratically control, the capital of their co-operative. At least part of that capital is usually the common property of the co-operative. Members usually receive limited compensation, if any, on capital subscribed as a condition of membership. Members allocate surpluses for any or all of the following purposes: developing their co-operative, possibly by setting up reserves, part of which at least would be indivisible; benefiting members in proportion to their transactions with the co-operative; and supporting other activities approved by the membership.

(4) **Autonomy and Independence**. Co-operatives are autonomous, self-help organisations controlled by their members. If they enter into agreements with other organisations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their co-operative autonomy.

(5) **Education, Training, and Information**. Co-operatives provide education and training for their members, elected representatives, managers, and employees so they can contribute effectively to the development of their co-operatives.

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[38] https://ica.coop/en/media/library/the-guidance-notes-on-the-co-operative-principles.

[39] The dominant English spelling is with a hyphen: "co-operatives". But spelling without the hyphen is also common and acceptable, and is used, for example, by the ICA.

They inform the general public – particularly young people and opinion leaders – about the nature and benefits of co-operation.

(6) **Co-operation among Co-operatives**. Co-operatives serve their members most effectively and strengthen the co-operative movement by working together through local, national, regional and international structures.

(7) **Concern for Community**. Co-operatives work for the sustainable development of their communities through policies approved by their members.

ABOUT COMMUNITY BENEFIT SOCIETIES

2.19 There is no statutory definition of a community benefit society. For registration under the CCBS, the FCA must be satisfied that:

> … the business of the society is being, or is intended to be, conducted for the benefit of the community.[40]

2.20 A community benefit society might, for example, own a local pub, or a local landmark like a pier, or provide co-working spaces to self-employed freelancers, or publish a newspaper, or develop a local renewable energy network, or provide social housing.

2.21 The FCA supplies the following additional guidance.[41] The society must be carrying on business solely for the benefit of the community. The society can seek to benefit the community at large, or it can define the community it seeks to benefit. Unlike co-operatives, a community benefit society cannot provide its benefits contingent on membership.

2.22 Generally, the CCBS Act applies equally to co-operatives and community benefit societies. Perhaps the major difference is that co-operatives carry on business mainly for the benefit of their members, whereas community benefit societies carry on business for the benefit of the wider community.

LEGISLATIVE FRAMEWORK

Historical development

2.23 This section sets out a summary overview of the history of legislation leading to the CCBS Act.[42]

2.24 There were once common law crimes of unlawful assembly and seditious libel. Seditious libel included speech which might stir dissatisfaction with government. If that happened at a meeting, it might lead to the threat of public disorder, and that

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40 CCBS Act, s 2(2)(a)(ii).

41 FCA Guide, pp 31 to 32.

42 For more detail see: G C Oke, *The Friendly Societies Manual* (1855); E W Brabrook, *The Law Relating to Industrial and Provident Societies* (1869); CCBS Handbook, ch 2; Adderley, ch 7.

amounted to unlawful assembly.[43] The storming of the Bastille in the French Revolution in July 1789 heightened anxiety in Britain about assemblies and the formation of societies. Some societies were prohibited by statute.[44] Other legislation prohibited meetings to discuss public grievances, unless notice was given.[45] If unlawful assemblies did not disperse, the punishment was death.

2.25 Against that background, legislation in 1793 allowed people to form and meet as "friendly" societies, as long as they notified themselves to the justices of the peace.[46] Friendly societies were defined as organisations for the purpose of raising funds from members for the relief of members in sickness, old age and infirmity, or for the relief of widows and children of deceased members (a form of "mutual insurance").

2.26 Legislation in 1846 extended the permitted purposes of friendly societies to include "investment societies".[47] These provided for the frugal investment of savings to enable members to purchase food, necessaries, or the tools of their trade, or to provide for the education of their children.

2.27 The Industrial and Provident Societies Act 1852 permitted people, who exercised in common any labour, trade or handicraft, to form societies for any of the purposes identified by the friendly society legislation.[48] In 1862 these industrial and provident societies were given corporate status and limited liability.[49]

2.28 Consolidating legislation in 1876 provided that industrial and provident societies had to state the "object" (purpose) of the society.[50] There was further consolidating legislation in 1893 which defined industrial and provident societies as those which carried on *any* industry, business or trade.[51]

2.29 The Prevention of Fraud (Investments) Act 1939 introduced further requirements for registration as an industrial and provident society. Either a society had to be a "bona fide co-operative",[52] which did not carry on business with the object of making profits mainly for the payment of interest on money invested with the society.[53] Or the society

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43 T Cunningham, *A New and Complete Law Dictionary* (1783); H J Stephen, *Summary of the Criminal Law* (1834) pp 52, 81; Sir James Fitzjames Stephen, *A History of the Criminal Law of England* (1883) vol 2 pp 298, 386.

44 39 Geo 3 c 79 (1799).

45 36 Geo 3 c 8 (1795).

46 33 Geo 3 c 54.

47 Friendly Societies Act 1846 (9 & 10 Vic c 27).

48 15 & 16 Vic c 31.

49 Industrial and Provident Societies Act 1862 (25 & 26 Vic c 87), s 5.

50 Industrial and Provident Societies Act 1876 (39 & 40 Vic c 45).

51 Industrial and Provident Societies Act 1893 (56 & 57 Vic c 39).

52 Prevention of Fraud (Investments) Act 1939, s 10(1)(a).

53 Prevention of Fraud (Investments) Act 1939, s 10(9).

had to conduct its business mainly for the purpose of improving the living conditions of the working classes,[54] or otherwise for the benefit of the community.[55]

2.30 The law was again consolidated in 1965.[56] This applied the same definition to industrial and provident societies, except that it removed any reference to improving the living conditions of the working classes.

2.31 Further (separate) legislation was passed for credit unions in 1979.[57]

2.32 Legislation for friendly societies was consolidated in the Friendly Societies Act 1974. This applied to friendly societies properly so called (those concerned with mutual insurance); it also applied to other societies, such as cattle insurance societies, benevolent societies, working men's clubs, and old people's homes. Today, new societies can no longer register under the 1974 Act.[58] Instead, new friendly societies properly so called can register under the Friendly Societies Act 1992. Other new types of society wishing to register must now use the CCBS Act.

2.33 After 2000, industrial and provident societies were renamed as co-operative and community benefit societies.[59] Community benefit societies (but not co-operatives) were given the power to choose a statutory "asset lock".[60] Where used, this ensures that the assets of the community benefit society cannot be dealt with except for prescribed purposes. In particular, it tends to prevent assets being applied for private profit. (We discuss asset locks further in Chapter 7.) Rules for the disqualification of company directors,[61] and for company insolvency,[62] were also applied to co-operatives and community benefit societies.

Current law

2.34 The law was consolidated in 2014 with the CCBS Act. It extends to England and Wales and to Scotland,[63] although different provisions apply in those two jurisdictions in respect of charges over a society's assets,[64] and mortgages.[65] A Northern Ireland

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54 Prevention of Fraud (Investments) Act 1939, s 10(1)(b)(i).

55 Prevention of Fraud (Investments) Act 1939, s 10(1)(b)(ii).

56 Industrial and Provident Societies Act 1965 (1965 c 12).

57 Credit Unions Act 1979.

58 There remain legacy societies registered under the 1974 Act. We will discuss these arrangements in more detail in our separate work on friendly societies. More information is available on the project page at https://lawcom.gov.uk/project/friendly-societies/.

59 Co-operative and Community Benefit Societies and Credit Unions Act 2010 (2010 c 7), s 2.

60 Co-operatives and Community Benefit Societies Act 2003 (2003 c 15), s 1; Community Benefit Societies (Restriction on Use of Assets) Regulations 2006 (SI 2006/264).

61 Co-operative and Community Benefit Societies and Credit Unions Act 2010, s 3; Co-operative and Community Benefit Societies and Credit Unions Act 2010 (Commencement No 2) Order 2014 (SI 2014/183).

62 Enterprise Act 2002 (2002 c 40), s 255; Industrial and Provident Societies and Credit Unions (Arrangements, Reconstructions and Administration) Order 2014 (SI 2014/229).

63 CCBS Act, s 153.

64 CCBS Act, Pt 5.

65 CCBS Act, ss 71 to 73.

society (that is, a society registered under comparable laws in Northern Ireland) can also apply to be registered under the CCBS Act for the purposes of any activities it carries on in Britain.[66]

2.35 The CCBS Act gives HM Treasury the power to amend the CCBS Act to assimilate any changes in company law since 2002,[67] and to apply company law to societies on matters of investigations, names, dissolution and restoration to the register.[68]

2.36 Most recently, the Co-operatives, Mutuals and Friendly Societies Act 2023 provides that regulations may be made by statutory instrument enabling co-operatives to choose a statutory asset lock too. No such regulations have yet been made.

THE MUTUALS PUBLIC REGISTER AND THE REGISTRAR

2.37 Co-operatives and community benefit societies can register under the CCBS Act. Once registered, they are listed on the Mutuals Public Register.[69]

2.38 There are two principal benefits of registration under the CCBS Act.[70] First, it gives corporate personality to the co-operative or community benefit society. This means that the society is a separate legal entity from its members. As a corporate body, the society can, for example, enter into contracts and hold property in its own name. Second, registration limits the liability of members: whatever debts are incurred by the society, a member's exposure is limited to the price of their shareholding.[71]

2.39 The registrar is the Financial Conduct Authority (FCA). This is an independent public body, accountable to HM Treasury, and funded by the fees which it charges regulated businesses.[72] Its roles under the CCBS Act include: registering a society;[73] suspending registration;[74] cancelling registration;[75] receiving annual returns;[76] on an

66 CCBS Act, s 142.

67 CCBS Act, s 134.

68 CCBS Act, s 135.

69 https://mutuals.fca.org.uk/.

70 CCBS Act, s 3.

71 If the share has not yet been paid for, the member will have to pay; if the share has been paid for, the member might lose that money, but will not be required to pay anything more. Someone who resigns their membership remains liable in this limited way for one year after their resignation, in respect of debts incurred during their membership, but only if those debts cannot be met by current members: CCBS Act, s 124.

72 https://www.fca.org.uk/about/what-we-do/the-fca.

73 CCBS Act, s 3.

74 CCBS Act, s 8.

75 CCBS Act, ss 5 to 7.

76 CCBS Act, s 89.

application by members of the society, appointing inspectors;[77] and prosecuting offences.[78]

2.40 The FCA says that its aim is to maintain public confidence in mutual societies by operating a system of oversight.[79] It publishes a detailed guide (which we call the "FCA Guide") to its role as the registering authority under the CCBS Act.[80]

2.41 The FCA also has a role under the Financial Services and Markets Act 2000, whereby it regulates those who provide regulated activities in the financial sector, and authorises and supervises individuals and businesses that carry out financial services. Some mutual societies, such as credit unions, carry out financial services. In these cases, the FCA has two different roles, one in registering the mutual society, and the other in authorising and supervising the financial services.

2.42 The FCA reports that, as at March 2023, there were 8412 societies registered under the CCBS Act.[81] Of these, 563 were co-operatives, 1391 were community benefit societies, and 6458 were "pre-commencement societies" which are those registered under legislation which preceded the CCBS Act. The FCA records 25 different areas of activity for societies, ranging from advocacy through fishing to welfare. The largest numbers of societies are housing societies and social clubs.

Financial mutuals

2.43 It is not only co-operatives and community benefit societies which appear on the Mutuals Public Register. Both credit unions and building societies appear on the Mutuals Public Register.

2.44 A building society has the principal purpose of making loans secured on residential property funded substantially by its members.[82]

2.45 Credit unions provide services to their members such as savings and loans. Their statutory objects are to promote "thrift" among members by the accumulation of their savings, to create sources of credit for members at fair interest rates, to use members' savings for their mutual benefit, and to educate members in the management of financial affairs.[83] Membership is restricted to those with a common bond, such as a particular occupation or locality.[84]

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77 CCBS Act, s 105 and 106.

78 CCBS Act, Pt 10.

79 https://www.fca.org.uk/firms/our-responsibilities-mutual-societies.

80 FCA, *Registration Function under the Co-operative and Community Benefit Societies Act 2014 Guide* (May 2023), https://www.handbook.fca.org.uk/handbook/RFCCBS.

81 https://www.fca.org.uk/publications/corporate-documents/mutual-societies-registration-function-2022-23.

82 Building Societies Act 1986, s 5.

83 Credit Unions Act 1979, s 1(3).

84 Credit Unions Act 1979, s 1A.

2.46 The Association of British Credit Unions Ltd is a secondary co-operative and a trade association which represents 70% of credit unions in Britain.[85] It reports that there are 246 credit unions in Britain, used by more than 1.44 million people, with total loans of £1.35 billion, and total deposits of £2.12 billion. Between 2014 and 2022, membership increased by 20%, loans by 67%, and deposits by 84%. Internationally there are nearly 88,000 credit unions in 118 countries, with more than 393 million members and total assets over US$3.4 trillion.[86]

2.47 Credit unions register under the CCBS Act, but are further regulated by the Credit Unions Act 1979. Building societies do not register under the CCBS Act. They are registered and regulated under the Building Societies Act 1986. Both the Credit Unions Act 1979 and the Building Societies Act 1986 are outside the scope of this project.

OTHER FORMS OF ORGANISATION

2.48 In this section, we introduce the following forms of organisation: companies, including community interest companies; charities; partnerships; and unincorporated associations. We compare these and their governing legislation to co-operatives and community benefit societies at various points in subsequent chapters. In particular, our terms of reference require us to consider to what extent the CCBS Act needs reform to align with company law, and with charity law (for charitable community benefit societies).

2.49 Note that, in English law, "co-operative" is a "sensitive word" which means that there are restrictions on who can use it. Of course, a business can register as a co-operative under the CCBS Act. However, a company can also call itself a co-operative, if it can show that it is operating as such. Partnerships or unincorporated associations might also conduct themselves according to co-operative principles. In other words, it is not only businesses registered under the CCBS Act which can call themselves co-operatives. (We discuss the use of this "sensitive word" in more detail in Chapter 7 below.)

Companies

2.50 A company is formed by one or more people who subscribe to a memorandum of association and register under the Companies Act 2006.[87] The Registrar for Companies is based at Companies House. Once registered, the company has corporate personality.[88] If the company's constitution so provides, the members can have limited liability. Their liability can be limited to the value of their shares or to an

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85 https://www.abcul.coop/about-us/about-abcul.

86 https://www.abcul.coop/credit-unions/credit-unions-facts-and-statistics.

87 Companies Act 2006, s 7.

88 Companies Act 2006, s 16.

amount which they agree to guarantee.[89] Companies can be private or public.[90] Only public companies can offer to the public any securities of the company (like shares).[91]

2.51 Company law can be a suitable point of comparison: like societies, companies are also businesses limited by shares, and company law has been updated more often and more recently. Indeed, the CCBS Act itself includes a power to amend the CCBS Act to assimilate changes in company law.[92] However, there are also differences between companies and societies, as we shall see throughout this paper; in some places those differences might warrant a different approach to governing law.

2.52 A company can be formed for any lawful purpose.[93] Unlike a co-operative, a company can conduct its business with the object of making profits mainly for the payment of dividends. Unlike a community benefit society, a company need not conduct its business for the benefit of the community.

2.53 The exception is a community interest company.[94] The purpose of a community interest company is primarily one of community benefit rather than private profit.[95] A company satisfies the community interest test if a reasonable person might consider that its activities are being carried on for the benefit of the community.[96] This excludes political campaigning.[97] It cannot be registered as a charity.[98] There is a Regulator for Community Interest Companies, also based in Companies House. A community interest company must produce an annual report which includes a description of the manner in which the company's activities during the financial year have benefited the community.[99]

2.54 A community interest company cannot transfer its assets other than for full consideration.[100] There are also limits to the size of dividends which can be declared,

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89 Companies Act 2006, s 3.

90 Companies Act 2006, s 4.

91 Companies Act 2006, s 755.

92 CCBS Act, s 134.

93 Companies Act 2006, s 7(2).

94 Companies Act 2006, s 6; Companies (Audit, Investigations and Community Enterprise) Act 2004, Pt 2.

95 Community Interest Companies Guidance (last updated 9 February 2024), https://www.gov.uk/government/publications/community-interest-companies-how-to-form-a-cic.

96 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 35.

97 Community Interest Company Regulations 2005 No 1788, Pt 2.

98 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 26(3).

99 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 34; Community Interest Company Regulations 2005 No 1788, r 26.

100 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 32; Community Interest Company Regulations 2005 No 1788, Pt 3.

and to the amount of interest which can be paid on debts.[101] On winding-up, any residual assets are to go to another organisation with an asset lock.[102]

Charities

2.55 Charities must carry on activities which have a charitable purpose. Those purposes which are charitable are listed by the Charities Act 2011, and include, for example, community development.[103] Charity trustees must prepare an annual report on the activities of the charity.[104]

2.56 The regulator is the Charity Commission, and it maintains a register of charities.[105] There is a tribunal for appeals against a decision of the Charity Commission.[106] Every charity must be registered, except exempt charities and small charities.[107] Importantly, charitable community benefit societies are exempt charities, meaning that they cannot register with the Charity Commission.[108]

2.57 A charitable purpose must be for the public benefit.[109] The Charity Commission must issue guidance about the public benefit requirement.[110] The Charity Commission says that a purpose is beneficial if a benefit is identifiable and capable of being proven by evidence rather than based on personal views; the activity must benefit the public in general, or at least a sufficient section of the public.[111] A sufficient section of the public might be defined by a geographical area, or a protected characteristic, or a profession, but not by skin colour, nor by reference to a family relationship or common employer.[112]

2.58 Charities can take various forms, including a company,[113] trust, or unincorporated association. There is also the charitable incorporated organisation,[114] which is a body corporate, and whose members might have no liability or only limited liability.[115]

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101 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 30; Community Interest Company Regulations 2005 No 1788, Pt 6.

102 Community Interest Company Regulations 2005 No 1788, r 23.

103 Charities Act 2011, s 3(1)(e).

104 Charities Act 2011, s 162.

105 Charities Act 2011, ss 15(4), 29.

106 Charities Act 2011, Pt 17.

107 Charities Act 2011, s 30.

108 Charities Act 2011, sch 9 para 4.

109 Charities Act 2011, s 2(1)(b).

110 Charities Act 2011, s 17.

111 https://www.gov.uk/guidance/public-benefit-rules-for-charities.

112 https://www.gov.uk/government/publications/public-benefit-the-public-benefit-requirement-pb1/public-benefit-the-public-benefit-requirement#part-2-what-for-the-public-benefit-means.

113 Charities Act 2011, Pt 10.

114 Charities Act 2011, Pt 11.

115 Charities Act 2011, s 205.

Partnerships

2.59 In a partnership, people carry on business in common with a view of profit, without having another registered form like a company.[116] A general partnership is not a corporate body. Each partner is jointly liable for all debts and obligations of the partnership,[117] and for any wrongs committed by a partner.[118] Each partner can bind the others.[119] Property brought into the partnership is to be held and applied exclusively for the benefit of the partnership.[120]

2.60 Alternatively, there is also a limited liability partnership, which is a body corporate.[121] In this way, debts and obligations are incurred by the partnership, not by the partners. Limited liability partnerships register at Companies House.

Unincorporated associations

2.61 An unincorporated association is when two or more people join together for a common purpose that is not a business purpose; they join together by mutual undertakings in an organisation that has rules.[122] It is not a corporate body. In dealing with third parties, a member might incur personal liability. A member's ability to bind other members, or to require an indemnity from other members, depends on the law of agency and the rules of the association. Most clubs are unincorporated associations.

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116 Partnership Act 1890, s 1.

117 Partnership Act 1890, s 9.

118 Partnership Act 1890, ss 10, 12.

119 Partnership Act 1890, s 5.

120 Partnership Act 1890, s 20.

121 Limited Liability Partnership Act 2000, s 1.

122 *Conservative and Unionist Central Office v Burrell* [1982] 1 WLR 522, 525 (Lawton LJ).

Chapter 3: What is a co-operative?

3.1 The Co-operative and Community Benefit Societies Act 2014 (CCBS Act) includes only a partial definition of a co-operative. This chapter considers whether there should be a new and full statutory definition and, if so, what that definition should be.

THE CURRENT LAW

3.2 The CCBS Act provides a definition of a co-operative which is fragmented and partial.

3.3 Section 2 of the CCBS Act provides:

> (1) A society for carrying on any industry, business or trade … may be registered under this Act as
>
> > (a) a co-operative society…
>
> (2) [if]…
>
> > (a) … it is shown to the satisfaction of the [registrar]
> >
> > > (i) that the society is a bona fide co-operative society…
> >
> > (b) …
> >
> > (c) … [whose] rules contain provision in respect of the matters mentioned in section 14…
>
> (3) … "co-operative society" does not include a society that carries on, or intends to carry on, business with the object of making profits mainly for the payment of interest, dividends or bonuses on money invested or deposited with, or lent to, the society or any other person.

3.4 Section 14 provides:

> A registered society's rules must contain provision about the following matters [including] … The objects of the society … The terms of admission of the members … the scale and right of voting … whether any or all shares are transferrable … whether any or all shares are withdrawable … whether members may withdraw from the society … The way in which the society's profits are to be applied…

3.5 Section 14 says that there must be rules on these matters, but does not say what those rules must be. For example, what rules for the admission of members, or for the allocation of voting rights, are consistent with being a bona fide co-operative? That appears to be a decision wholly within the discretion or "satisfaction" of the registrar.

There is currently no appeal against a decision of the registrar that a co-operative is not bona fide and therefore cannot be registered under the CCBS Act.[123]

ORIGINS OF THE CURRENT LAW

3.6 We have set out the general legislative history of co-operatives in Chapter 2. For present purposes, we focus here on the Prevention of Fraud (Investments) Act 1939.

3.7 The 1939 Act was enacted in response to an inquiry into "share-pushing".[124] Fraudsters were selling shares in companies to the public. The fraudsters took the money without transferring the shares, or they were selling shares in worthless companies created simply as a vehicle for fraud. This was causing millions of pounds of loss annually.[125]

3.8 The 1939 Act required all traders in shares to be licensed,[126] except that this did not apply to industrial and provident societies.[127] The question therefore arose how to prevent societies becoming the new vehicle for share-pushing.

3.9 The solution contained in the 1939 Act was to require societies to meet further requirements for registration. Either the society was to be a bona fide co-operative[128] that did not seek to make profits mainly for paying interest on shares,[129] or the society was to carry on business for the benefit of the community.

3.10 Thus it was the 1939 Act that introduced the phrase "bona fide co-operative", and that introduced the negative definition still found in section 2(3) of the CCBS Act (not making profits to pay interest on shares).

3.11 A contemporaneous internal document, seemingly from the Registry of Friendly Societies (the then registrar), provides further context.[130] A copy of this document is reproduced in Appendix 3. It states as follows:

> What is a "bona fide co-operative society"? This phrase was used as a last resort because it had not been found possible to arrive at a satisfactory definition.
>
> It is suggested that a bona fide co-operative society must satisfy the following conditions:
>
> (a) it cannot be a "money-making" society as defined in sub-clause 6 [the negative definition];

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123 CCBS Act, section 9(3).

124 Hansard, House of Lords Debate, 28 February 1939, Prevention of Fraud (Investments) Bill.

125 *Share-Pushing*, Report of the Departmental Committee appointed by the Board of Trade (1937) Cmd 5539.

126 Prevention of Fraud (Investments) Act 1939, s 1.

127 Prevention of Fraud (Investments) Act 1939, s 2(1)(b).

128 Prevention of Fraud (Investments) Act 1939, s 10(1)(a).

129 Prevention of Fraud (Investments) Act 1939, s 10(9).

130 We are very grateful to Ian Adderley of the FCA for supplying this.

(b) it must so conduct its business as to show that it exists primarily for the mutual benefit of its members, such benefit taking different forms according to the nature of the society but being always directly related to the use which the member makes of the facilities provided by the society and not to the amount of capital which he invests…

(c) there must be no artificial restriction of membership ie no restriction with the object of enhancing the value of the "proprietary" rights or interests of the members. On the other hand restriction of membership would not necessarily offend the co-operative principle eg in the case of a club which must relate the number of members to the size of its premises, or in the case of a society which confines its activities to a particular area;

(d) no member other than a registered society shall have more than one vote;

(e) the return (in whatever form) on share capital must not exceed a moderate rate…

3.12 We make the following observations. First, the phrase "bona fide co-operative" was a placeholder for a definition. Second, although the then registrar said that legislators could not arrive at a definition of a co-operative, nevertheless the registrar does then proceed to identify quite clearly what they see as the necessary conditions for being a bona fide co-operative.

REGISTRAR GUIDANCE

Historic guidance

3.13 When the requirement of being a "bona fide co-operative" was first introduced by the 1939 Act, the Registry of Friendly Societies issued guidance. This provides a useful comparison to modern guidance. A copy of that guidance is reproduced in Appendix 3.

3.14 That historic guidance states as follows:

There is no statutory definition of a bona fide co-operative society but such a society will normally be expected to satisfy the following conditions:

(a) … The business of the society will be conducted for the mutual benefit of its members in such a way that the benefit which members obtain will in the main stem from their participation in its business…

(b) … Control of the society will under its rules be vested in the members equally and not in accordance with their financial interest in the society. In general therefore the principle of "one man one vote" must obtain.

(c) … Interest payable on share and loan capital will under its rules not exceed a rate necessary to obtain and retain the capital required to carry out the objects of the society…

(d) … The profits of the society's business after payment of interest on share capital, if distributable amongst the members, will under its rules be distributable amongst them in relation to the extent to which they have traded with or taken part in the

business of the society… In some societies … profits will not usually be distributable amongst members but are ploughed back to cheapen and improve the amenities available to members.

(e) … There should be no artificial restriction of membership with the object of increasing the value of proprietary rights and interests. There may, of course, be grounds for restricting membership that do not offend the co-operative principle; for example, the membership of a club might be limited by the size of its premises and of a self-build housing society by the number of houses that could be erected on a particular site.

Current guidance

3.15 The current registrar is the Financial Conduct Authority (FCA). The FCA Guide says that a co-operative can pay interest or dividends on money invested or lent – but this must not be the "main purpose" of the society.[131] Whether it is the main purpose, says the FCA Guide, is judged not solely by looking at the rules of the society and its stated objects, but also by reviewing its trading patterns or accounts,[132] and generally considering "all the information available".[133] We note in passing that this seems to have the potential to be both burdensome on the FCA and unpredictable for would-be co-operatives.

3.16 Otherwise, more generally, the FCA Guide says that it considers a society to be a bona fide co-operative where:

> It is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise.[134]

3.17 The FCA Guide acknowledges that it has taken this definition from the International Labour Organisation (ILO),[135] and from the International Cooperative Alliance (ICA).[136] As we saw in Chapter 2, the ICA also publishes the Co-operative Values and the Co-operative Principles alongside its definition of a co-operative. The FCA Guide says that it is an "indicator" that the society is a bona fide co-operative where the society puts the Co-operative Values into practice through the Co-operative Principles.[137]

3.18 In summary, the Co-operative Principles are:

(1) Voluntary and open membership.

(2) Democratic member control.

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131 FCA Guide, para 4.2.1.

132 FCA Guide, para 4.2.4.

133 FCA Guide, para 4.2.3.

134 FCA Guide, para 4.3.1.

135 Promotion of Cooperatives Recommendation No 193 (2002), para 2.

136 ICA Statement on the Cooperative Identity (1995).

137 FCA Guide, para 4.3.3.

(3) Member economic participation.

(4) Autonomy and independence.

(5) Education, training and information.

(6) Co-operation among co-operatives.

(7) Concern for community.

3.19 The FCA Guide says that it generally expects to be able to verify compliance with Co-operative Principles 1 to 4 by considering the society's rules.[138] It does not necessarily expect to be able to verify compliance with Co-operative Principles 5 to 7.[139] Further, the FCA Guide does not exclude that there may be yet other indicators that a society is a bona fide co-operative.[140]

CRITICISMS OF THE CURRENT FRAMEWORK

3.20 The negative definition of what a co-operative is not, in section 2(3) of the CCBS Act, is primarily concerned with paying interest on shares. We discuss shares in Chapter 5, where we consider section 2(3) in detail. We do not consider it any further in this chapter; here we consider a positive definition of a co-operative.

3.21 There are a number of criticisms of the current framework for registering a society as a co-operative, as follows.

3.22 The phrase "bona fide co-operative" is not a definition, but a placeholder for a definition, as we saw above. It provides no guidance. Instead, the registrar has a discretion to decide what a co-operative is, unfettered by almost any statutory rules and no right of appeal. This risks inconsistency with the rule of law.

3.23 The FCA is to be commended for setting out its approach in writing in a guide which is clearly written. In the absence of statutory guidance, it is proper for the FCA to draw on guidance from elsewhere. It is not surprising that the FCA has looked to guidance from the ICA and the Co-operative Principles. However, the FCA Guide acknowledges (realistically) that the FCA can only verify a society's compliance with some of those Principles. In our view, this reveals the limited value of those Principles as guidance in deciding whether to register a society.

3.24 Further still, the FCA Guide says that the Co-operative Principles are (merely) an "indicator" that a society is a co-operative. Similarly, the ICA says that the Principles are only "guidelines". The FCA Guide says that other – unspecified – indicators might show a society to be a bona fide co-operative. All this reveals the uncertainty in the current approach.

3.25 We have also heard the following complaints from stakeholders. Some say that the approach of the FCA is idiosyncratic, or rooted in one particular vision of the co-

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138 FCA Guide, para 4.3.4.

139 FCA Guide, para 4.3.5.

140 FCA Guide, para 4.3.6.

operative form. Some say that attempting to register anything innovative, or even a modest departure from the traditional form, can be slow, unpredictable, and even unsuccessful. Some say that this is the case whether registering a society for the first time, or seeking to change the rules of a registered society. Some stakeholders compare this situation unfavourably to company law: they say that, in contrast, the process for setting up a new company is certain and quick.

3.26 For their part, the FCA say that they aim to register at least 90% of "valid" applications within 15 days, although it can take up to a year to register a credit union.[141] A difficulty, of course, is identifying which applications are indeed valid.

BENEFITS OF HAVING A NEW DEFINITION

3.27 Assuming that one can be formulated, a new definition could reduce the discretion which the registrar needs to exercise in deciding whether to register a society as a co-operative. In turn, this could make the registration function more efficient and predictable. It would also cause the process to be more strongly aligned with the rule of law.

3.28 A more comprehensive definition could provide an orienting framework for other topics within co-operative law, such as what shares might be allowed and how they might be regulated. A definition could also provide a "hook" for other policy initiatives, like new funding for co-operatives, or changes in their tax treatment. Put simply, it might be easier, for example, to develop a tax regime favourable to co-operatives if the relevant authorities know more clearly what a co-operative is.

3.29 Some stakeholders have said that a definition can have explanatory power: a definition can communicate quickly, in general terms, what a co-operative is, and thus how it might be distinctive (for example, in comparison to a company). Some stakeholders have said that this might help them in promoting their form and activity. For example, a funding body might be more likely to allocate money if it knows with more certainty to what type of body it is giving the money, and if the body must by its characterisation adhere to certain principles.

3.30 On the other hand, although one of the criticisms of the current framework is its lack of certainty, the corollary is flexibility. A new definition might exclude some current practice. We have repeatedly heard from stakeholders of their desire to modernise society law; any such modernisation will inevitably involve change.

3.31 Overall, and on the assumption that suitable wording can be found, we are provisionally of the view that there should be a new statutory definition of a co-operative, given the potential benefits of a new definition, and in light of the criticisms of the current framework.

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141 https://www.fca.org.uk/firms/register-mutual-society

Consultation Question 1.

3.32 We provisionally propose that there should be a new statutory definition of a co-operative. Do you agree in principle (subject to the formulation of a suitable definition)?

IDENTIFYING A NEW DEFINITION

3.33 Later in this chapter, we provisionally propose a new definition of a co-operative. In arriving at that definition, we considered other definitions which have been generated by the co-operative sector itself, in particular the ICA and PECOL definitions. Ultimately, we do not think that these other definitions are suitable as a statutory definition in legislation for England and Wales, but they do point the way towards a definition which might be more precise and fitting. We also benefitted from discussions with stakeholders, and carried out our own further research. We think it worth making clear up front that any definition adopted for statutory purposes should properly focus on the essential rather than the aspirational elements of what it means to be a co-operative.

OTHER EXISTING DEFINITIONS

ICA definition

3.34 As introduced in Chapter 2, the ICA Statement on Co-operative Identity provides the following definition of a co-operative.[142]

> A co-operative is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise.

3.35 It also contains the Co-operative Values, as well as the Co-operative Principles, which are "guidelines by which co-operatives put their values into practice". We note, for example, that the Co-operative Principles are given statutory effect in Australian co-operative law.[143]

3.36 We do not think that it would be appropriate to adopt the ICA definition into domestic legislation in England and Wales, and this section explains why.

3.37 A preliminary concern for us is this: the Co-operative Principles are expressed to be merely "guidelines". It would be preferable for a statutory definition to include definite conditions with which a society can clearly show compliance, so as to provide certainty in respect of registration. To some extent, the material in the Co-operative Principles is aspirational, whereas a statutory definition would normally set only minimum standards for compliance.

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142 https://www.ica.coop/en/whats-co-op/co-operative-identity-values-principles.

143 The Co-operatives National Law, first adopted in New South Wales: Co-operatives (Adoption of National Law) Act 2012 No 29.

3.38 Similarly, there are seven Co-operative Principles. Each comes with a paragraph of explanation even in the headline Statement of Co-operative Identity. However, those Principles come with a separate guidance document over 100 pages long.[144] A statutory definition would ideally speak for itself.

3.39 The ICA operates internationally. There are countries which do not enjoy political democracy or freedom of association, or where businesses cannot make decisions autonomously. In that regard, the ICA definition is an appropriately aspirational statement of global political ambition. However, those are not the conditions in the United Kingdom, where co-operatives have enjoyed increasing legislative support since 1793. Our purpose here is to identify a definition which is fitting to our domestic legislative context. From the latter perspective, we make the following comments on the ICA definition.

3.40 **Jointly owned**. We are not persuaded that co-operatives are jointly owned insofar as this term is used in a technical legal context. "Jointly owned" property under the law of England and Wales is property that is owned by two or more people. However, registration under the CCBS Act renders a co-operative a corporate body with its own legal personality. The society owns its assets in its own name. Members do not own the society's assets, jointly or at all. On dissolution, surplus assets might not be distributed among members. The rules of a co-operative might prescribe that, on dissolution, surplus assets go to another co-operative. If a co-operative adopts a statutory asset lock, then assets cannot be distributed to members. Further, to the extent that a member "owns" shares, if those shares are non-withdrawable, their purchase price is tantamount to a donation to the co-operative.

3.41 The Third Co-operative Principle, "Member Economic Participation", provides:

> Members contribute equitably to, and democratically control, the capital of their co-operative. At least part of that capital is usually the common property of the co-operative … Members allocate surpluses for any or all of the following purposes: developing their co-operative, possibly by setting up reserves, part of which at least would be indivisible…

3.42 Again, this is not quite the same as joint ownership in domestic legal terms. "Indivisible reserves" are those which cannot be distributed to members. If they are the "common property" of the co-operative, they are owned by the co-operative as its own legal person – they are not owned by the members.

3.43 **Democratically controlled**. We think that this phrase is too vague to be used in a statutory definition, and would require further particularisation. Democracy means different things to different people in different contexts – there is no single meaning of democracy which has attracted universal endorsement. If a statutory definition were to use a phrase this vague, it would provide little guidance to societies in terms of what they need do to obtain or retain registration. It would instead make registration once again a matter for the discretion of the registrar.

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144 https://ica.coop/en/media/library/the-guidance-notes-on-the-co-operative-principles.

3.44 **Autonomous association**. Similarly, we think that the word autonomous is also too vague for inclusion in a statutory definition. At the least, there can be gradations of autonomy. Furthermore, the Fourth Co-operative Principle states that organisations maintain their autonomy by ensuring that they retain "democratic control by their members". If this is the intended meaning of autonomy in this context, then it merely duplicates the requirement of democratic control, rather than adds anything new.

3.45 **Needs and aspirations**. We do not think that these words reflect what co-operatives necessarily do with sufficient precision for a statutory definition. Our reasons are as follows.

3.46 "Needs" tends to suggest a basic necessity. The Rochdale Pioneers, for example, were concerned with sourcing basic food items like flour at affordable prices. Many modern co-operatives seek to go beyond basic necessities. For example, modern retail co-operatives sell food items which might be classed as luxuries.

3.47 Perhaps an extension beyond needs is what the word "aspirations" aims to reflect. However, "aspirations" tends to mean hopes and ambitions. These are abstract concepts, rather than material things like food or a wage. They also tend to be inchoate or yet to be achieved – a fulfilled ambition is no longer an aspiration (and does not necessarily continue as a need).

3.48 Even if "needs and aspirations" can be given a precise meaning, we doubt that it distinguishes what co-operatives do from what any business does. For example, we think it just as plausible to say that companies or partnerships seek to meet the needs and aspirations of their members.

3.49 We think that meeting members' "needs and aspirations" is itself an aspirational statement. We think that it suffices to say that modern co-operatives perform a function, and members are simply those who want to benefit from that function. It is not necessary to talk about needs and aspirations.

3.50 Finally, we are not sure what "economic, social and cultural" adds. We accept that co-operatives might perform economic, social or cultural functions – but we are not persuaded that those must be the only functions which a co-operative could perform. Rather, we think that a co-operative might perform any (lawful) function: for example, legal, political, environmental, health, and so on.

PECOL definition

3.51 The *Principles of European Cooperative Law* (PECOL) surveys co-operative law across European countries. It aims to distil common characteristics into rules. It also provides a detailed commentary on how those rules are reflected in each country. It suggests the following headline definition:[145]

> (1) Co-operatives are legal persons governed by private law that carry on any economic activity without profit as the ultimate purpose and (a) mainly in the interest of their members, as consumers, providers or workers of the co-operative enterprise

[145] PECOL, r 1.1.

("mutual co-operatives"), or (b) mainly in the general interest of the community ("general interest co-operatives").

(2) "Profit as the ultimate purpose" means making profits mainly for the payment of interest, dividends or bonuses on money invested or deposited with, or lent to, the co-operative or any other person.

3.52 We make the following observations. First, carrying on an economic activity mainly in the interest of their members seems a more realistic description of co-operative business than meeting "needs and aspirations" of members.

3.53 Second, "general interest co-operative" corresponds to a community benefit society under the CCBS Act. A "mutual co-operative" corresponds with a co-operative under the CCBS Act. PECOL defines a co-operative as operating "mainly in the interest of their members as consumers, providers or workers of the co-operative enterprise".

3.54 Third, it seems to us that central to this definition is the negative definition of what a co-operative is not ("without profit as the ultimate purpose"). This corresponds closely to section 2(3) of the CCBS Act. To repeat, we consider that section in detail in Chapter 5 when we look at shares, which we think is its proper context.

Other suggested ingredients

3.55 Stakeholders have suggested other ingredients that could form part of a definition of a co-operative. There are five to consider here, as follows.

(1) An applicant society should be registered unless no reasonable person could characterise it as a co-operative.

On the one hand, this would make registration almost inevitable: it only requires one reasonable person to characterise the applicant society as a co-operative (even if everyone else disagrees). On the other hand, it still leaves unanswered the question of when it would be unreasonable to characterise a society as a co-operative.

(2) There should be solidarity in remuneration, with a maximum cap on wage disparity between the highest and lowest paid employee in a co-operative.[146]

While this might reflect the aspiration of equality (which is one of the Co-operative Values), we think that this is properly an issue for individual co-operatives and is unlikely to be suitable for a statutory requirement.

(3) Workers employed by a co-operative should have votes, otherwise it simply recreates the model of capital hiring labour.

We have sympathy with this suggestion too. But we think that this is again aspirational rather than essential. Which is to say that, while pursuing those goals (solidarity in remuneration, worker votes) may be commendable, we do not think them a necessary pre-requisite to being (registered as) a co-operative.

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[146] See too: Kiatpongsang, S, and M I Norton, "How Much (More) Should CEOs Make? A Universal Desire for More Equal Pay" (2014) 9 *Perspectives on Psychological Science* 587.

Indeed, for better or worse, we question how many co-operatives currently comply with these latter two suggestions. We also note that they do not feature in the ICA definition.

(4) Education should be a compulsory component of being a co-operative.

We note that the Fifth Co-operative Principle is "Education, Training, and Information", and it provides as follows:

> Co-operatives provide education and training for their members, elected representatives, managers, and employees so they can contribute effectively to the development of their co-operatives. They inform the general public – particularly young people and opinion leaders – about the nature and benefits of co-operation.

Some stakeholders have said that a specified minimum amount of any surplus should be put into an indivisible reserve earmarked for education. For example, a similar arrangement is reported in the laws of Spain and Portugal.[147] Other stakeholders were concerned that some co-operatives, perhaps some working men's clubs for example, might not have sufficient profitability to be able to provide for education.

We believe strongly that education is a force for good. However, we think that the Fifth Co-operative Principle is more aspirational than essential. We doubt that there is a sufficiently precise answer to "what education and how much" that would make its inclusion workable within a statutory definition of a co-operative which sets the minimum requirements simply for registration.

(5) The Sixth and Seventh Co-operative Principles should also be compulsory. These are "Cooperation among Co-operatives" and "Concern for Community".

Some stakeholders have said that a co-operative is only a co-operative when it complies with all the Co-operative Principles. For example, some said that a percentage of any surplus should be sent mandatorily to the national federation for a ring-fenced fund for financing new co-operatives.

In contrast, one stakeholder said that compliance with the first four Co-operative Principles identifies a co-operative, whereas compliance with the last three Co-operative Principles identifies a good co-operative. In other words, the first four are essential requirements, whereas the last three are desirable only.

Once again, we doubt that there are sufficiently precise answers to the questions "how much co-operation among co-operatives and in what form" and "how much concern for community and how manifested" which would make inclusion workable within a statutory definition.

147 PECOL, p 84.

PROPOSED DEFINITION

3.56 We provisionally propose that a statutory definition of a co-operative should contain the following elements: that it is a society for carrying on any business mainly for the benefit of its members through transactions with its members; and that membership is voluntary and open to all, with one vote per member. We discuss each ingredient below.

3.57 This proposed definition does not purport to be an exhaustive list of all co-operative ideals. Rather, it is intended to contain only the minimum requirements necessary for registration under the CCBS Act. Co-operatives would be free of course to go beyond these minimum requirements as they seek fuller alignment with the Co-operative Principles and the Co-operative Values.

3.58 Our proposed definition need not stand or fall in its entirety. It may be that consultees agree with some ingredients but disagree with others, so that our final recommendation might contain more or less than our current proposal. For example, we acknowledge that it might be controversial to describe membership as being open to all, or to require one vote per member.

3.59 **Society for carrying on any business**. We do not see this element as controversial. It is part of the current CCBS definition. The ICA definition uses the word "association", and we think that "society" tends to mean the same thing – which is to say, more than one person. Some businesses can consist of a single person, but a co-operative needs at least another person with whom to co-operate. (We add in passing that, if our ultimate recommendations for reform lead to legislation, the final choice of wording, in this case and more generally, would be for parliamentary drafters.)

3.60 Further, the ICA definition refers to an "enterprise", while PECOL refers to carrying on an "economic activity". We have retained the reference to "business", which we think is similarly broad. We are not convinced that reference in the current CCBS Act to "industry" or "trade" adds anything. Also, we have not yet heard from any stakeholder that a co-operative should be other than a business.

3.61 **Mainly for the benefit of its members**. The ICA definition says that people unite to meet their common needs. In other words, people co-operate in order to benefit themselves. This is consistent with the Co-operative Values of self-help and self-responsibility. The PECOL definition makes this express, saying that a mutual co-operative carries on business mainly in the interest of its members.

3.62 Of course, people other than members might benefit from the co-operative's business. For example, non-members might shop in a consumer co-operative. The local community might benefit from having a successful business in the area through, for example, the creation of jobs. However, when we suggest that a co-operative carries on business "mainly" for the benefit of its members, this is not simply in recognition of the fact that a co-operative business might incidentally benefit others. Rather, we intend to allow that a co-operative might formally have objects beyond benefitting its members.

3.63 For example, the Fifth Co-operative Principle states that co-operatives might provide education and training. The Sixth Co-operative Principle states that one co-operative might support another co-operative. The Third Co-operative Principle, which is "Member Economic Participation", allows that a trading surplus might be applied to "other activities approved by the membership" rather than returned as a benefit to members through a member dividend.

3.64 Further, we think that the word "benefit" is more flexible than "needs" and more realistic than "aspirations". It is also the word used for community benefit societies. We do not think it is necessary to qualify "benefit" with such adjectives as "economic", "social" or "cultural", whether applied cumulatively (as in the ICA definition) or alternatively. At any rate, we would not wish to constrain the use of the co-operative form to deliver innovative benefits to members.

3.65 **Through transactions with its members**. We do not think it sufficient merely to say that a co-operative benefits its members. Every business might seek to benefit its members in some way. For example, a company might pay its shareholders a dividend out of its profits. What we are seeking here is a criterion which distinguishes a co-operative from other businesses, especially companies. How does a co-operative benefit its members *distinctively*? We think that a co-operative benefits its members through transactions with its members.

3.66 For example, a consumer co-operative sells at fair prices to member shoppers who buy from it. A worker co-operative aims to set fair pay for its members who work for it. A producer co-operative aims to buy at fair prices from its members who sell it their produce. It is primarily through these transactions that a co-operative seeks to benefit its members.

3.67 In contrast, a company might typically benefit its investor members by sharing profit with them. A co-operative might reward investors by paying interest on shares, but in Chapter 5 we propose a limit on such interest so that the main focus remains transactions rather than investments.

3.68 That members are benefitted mainly through transactions with the society was also the view of the then registrar when the 1939 Act introduced the requirement of being a "bona fide co-operative". As noted above, the registrar said that a member benefits in "different forms according to the nature of the society but being always directly related to the use which the member makes of the facilities provided by the society".[148] Similarly, the registrar said that "the benefit which members obtain will in the main stem from their participation in its business".[149] Similarly, in New Zealand legislation, a co-operative is defined in terms of being a company which transacts with its shareholders.[150]

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148 See para 2.11 above.

149 See para 2.14 above.

150 Co-operative Companies Act 1996, ss 2 and 3.

3.69 PECOL also says that co-operatives: pursue their objective mainly through co-operative transactions with their members;[151] and act mainly in the interest of their members as consumers, providers or workers of the co-operative enterprise.[152]

3.70 The centrality of a co-operative transacting with its members also finds expression in the Third Co-operative Principle, which states:

> Members allocate surpluses for any or all of the following purposes … benefiting members in proportion to their transactions with the co-operative…

3.71 Using the example of a consumer co-operative, this might work as follows. At the year end, the co-operative might have a trading surplus. This means that its prices were perhaps higher than they needed to be. The co-operative can now make a price adjustment and refund members. It is not that members get a share of any profit. Rather, they receive a refund on their own purchases – a "member dividend" paid in proportion to their own transactions with the society. In this way, the share of any trading surplus is also a function of a member's transactions with the co-operative.

3.72 Finally here, we note of course that co-operatives can trade with non-members, and that this might be an important source of income. But we think that there is a difference between how a co-operative is funded, and its purpose. A co-operative might trade with non-members, but we think that its purpose is to benefit members through transactions with those members.

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151 PECOL, r 1.4(1).

152 PECOL, r 1.1.

Case study: green energy co-operatives

3.73 How does a requirement to transact with members work for a green energy co-operative? Energy producers cannot usually sell directly. Instead the energy goes into the national grid. When consumers buy energy, they might demonstrate their support for green energy generation in general, or even from a particular producer, by buying a green tariff, but the actual energy they receive comes from the national grid "pool".

3.74 Given this physical constraint, we think that it might still be fair to characterise a green energy co-operative as transacting with its members if the following occurred. First, members choose a green energy tariff. Second, for any surplus generated by the co-operative, if the co-operative pays a member dividend, that dividend is calculated as a proportion of each member's energy consumption.

3.75 In contrast, if a member does not choose a green energy tariff, and seeks a share of trading profits regardless of their energy consumption, this looks much less like co-operating, and more like seeking a return on an investment.

3.76 Alternatively, members might subscribe to a society whose goal is simply to put green energy into the national grid. No doubt that is a laudable ambition. If that was the only characteristic of the society, we think it aligns more closely with a community benefit society.

Case study: trade bodies

3.77 How does a requirement to transact with members work with a trade body? For example, primary co-operatives might confederate to create a secondary co-operative as their representative trade body. This trade body might provide advice or support to individual members. This would be a straightforward transaction with the member.

3.78 However, much of the work of the trade body might be advocacy or lobbying on behalf of the sector to third parties. The trade body's time is mostly spent engaging with third parties. Nevertheless, in this case, we think that the transaction with the member is as follows: the member pays its subscription fee, and in return receives advocacy services on its behalf. An analogy might be a barrister acting in a group claim on behalf of multiple claimants, or an agent working on behalf of several clients.

3.79 **Membership is voluntary**. This means that a person has a choice whether to join the co-operative, and is also free to leave. We do not think that this should be controversial since it is part of the ICA definition, and is part of the First Co-operative Principle, "Voluntary and Open Membership", which says:

> Co-operatives are voluntary organisations, open to all persons able to use their services and willing to accept the responsibilities of membership, without gender, social, racial, political or religious discrimination.

3.80 Further, the co-operative will of course be regulated by the general law of England and Wales or Scotland – for example, in the prohibition of discrimination.[153]

3.81 **Membership is open to all**. Again, this is part of the First Co-operative Principle: "open to all persons able to use their services and willing to accept the responsibilities of membership". It is also specified by PECOL.[154]

3.82 We acknowledge that the phrase "open to all" is capable of various interpretations. We have chosen this phrase because it is the one currently used in the Co-operative Principles, and we think it worthwhile to consult on whether it is capable of having a meaning which is sufficiently precise for a statutory definition.

3.83 Our concern is that co-operative membership might not be literally open to all. Membership can be declined; in some cases, membership is necessarily limited – for example, a housing co-operative will have a finite number of rooms. We question whether membership can be described as open to all if there is a selection process through which only some applicants might be successful. It may be that open membership is an aspiration for the co-operative sector as a whole and should not appear as an ingredient in the definition of an individual co-operative.

3.84 **One vote per member**. Surprisingly perhaps, this is the ingredient we have found most vexing, because of the variety of current practices.

3.85 The co-operative movement tends to extol its democratic credentials. Indeed, democracy features in the ICA definition and in the Co-operative Values. But if democracy is to be a genuine *distinguishing* characteristic of co-operatives, it cannot simply mean that co-operatives sometimes take a vote. All businesses, including companies, take a vote at least occasionally.

3.86 Democracy can mean different things to different people. What we seek here is not the one right meaning of democracy, but a particular democratic practice that is characteristic of co-operatives. We propose: one vote per member. In other words, when a vote is put to the membership, for example in an annual general meeting, each member has a vote, but only one vote.

3.87 We think that this is a focal meaning of democracy. It aligns with the Second Co-operative Principle, which is "Democratic Member Control", which says "in primary co-operatives members have equal voting rights (one member, one vote)". It is also consistent with equality as a Co-operative Value, because it recognises that all members have moral equality when it comes to voting rights. It is consistent with the views and guidance of the registrar in 1939 when statute introduced the requirement of being a bona fide co-operative. We note also that one vote per member is a

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153 See the Equality Act 2010.

154 PECOL, r 2..2(1).

requirement in Canadian legislation for primary co-operatives,[155] and it is what allows a company limited by guarantee, in Australian legislation, to show that it is a mutual.[156] It also distinguishes co-operatives from companies which might typically have one vote per share, so that those with more shares have more votes.

3.88 However, some stakeholders have told us that not all British co-operatives operate on the basis of one vote per member.[157] Here are three examples.

(1) We were told that some agricultural co-operatives require their members to buy shares in proportion to their contributed produce. For example, a farmer who produces 1000 litres of milk will have ten times more shares than someone who produces 100 litres of milk. This might well be a practical way of funding the co-operative, but we were then told that votes are also allocated according to shares.

(2) We were told that some multi-stakeholder co-operatives might have votes allocated to constituencies. For example, worker members in the co-operative might have 50% of the votes, and consumer members 50% of the votes, even though there might be unequal numbers of workers and consumers, with the result that the vote of one person might influence more than the vote of another.

(3) We were told that secondary co-operatives might give weighted votes to each primary co-operative member to reflect the size of the primary co-operative's own membership.[158]

3.89 It is because of this variety in current practice that this criterion of one vote per member might be controversial. We seek the views of stakeholders as to whether this should be a strict requirement, or should remain as an aspirational guideline (in which case it would not be suitable for inclusion in a statutory definition).

3.90 We have also considered whether a statutory definition could include a presumption as to one member one vote, but could leave some discretion for the registrar if an organisation applying for registration as a co-operative did not intend to operate as one member one vote but could still show that its arrangements operated along democratic principles and for the benefit of the membership. Our provisional conclusion, however, is that such discretion is undesirable and could undermine the certainty sought by the inclusion of a statutory definition.

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155 Canada Cooperatives Act (SC 1998 c 1), s 7(1)(b). Secondary co-operatives can be organised other than one vote per member: s 7(3).

156 Corporations Act 2001 (Australia), s 51M. A similar idea is reflected in the UK in the Mutuals' Deferred Shares Act 2015, s 2(1).

157 PECOL also seems to recognise a variety of voting patterns, although primacy is given to one vote per member: rr 2.4(1), (7), (8), and (12). See too: Adderley, ch 5.

158 See too: PECOL, r 5.2(4).

Consultation Question 2.

3.91 We provisionally propose a definition of a co-operative with the following ingredients.

A co-operative is:

(1) A society for carrying on any business;

(2) Mainly for the benefit of its members…

(3) …through transactions with its members;

(4) Membership is voluntary;

(5) Membership is open to all;

(6) One vote per member.

Do you agree with these elements? Are there any that you do not agree with?

3.92 In particular, do you think it accurate to describe the membership of any co-operative as "open to all", and if so why?

Retrospective effect

3.93 We have also considered to whom any new statutory definition should apply. Should it only apply to new applicants for registration after the introduction of the new definition? Or should it have retrospective effect such that, after a transitional period, all existing co-operatives would have to satisfy the definition if they were to remain registered as co-operatives?

3.94 We provisionally conclude that it should be the latter. Our current view is that it would not be appropriate to have a "two-tier" system with one regime for pre-reform co-operatives and another regime for post-reform co-operatives. Our reasons are as follows.

3.95 It would diminish the utility of having a definition at all if it only applied to some co-operatives and not others – especially when the pre-reform co-operatives would be the much greater number for years to come. Some of the other reforms considered in this consultation paper build upon the idea of a definition; if a co-operative did not satisfy the definition, those other reforms might not be applicable either. Nor should a co-operative be able to exclude itself from other reforms by choosing not to comply with a new definition.

3.96 There is precedent in requiring co-operatives to conform to a new definition. An obvious example is the Prevention of Fraud (Investments) Act 1939, which required societies to show that they were "bona fide co-operatives" or risk de-registration. Further, society law before and after that Act has evolved, and societies have been

expected to conform to new regimes, just as companies must comply with new company law as it too develops.

3.97 We think that most co-operatives already satisfy our proposed definition. But there might be some co-operatives who need to change their rules, for example in relation to voting. Societies can change their rules, so complying with a new definition need not be too burdensome. If a society does not wish to change its rules, that is perhaps confirmation that its members no longer wish to be organised as a co-operative. The society can then convert to another form – the business need not cease altogether.

3.98 There would need to be a transition period allowing societies to change their rules as necessary. We provisionally propose a transition period of 18 months. We have suggested this because it might allow societies to co-ordinate any changes with their next annual report to the FCA. (We propose 18 months rather than 12 months in case the next annual report is due too soon for the society to bring about the necessary changes.) This might further reduce any burden on societies by grouping their administrative processes together rather than requiring additional processes mid-year.

Consultation Question 3.

3.99 We provisionally propose that any new statutory definition of a co-operative should apply to all co-operatives and not only those registering after the introduction of the new definition. Do you agree?

Consultation Question 4.

3.100 We provisionally propose a transition period of 18 months for existing co-operatives to comply with any new definition. Do you agree?

Chapter 4: What is a community benefit society?

4.1 As with co-operatives, the Co-operative and Community Benefit Societies Act 2014 (CCBS Act) contains only a partial definition of a community benefit society. This chapter considers whether there should be a new statutory definition of a community benefit society, and if so what that definition should be.

THE CURRENT LAW

4.2 Section 2 of the CCBS Act 2014 provides:

> (1) A society for carrying on any industry, business or trade … may be registered under this Act as
>
> (a) …
>
> (b) a community benefit society
>
> (2) [if]…
>
> (a) … it is shown to the satisfaction of the [registrar]
>
> (i) …
>
> (ii) … that the business of the society is being, or is intended to be, conducted for the benefit of the community
>
> (b) …
>
> (c) [and] that the society's rules contain provision in respect of the matters mentioned in section 14…

4.3 Section 14 provides:

> A registered society's rules must contain provision about the following matters [including] … The objects of the society … The terms of admission of the members … the scale and right of voting … whether any or all shares are transferrable … whether any or all shares are withdrawable … whether members may withdraw from the society … The way in which the society's profits are to be applied…

4.4 Under section 29 of the CCBS Act, the Treasury has made regulations which allow a community benefit society (other than a social landlord or a charity) to make rules which unalterably restrict the society's ability to apply its assets other than for the benefit of the community.[159] This is known colloquially as an "asset lock".

[159] The Community Benefit Societies (Restriction on Use of Assets) Regulations 2006 (SI 2006/264), preserved by the operation of CCBS Act, schedule 5, and quoted in the FCA Guide (2023), para 3.4.15.

4.5 We note that section 14 says that there must be rules on certain matters, but does not say what those rules must be. For example, what rules about membership or voting are consistent with conducting business for the benefit of the community? That appears to be a decision wholly within the discretion or "satisfaction" of the registrar. And there is currently no basis in the CCBS Act on which to challenge a decision of the registrar that a society is not conducting its business for the benefit of the community.[160]

ORIGINS OF THE CURRENT LAW

4.6 The Prevention of Fraud (Investments) Act 1939 first articulated the idea of a society carrying on business for the benefit of the community. As discussed in Chapter 3, the 1939 Act was a response to a "share-pushing" scandal. As a result of that scandal, selling shares in companies was directly regulated by the 1939 Act. To prevent societies from becoming the next vehicle for fraud, an industrial and provident society had to show either that it was a "bona fide co-operative" or that its business was "conducted for the benefit of the community".[161]

4.7 In a contemporaneous internal note, the Registry of Friendly Societies (the then registrar) said:[162]

> The intention is to let in societies which … exist exclusively or mainly for a philanthropic or charitable purpose or for the promotion of social welfare … which do not aim at profit-making but seek to benefit members of the working classes who are usually not members of the society.

4.8 The Registry also issued guidance which said:

> [The society] must be able to show … that it will benefit persons other than its own members and that its business will be in the interests of the community. … regard will also be had to whether it is non-profit making and is prohibited by its rules from distributing assets among members and to matters referred to at (b), (c) and (e)…

4.9 Paragraphs (b), (c) and (e) of that guidance discussed what it meant to be a "bona fide co-operative". We have already quoted these in Chapter 3 but, since they were used to apply also to community benefit societies, we repeat them here for convenience. They provided:

> (b) … Control of the society will under its rules be vested in the members equally and not in accordance with their financial interest in the society. In general therefore the principle of "one man one vote" must obtain.
>
> (c) … Interest payable on share and loan capital will under its rules not exceed a rate necessary to obtain and retain the capital required to carry out the objects of the society…

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160 CCBS Act, section 9(3).

161 Prevention of Fraud (Investments) Act 1939, s 10.

162 We are grateful to Ian Adderley for supplying us with this internal note and the contemporaneous guidance.

(e) … There should be no artificial restriction of membership with the object of increasing the value of proprietary rights and interests. There may, of course, be grounds for restricting membership that do not offend the co-operative principle; for example, the membership … of a self-build housing society [might be limited] by the number of houses that could be erected on a particular site.

4.10 At this point, we note that the Registry considered that rules on voting, membership, and profit-making which applied to co-operatives should apply equally to community benefit societies. In other words, in their view a common set of principles underpinned both co-operatives and community benefit societies.

CURRENT GUIDANCE

4.11 The current registrar is the Financial Conduct Authority (FCA). It has issued a guide (FCA Guide),[163] which provides as follows.

4.12 The community to be benefitted could be the community at large. Or it could be a defined community, like a locality – except that this should not inhibit benefit to the community at large.[164]

4.13 A community benefit society must have members who hold shares in the society.[165] The society should usually be run democratically on the basis of one vote per member,[166] although it could deviate from this principle if it can satisfy the registrar that doing so helps it to fulfil its purpose of benefitting the community.[167]

4.14 Community benefit societies should not provide benefits contingent on membership.[168] Profits should not be distributed to people on the basis that they are members of the society.[169]

4.15 The society must conduct its business entirely for the benefit of the community, without any secondary purpose.[170] Profits must be applied for the benefit of the community (which includes developing the community benefit society itself).[171] The society must only use its assets to benefit the community; if the society sells its

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163 Financial Conduct Authority, *Registration Function under the Co-operative and Community Benefit Societies Act 2014 Guide* (May 2023).

164 FCA Guide, para 5.1.1.

165 FCA Guide, para 5.1.6.

166 FCA Guide, para 5.1.7.

167 FCA Guide, para 5.1.8.

168 FCA Guide, paras 5.1.5 to 5.1.7.

169 FCA Guide, para 5.1.10.

170 FCA Guide, para 5.1.3.

171 FCA Guide, para 5.1.9.

assets, the proceeds must be applied to benefit the community.[172] If the society dissolves, or converts to a company, the assets cannot be distributed to members.[173]

4.16 It is acceptable to pay interest on shares as a cost of capital – this is not a distribution of profits. But paying interest cannot be the primary purpose of the society.[174]

CRITICISMS OF THE CURRENT FRAMEWORK

4.17 The historic guidance of the Registry of Friendly Societies, and the current FCA Guide, state in terms that a community benefit society should not seek to make profits mainly to pay interest on shares. We discuss this in detail in Chapter 5. We do not discuss it further here. Instead, in this chapter we seek a positive definition of a community benefit society.

4.18 The criticisms of the current framework reflect those that we made in the context of co-operatives in Chapter 3, as follows. Section 2 of the CCBS Act provides no guidance on what it means to be a community benefit society, or how such a society should conduct its business for the benefit of the community. Instead, the FCA has discretion to decide whether it considers an applicant society to be a community benefit society. That discretion is unfettered by any statutory rules, and has no right of appeal. This creates uncertainty, and risks inconsistency with the rule of law.

4.19 The FCA is to be commended for setting out its approach in a guide which is clearly written. The FCA Guide is consistent with the guidance issued in 1939 by the Registry of Friendly Societies. However, there is no statutory basis for any of this guidance and no requirement that the registrar retain a similar approach to its guidelines in the future.

BENEFITS OF A NEW DEFINITION

4.20 The benefits of having a new statutory definition similarly reflect those that we suggested in the context of co-operatives in Chapter 3.

4.21 A clear statutory definition could reduce the discretion which the registrar needs to exercise in deciding whether to register a society as a community benefit society. In turn, this could make the registration function more efficient and predictable. It would also align more strongly with the rule of law.

4.22 A definition could provide an orienting framework for other topics, like what shares might be allowed and how they might be regulated. A definition could also provide a "hook" for other policy initiatives, like tax treatment. Put simply, it might be easier, for example, to develop a tax regime favourable to community benefit societies if the tax authorities know more clearly what a community benefit society is.

4.23 A definition can also have explanatory power: it can communicate quickly, in general terms, what a community benefit society is, and thus how it might be distinctive. This

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172 FCA Guide, para 5.1.12.

173 FCA Guide, para 5.1.13.

174 FCA Guide, para 5.1.11.

might help in promoting their form and activity and, as we suggested for co-operatives, in applying for funding or lobbying for policy changes.

4.24 Overall, we are provisionally of the view that there should be a new statutory definition of a community benefit society, given the potential benefits of a new definition and the criticisms of the current framework.

Consultation Question 5.

4.25 We provisionally propose that there should be a new statutory definition of a community benefit society. Do you agree in principle (subject to the formulation of a suitable definition)?

PROPOSED DEFINITION

4.26 We provisionally propose that a new statutory definition of a community benefit society should include the following ingredients: that it is a society for carrying on any business for the sole benefit of the community; and that membership is voluntary and open to all, with one vote per member.

4.27 We shall explain each ingredient in turn. There is in our list of suggested ingredients a clear overlap with our suggested definition of a co-operative in Chapter 3. This is not coincidental, for the following reasons.

4.28 The 1939 Act divided industrial and provident societies into co-operatives and community benefit societies. However, the then Registry applied similar requirements to both forms, and both forms have been bracketed together in legislation ever since.

4.29 Thus, the provisions of the CCBS Act apply to both forms without otherwise distinguishing between them. For example, the requirements of section 14 (including rules on membership and voting) apply whether the society is a co-operative or a community benefit society. If both forms of society remain bracketed together in the CCBS Act, so that its requirements apply equally to both forms, then it makes sense to treat them as similarly as possible for clarity and efficiency.

4.30 Of course, there is one major difference between co-operatives and community benefit societies in our proposed definitions: co-operatives carry on business for the benefit of their members, whereas community benefit societies carry on business for the benefit of the community. We think that, if the CCBS Act recognises two forms of corporation, then there should be a distinction between them. Our proposed distinction is clean and immediately intelligible, which again promotes clarity.

4.31 We note that there are other corporate forms, including community interest companies and charitable incorporated organisations, as well as partnerships and companies, which can be run on co-operative principles. Given the availability of a variety of corporate forms, we do not think that there is any need to blur the identity of a community benefit society to capture a wider range of activities.

4.32 **Society for carrying on any business**. This is the current wording of the CCBS Act. We have not heard of any need to change it. We do not think that the words "industry" or "trade" add anything to "business". Our proposal here aligns with our proposed definition for co-operatives.

4.33 **For the sole benefit of the community**. It is uncontroversial that the society should act for the benefit of the community. Whether it should be for the "sole" benefit of the community may generate more debate.

4.34 As noted above, the FCA Guide requires the society to act entirely for the benefit of the community and profit not be distributed to members. The authors of the *Principles of European Cooperative Law* (PECOL) agree that "general interest co-operatives" (their name for a community benefit society) may not distribute any surplus to their members.[175] In contrast, the Registry of Friendly Societies originally said that a society could register if it acted "mainly" for the benefit of the community (as quoted above).

4.35 Some stakeholders have criticised the idea that a society cannot provide benefits contingent on membership. For example, they have said that providing benefits to members can incentivise membership, which in turn generates share capital and involvement, which in turn helps a society to flourish and achieve its goals of benefitting the community.

4.36 In contrast, other stakeholders approve of the current approach of prohibiting benefits contingent on membership because it marks a clean distinction from co-operatives. One stakeholder warns that it might jeopardise the ability of a community benefit society to be charitable if there is overlap with a co-operative.

4.37 We provisionally agree with the current approach of the FCA that the sole purpose of a community benefit society should be to benefit the community, for the following reasons.

4.38 If something calling itself a community benefit society is raising funds, then those funds should be applied for the benefit of the community. Those funds should not also be applied for the benefit of private individuals – benefits should not be contingent on membership.

4.39 It may be that members of the society are residents of the community, so that benefits offered to the community can be taken up by members of the society, not in their capacity as members, but in their capacity as residents. It might even be that the only residents who take up the benefits happen to be members. None of this is objectionable as long as the benefits are extended only to residents, and do not require a beneficiary to be a member.

4.40 **Membership is voluntary and open to all**. These ingredients also appear in our proposed definition of a co-operative. They derive from the First Co-operative Principle. At the time of the 1939 Act, the then Registry also thought that the membership rules which applied to co-operatives should similarly apply to community benefit societies (as quoted above).

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[175] PECOL, r 3.6(7).

4.41 In Chapter 3, we questioned whether membership of a co-operative was indeed open to all if membership could be declined or limited. Similarly, a community benefit society might limit membership. For example, it might seek to raise money for a particular project, and once enough funding is secured, membership might be closed. It might be that open membership is an aspiration for the whole sector, rather than a requirement to be applied to individual community benefit societies. However, we think it worth canvassing the views of consultees on whether an acceptable meaning can be given to the phrase "membership is open to all" so as to make it worthwhile to retain it.

4.42 **One vote per member**. Again, this aligns with our proposed definition for co-operatives. That one vote per member should also apply to community benefit societies was the view of the then Registry at the time of the 1939 Act (quoted above), and is also the expectation stated in the current FCA Guide.[176]

4.43 In Chapter 3, we explained how co-operatives see themselves as "democratic". There, we were searching for a democratic practice which distinguished co-operatives from the voting patterns of other business forms. One vote per member seemed the best rule, but we acknowledged that this might be controversial in light of the diversity of current practice.

4.44 There may be a similar controversy applying one vote per member to the definition of a community benefit society. After all, the FCA Guide indicates that a society might be allowed to deviate from one vote per member if that helps to benefit the community.[177] For example, we have been told that a charity might become an "anchor" member of a community benefit society, and be given extra votes so as to direct the society on delivering community benefit. We have been told that one vote per member in a community benefit society might in practice be rare.

4.45 In Chapter 3, we were minded, on balance, to propose the requirement of one vote per member for co-operatives, at least provisionally to focus debate ahead of responses from consultees. Similarly, we are minded to propose provisionally one vote per member for community benefit societies, to keep aligned the two forms (co-operatives and community benefit societies) – pending the views of consultees.

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176 FCA Guide, para 5.1.7.

177 FCA Guide, para 5.1.8.

Consultation Question 6.

4.46 We provisionally propose the following ingredients for a new statutory definition of a community benefit society.

A community benefit society is:

(1) A society for carrying on any business;

(2) For the sole benefit of the community;

(3) Membership is voluntary;

(4) Membership is open to all;

(5) One vote per member.

Do you agree with these elements? Are there any that you do not agree with?

4.47 In particular, do you think it accurate to describe the membership of any community benefit society as "open to all", and if so why?

Retrospective effect

4.48 As with co-operatives, so too with community benefit societies, we have considered to whom any new statutory definition should apply. Should it only apply to new applicants for registration after the introduction of the new definition? Instead, should it have retrospective effect such that, after a transitional period, all community benefit societies would have to satisfy the definition if they were to remain registered?

4.49 We provisionally conclude that it should be the latter. We do not think it would be appropriate to have a "two-tier" system with one regime for pre-reform community benefit societies and another regime for post-reform community benefit societies. Our reasons here are the same as they were for co-operatives. We repeat them as follows.

4.50 It would diminish the utility of having a definition at all if it only applied to some community benefit societies and not others – especially when the pre-reform community benefit societies would be the much greater number for years to come. Some of the other reforms considered in this consultation paper build upon the idea of a definition; if a community benefit society did not satisfy the definition, those other reforms might not be applicable either. Nor should a co-operative be able to exclude itself from other reforms by not choosing not to comply with a new definition.

4.51 There is precedent in requiring societies to conform to a new definition. An obvious example is the Prevention of Fraud (Investments) Act 1939, which required societies to show that they were "conducted for the benefit of the community" or risk de-registration. Further, the law both before and after that Act has evolved, and societies

have been expected to conform to new regimes, just as companies or charities must comply with new law as it too develops.

4.52 We think that most community benefit societies already satisfy our proposed definition. There might be some who need to change their rules, for example around voting. Societies can change their rules, so complying with a new definition need not be too burdensome. If a society does not wish to change its rules, that is perhaps confirmation that its members no longer wish to be organised as a community benefit society. The society can then convert to another form – the business need not cease altogether.

4.53 There would need to be a transition period allowing societies to change their rules as necessary. We propose a transition period of 18 months. This might allow societies to co-ordinate any changes with their next annual report to the FCA. (We propose 18 months rather than 12 months in case the next annual report is due too soon for the society to bring about the necessary changes.) This might further reduce any burden on societies by grouping their administrative processes together rather than requiring additional processes mid-year.

Consultation Question 7.

4.54 We provisionally propose that any new statutory definition of a community benefit society should apply to all community benefit societies and not only those registering after the introduction of the new definition. Do you agree?

Consultation Question 8.

4.55 We provisionally propose a transition period of 18 months for existing community benefit societies to comply with any new definition. Do you agree?

CHARITABLE COMMUNITY BENEFIT SOCIETIES

4.56 Community benefit societies can be charitable. After all, the charitable purposes listed by the Charities Act 2011 include community development.[178] According to the Charity Commission, there are about 1467 societies registered under the CCBS Act which are charitable. Of these, 689 are regulated by the Regulator of Social Housing.

4.57 However, in England and Wales, charitable community benefit societies are "exempt charities", meaning that they cannot register with the Charity Commission. It seems that, following the passing of the CCBS Act, the expectation was that a different "principal regulator" (other than the Charity Commission) would be appointed for

[178] Charities Act 2011, section 3(1)(e).

charitable community benefit societies, but that appointment never happened.[179] Being an exempt charity has consequences for conversion into charitable incorporated organisations and for audits. Otherwise, exempt charitable community benefit societies must still comply with charity law.

Exempt charities

4.58 This section explains how charitable community benefit societies in England and Wales are exempt charities.

4.59 The Charities Act 1993 stated that the following were exempt charities:[180] any society registered under the Industrial and Provident Societies Act 1965; and any society registered under the Friendly Societies Act 1974. The 1965 Act allowed for the registration of co-operatives, and societies for the benefit of the community. The 1974 Act allowed for the registration of societies including benevolent societies, working men's clubs, and old people's homes.

4.60 Section 11(8) of the Charities Act 2006 sought to amend the 1993 Act so that the following were exempt charities: any society registered under the Industrial and Provident Societies Act 1965 which is also registered in the register of social landlords. However, section 11(8) was never brought into force. As a result, paragraph 4 of Schedule 9 to the Charities Act 2011 applies. Overall, this means that the following are exempt charities under the 2011 Act:[181] any society registered under the CCBS Act if it is also a non-profit registered provider of social housing;[182] any society registered under the CCBS Act and any society registered under the Friendly Societies Act 1974.[183]

4.61 Thus charitable community benefit societies in England and Wales are exempt charities. Exempt charities cannot register with the Charity Commission. Instead, some types of exempt charities often have a designated "principal regulator" (instead of the Charity Commission).[184] Examples include, for universities, the Office for Students, and for museums, the Department for Digital, Culture, Media and Sport.[185] The principal regulator can also refer difficult matters to the Charity Commission for the latter to use their own full statutory powers.[186] But no principal regulator has been designated for charitable community benefit societies.

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179 Con Alexander and Charities Team at Veale Wasbrough Vizards, *Charity Governance* (2nd edn 2014), para 4.71.

180 Charities Act 1993, sch 2 para (y).

181 Charities Act 2011, s 22 and sch 3.

182 Charities Act 2011, sch 3 para 26.

183 Charities Act 2011, sch 3 para 27, as amended by sch 9 para 4.

184 Charities Act 2011, s 25.

185 https://www.gov.uk/government/publications/exempt-charities-cc23/

186 Charities Act 2011, s 46 (power of Charity Commission to institute inquiries) and s 28 (duty first to consult principal regulator).

Conversion

4.62 Can a community benefit society convert into a charitable incorporated organisation? Some stakeholders have suggested that it should be able to do so.

4.63 Under the CCBS Act, societies can convert into companies,[187] and vice versa.[188] The CCBS Act does not provide that a community benefit society can convert into a charitable incorporated organisation.

4.64 However, the Charities Act 2011 provides that a charity which is a society registered under the CCBS Act can apply to convert into a charitable incorporated organisation,[189] unless the society is an exempt charity.[190]

4.65 Thus it seems that a non-charitable community benefit society must first become a charity before it can convert into a charitable incorporated organisation.

4.66 A charitable community benefit society can convert into a charitable incorporated organisation in Scotland (where community benefit societies are not exempt charities).[191]

4.67 The only gap is therefore where a charitable community benefit society in England and Wales wishes to convert into a charitable incorporated organisation. This gap only exists because, in England and Wales, charitable community benefit societies are exempt charities. If they were not exempt, then they could convert. Below, we consider whether they should no longer be exempt.

Audits

4.68 We discuss audits in detail in Chapter 7. There we propose revising the audit requirements imposed on societies by the CCBS Act.

4.69 A society might have to comply with additional audit rules beyond those found in the CCBS Act – for example, where a society operates in a sector with additional regulation. In this way, a charitable community benefit society might need to comply with charity law audit rules.

4.70 However, the charity rules on audits do not apply to exempt charities.[192] This means that charitable community benefit societies are only subject to the generalist regime of the CCBS Act, rather than the specialist regime of charity law. They would be subject to the specialist regime if they were no longer exempt charities.

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187 CCBS Act, ss 112 to 114.

188 CCBS Act, ss 115 to 117.

189 Charities Act 2011, s 229.

190 Charities Act 2011, s 229(2)(b).

191 FCA Guide, § 8.11.

192 Charities Act 2011, s 160.

No longer exempt?

4.71 Should charitable community benefit societies cease to be exempt charities?

4.72 Some stakeholders have said that charitable community benefit societies should be registered with the Charity Commission. After all, in Scotland, charitable community benefit societies are regulated by the Office of the Scottish Charity Regulator (OSCR).[193] Similarly, the Charity Commission for Northern Ireland regulates charitable community benefit societies registered under local legislation.[194]

4.73 We provisionally agree that charitable community benefit societies in England and Wales should at least be regulated as charities. If societies are raising funds on the basis that those funds will be applied to charitable purposes, the honesty and efficacy of that activity should be promoted through proper regulation. For example, it should not be possible that a society neglects its duties, gets struck off the register by the FCA, at which point it has no regulator.

4.74 There are two ways in which charitable community benefit societies might be regulated. First, they might be regulated by the Charity Commission. Second, they might remain exempt charities, and the FCA might be designated as their principal regulator.

4.75 Some stakeholders have said that exempt charities are not given charity registration numbers, which can be confusing for the society to explain. If charitable community benefit societies were no longer exempt charities, they would also be able to convert into charitable incorporated organisations; and they might have a more relevant set of audit rules. Some stakeholders have said that charitable community benefit societies should not be subjected to difference in treatment compared to other charities.

4.76 If they were no longer exempt, charitable community benefit societies would have to register with the Charity Commission, thereby ending up with multiple regulators. For example, multiple regulators might include: the FCA as registrar of community benefit societies; the Charity Commission as regulator of charities in England and Wales; where a charitable community benefit society provides social housing, then (in England) the Regulator of Social Housing, or (in Wales) the Welsh Ministers' Housing Regulation Team; or by the Care Quality Commission, if a charitable community benefit society provides health or social care in England.

4.77 It is not unusual that a charity might have overlapping regulators.[195] Ultimately, the need for different regulators reflects the fact that an organisation operates across a number of spheres where specialist regulation has been deemed to be in the public

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193 The Charities Act 2011 extends only to England and Wales. The OSCR was created by the Charities and Trustee Investment (Scotland) Act 2005.

194 Co-operative and Community Benefit Societies (Northern Ireland) Act 1969; https://www.charitycommissionni.org.uk/manage-your-charity/industrial-and-provident-societies-guidance/.

195 D Morris, "An Examination of Charity Accountability: To Whom, and How Can We Make It Better?" in Langford (ed), *Governance and Regulation of Charities: International and Comparative Perspectives* (2023) p 31.

interest. At any rate, we do not think that the response to this situation should be to exempt societies from such specialist regulation.

4.78 Multiple regulation should not be unworkable. In Scotland, there is a Memorandum of Understanding between the OSCR and the FCA concerning, for example, the mutual sharing of information concerning community benefit societies which are also Scottish charities.[196] There is also a Memorandum of Understanding between the OSCR and the Scottish Housing Regulator which deems the latter to be the "lead" regulator,[197] and another between the OSCR and the Regulator of Community Interest Companies.[198] In England and Wales, the Charity Commission has Memoranda of Understanding with a range of other regulators,[199] and we have also heard that the (English) Regulator of Social Housing already works successfully alongside the Charity Commission.

4.79 In this regard, there might be little practical difference between, on the one hand, the FCA designated as principal regulator, and on the other hand, charities being regulated by the Charity Commission who agree with the FCA for the FCA to act as lead regulator.[200]

4.80 Overall, we provisionally consider that charitable community benefit societies should no longer be exempt charities. Then charity law would apply to them in full, including the allocation of charity registration numbers, the power to convert to a charitable incorporated organisation, and the rules about audits. They would be required to register with the Charity Commission. This will produce overlapping regulation, at least between the Charity Commission and the FCA. It is not for us to propose a Memorandum of Understanding between the Charity Commission and the FCA, but we do note that similar arrangements have been successful in similar cases, and we can see sense in the FCA being designated the lead regulator.

Consultation Question 9.

4.81 We provisionally propose that charitable community benefit societies should cease to be exempt charities, so that they will be required to register with the Charity Commission. Do you agree?

196 https://www.fca.org.uk/publication/mou/mou-between-oscr-fca.pdf.

197 https://www.scottishhousingregulator.gov.uk/media/1730/oscr-and-scottish-housing-regulator-mou-october-2021.pdf

198 https://www.oscr.org.uk/media/3162/cic-mou-review-2017.pdf.

199 Including: Higher Education Funding Council for England, Fundraising Regulator, Department for Culture, Media and Sport, Secretary of State for Justice, Office for Students, Solicitors Regulation Authority, Department for Education, and the Department for the Environment, Food and Rural Affairs. See: https://www.gov.uk/government/publications.

200 We note that the CCBS Act, s 10, is premised on the FCA already considering whether a society is being conducted for charitable purposes.

Consultation Question 10.

4.82 Do you think that the lead regulator for charitable community benefit societies should be the Charity Commission or the FCA?

Chapter 5: Shares

5.1 In this chapter, we discuss shares. We explain the types of shares that are envisaged by the Co-operative and Community Benefit Societies Act 2014 (CCBS Act). We make various proposals on a range of issues concerning the law of society shares. We also ask whether societies need a new type of share.

INTRODUCTORY OVERVIEW AND SUMMARY OF PROPOSALS

5.2 This chapter involves technical detail. It is further complicated by the need to address a number of overlapping issues. We offer the following introductory overview to provide relevant background and preview what follows.

5.3 All co-operative and community benefit societies have shares. Societies are corporate bodies with limited liability. This means liability limited by shares. In comparison, some companies are limited by shares, and others are limited by guarantee. Societies are only limited by shares.

5.4 When a society is limited by shares then, if the society incurs debts, the members of the society need not contribute to paying off those debts beyond paying the price of their shares. If members have already paid for their shares, they need pay nothing more. To be a member of a society means to be a shareholder, and vice versa.

5.5 Some stakeholders say that it is uncertain what types of share can be offered by societies. We think that the CCBS Act allows for shares that are withdrawable or non-withdrawable, and transferable or non-transferable.

5.6 The CCBS Act does not define withdrawable or transferable shares. Some stakeholders say that it would increase certainty and hence usability if these concepts were defined. We think that withdrawable shares can be “cashed in”, such that the society pays the value of the share to the shareholder in exchange for the share being cancelled or returned (like cashing in a premium bond). Transferable shares can be “passed” from one person to another, such that the transferee holds that share in place of the transferor.

5.7 Different share types might have different appeal. For example, a withdrawable share might attract an investor who wants the possibility of recovering their investment. On the other hand, this means that the society might have to return the funds. A non-withdrawable transferable share might allow the society to keep the funds, and the investor might still be able to recover their investment by selling the share to someone else. That requires finding someone else to sell to, and if a society offers transferable shares, it may be further subject to the burdens of the financial services regulatory regime.

5.8 Some stakeholders say that it is uncertain what rules apply to withdrawal or transfer. They say that uncertainty can make it difficult to raise funds, either through shares themselves, or through other forms of financing which might then interact with shareholdings. Relatedly, society share law has not developed much in 150 years,

when there have been significant developments in company share law. There is a need to update society share law to ensure that shares are dealt with in ways which are fair and responsible.

5.9 We do not think it appropriate simply to transfer across company law into the CCBS Act. Societies and companies have differences which justify different rules. However, the principles which underlie company law are highly relevant; comparison to company law can inform what rules should apply to societies. In this chapter we make proposals to reform society share law.

5.10 As for the rules of withdrawal, we provisionally propose that the CCBS Act should prescribe the following minimum rule. We propose that a society should pay for withdrawable shares only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year. This is comparable to company law rules about redeemable shares and reductions in share capital. We think that society rules might set further conditions on when shares can be withdrawn if the society itself sees fit. For example, withdrawals might only be allowed at specified times of the year, or after a specified period of holding.

5.11 As for the rules of transfer, we provisionally propose that the CCBS Act should prescribe as follows: the consent of the officers of a society is needed to transfer shares; officers can in their discretion refuse a transfer of shares; their discretion must be exercised consistently with their duties as officers. (We discuss these duties further in Chapter 6.) We also propose that the CCBS Act provides that the rules of a society can set further conditions on the transfer of shares if the society sees fit, and that the rules of a society must prescribe the form for any transfer of shares. All this aligns with the position in company law.

5.12 As for further updates, there are two to mention here: protection against varying class rights; and writing down shares. Our proposals are as follows.

5.13 The CCBS Act allows for different classes of shares. In other words, different "batches" of shares might have different rights attached to them. For example, some shares might attract a higher rate of interest. What rights are attached to which shares is determined by the rules of the society. Society rules can be changed. We think that there should be protections when changes to society rules seek to change share rights. Similar protections can be found in company law.

5.14 We provisionally propose that class rights should only be changed if the change is approved by at least 75% of those affected. Even then, there should be some form of protection for minority shareholders who object to the change. If shares are changed from non-withdrawable to withdrawable, that should require a solvency statement by the officers of the society, confirmed by an auditor. A solvency statement avows that the society remains capable of paying its debts as they fall due at that time and over the following year.

5.15 Shares are "written down" when their face value is reduced. This might happen, for example, to reflect more accurately depreciation in the value of the society's assets. When a society seeks to write down its shares, we propose that that should also require a solvency statement by officers of the society, and a special resolution (a vote taken by members of the society).

5.16 There are then two further topics to discuss. First, to what extent might societies reward shareholders? For example, profitable companies might distribute their profits to shareholders. We think that societies are different. With co-operatives, we think that members should be benefitted in proportion to their transactions, not in proportion to their investments. (We discuss this also in Chapter 3.) With community benefit societies, we think that all profits should be applied to the benefit of the community, and not to private profit. (We discuss this also in Chapter 4.) But we recognise, of course, that some reward may be necessary to attract investment at all.

5.17 We propose that societies should be able to pay interest on shares, but only at rates which are both reasonable and necessary to attract investment. This rate may vary in different economic climates and according to the business of the society. And different shares might attract different rates of interest.

5.18 Further, we propose that interest on shares should be paid only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year. In other words, a shareholder has no automatic entitlement to interest on their shares.

5.19 Beyond interest on shares, might members make capital gains from their shares? In other words, could members sell their shares to others for a profit (at a higher price than the shares were originally bought for)? We do not think it necessary for statute to preclude this. A limit on payable interest will dampen capital gains, and society rules can preclude capital gains if that is thought appropriate. Society officers might even refuse a share transfer for capital gain if consistent with their duties as officers.

5.20 Finally, some stakeholders have suggested that a new type of non-user investor share should be recognised by statute. A non-user investor is someone who has invested in a society through shares, and so is a member of the society, but who does not otherwise use the services of the society. Some stakeholders have said that there should be available a non-user investor share which is non-withdrawable but transferable. In our view, these types of shares are available already – so we provisionally conclude that no reform is necessary. However, we ask stakeholders whether a new type of share with different characteristics might be needed, and if so, what that new type of share would be.

The structure of this chapter

5.21 The rest of this chapter proceeds through the following steps.

(1) What is a share?

(2) What types of share does the CCBS Act allow?

(3) Withdrawable shares: what are they, and what are the rules for withdrawal?

(4) Transferable shares: what are they, and what are the rules for transfer?

(5) What variety of shares and membership can a society offer?

(6) Does the CCBS Act need rules on changes to class rights?

(7) Does the CCBS Act need rules on writing down shares?

(8) To what extent might societies reward investors?

(9) Do societies need a new type of share?

WHAT IS A SHARE?

5.22 The CCBS Act does not define a share. The Companies Act 2006 says that "share, in relation to a company, means share in the company's share capital".[201] This takes the issue no further forward. The 2006 Act says that shares are personal property and not real estate.[202] A share creates a relationship between the corporation and the shareholder. This leads to a further multilateral contract, via the corporation's rules, between the shareholder and other shareholders.[203]

5.23 Society shares might serve more than one function. For example, they might denote membership, provide a right to vote, or represent an investment. The sale of shares can help a society raise money. They are also the limit of a member's financial liability for the debts of the society.[204]

5.24 The rights that are bestowed by the share might vary. For example, some shares give shareholders a claim to the assets of the corporation, and some do not. Some shares pay shareholders a rate of interest, and some do not. A corporation might issue different "classes" of share with different rights attached to each class.[205]

WHAT TYPES OF SHARE DOES THE CCBS ACT ALLOW?

5.25 Some stakeholders say that it is uncertain whether societies can issue non-withdrawable and transferable shares. We think that societies can issue shares which are withdrawable or non-withdrawable, and which are transferable or non-transferable, for the reasons which follow.

Current legislation

5.26 Section 14 of the CCBS Act states as follows.

> A registered society's rules must contain provision about the following matters –
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> …
>
> *9. Shares* Determination whether any or all shares are transferable, and provision for the form of transfer and registration of shares, and for the consent of the committee to transfer or registration. Determination whether any or all shares are

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201 Companies Act 2006, s 540.

202 Companies Act 2006, s 541.

203 Companies Act 2006, s 33(1); CCBS Act, s 15(1).

204 CCBS Act, s 124.

205 On class rights generally, see: *Boyle and Bird's Company Law* (10th edn 2019) para 8.9.

withdrawable, and provision for the method of withdrawal and for payment of the balance due on them on withdrawing from the society.

5.27 We think it clear that section 14 allows for the issue of transferable, non-transferable, withdrawable, and non-withdrawable shares. This is also the view of the Financial Conduct Authority (FCA),[206] and the CCBS Handbook.[207]

Past legislation

5.28 A review of the legislation which preceded the CCBS Act shows how the available types of society share has evolved over time. We provide a summary here. The legislation, which is not always available online, is quoted in Appendix 4. It repays to read the historic legislation, because the language found in the CCBS Act is a direct descendant of the language found in the earlier Acts.

5.29 The Friendly Societies Act 1846 recognised "investment societies".[208] The Act provided that shares were withdrawable and not transferable.[209]

5.30 The (first) Industrial and Provident Societies Act 1852 stated similarly that shares were withdrawable and not transferable.[210]

5.31 The Industrial and Provident Societies Act 1862 provided that shares could be transferable, and if not, then they were withdrawable.[211]

5.32 The Industrial and Provident Societies Act 1876 stated that the rules of a society were to determine whether any shares were transferable (or not), and whether any shares were withdrawable (or not).[212]

5.33 This was reworded slightly by the Industrial and Provident Societies Act 1893, but to the same effect.[213] This formulation was left unchanged in the Industrial and Provident Societies Act 1965,[214] and is very similar to the text of section 14 of the CCBS Act as it is today.

5.34 Thus, the legislative history shows that society shares were originally non-transferable, but transferable shares have been allowed since 1862.[215] Society shares were originally withdrawable, but non-withdrawable shares have been allowed since 1876. In all cases, it has been for the society, in its rules, to determine which of its

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206 FCA Guide, ch 6.

207 CCBS Handbook, p 179.

208 9 & 10 Vic c 27.

209 Friendly Societies Act 1846, s 1.

210 15 & 16 Vic c 31, s 3.

211 25 & 26 Vic c 87, s 4 and sch.

212 39 & 40 Vic c 45, s 9(1) and sch 2.

213 56 & 57 Vic c 39, s 10(1) and sch 2.

214 1965 c 12, s 1(1)(b) and sch 1 para 9.

215 Further evidence that shares can be transferable is found in CCBS Act, s 37(3).

shares are transferable or non-transferable, and which of its shares are withdrawable or non-withdrawable. That remains the position today under the CCBS Act.

Society practice

5.35 Some model rules for societies provide that shares are non-withdrawable and non-transferable.[216] Some provide that shares can be a mix of non-withdrawable and withdrawable.[217] Some provide for shares which are withdrawable and non-transferable.[218] Some provide that shares can be transferable.[219] For example, when an unincorporated association is a member of the society, it may be necessary to transfer the shares of that member to a new nominee holder on behalf of that unincorporated association member.[220] For comparison, international practice also sees some foreign co-operatives issue transferrable shares.[221] In other words, current practice already recognises the four main types of society share.

Conclusion

5.36 It seems to us beyond doubt that society shares can be withdrawable or non-withdrawable, and transferable or non-transferable. This is clear from the CCBS Act itself, especially in light of its legislative history. It is also consistent with society practice.

5.37 Further, it is for societies by their rules to determine which of their shares are withdrawable or non-withdrawable, and transferable or non-transferable. Again, the CCBS Act says so explicitly. Put simply, there is no-one else in a position to make that determination.

5.38 Nevertheless, if the CCBS Act is to be amended anyway, it might be best if the CCBS Act used modern language to state explicitly that society shares can be withdrawable or non-withdrawable, and transferable or non-transferable, and that it is for societies by their rules to determine which of their shares are withdrawable or non-withdrawable, and transferable or non-transferable. We do not wish any stakeholder reading the CCBS Act to be in any doubt here.

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216 Co-operatives UK & Confederation of Co-operative Housing Fully Mutual Housing Co-op Model Rules.

217 Co-operatives UK Co-operative Consortium Model Rules.

218 https://www.uk.coop/resources/community-shares-handbook-cs.

219 Co-operatives UK Multi-Stakeholder Model Rules, Co-operative Consortium Model Rules, Worker Co-operative Model Rules, Community Benefit Society Model Rules.

220 For example, Co-operatives UK Co-operative Consortium Model Rules, Community Benefit Society Model Rules.

221 Filene Research Institute, *Survey of Co-operative Capital* (2015); ICA, *The Capital Conundrum for Co-operatives* (2017).

Consultation Question 11.

5.39 We provisionally propose that the CCBS Act should be amended to state explicitly as follows.

(1) Society shares can be withdrawable or non-withdrawable, and transferable or non-transferable.

(2) It is for societies by their rules to determine which of their shares are withdrawable or non-withdrawable, and transferable or non-transferable.

Do you agree?

Financial services regulation

5.40 The CCBS Act allows societies to issue shares which are withdrawable or not, and transferable or not. However, any share issue might need to comply with further regulation outside the CCBS Act.

5.41 Particular regard should be had to the Financial Services and Markets Act 2000 (FSMA).[222] For example, in very broad terms, the FSMA prohibits anyone from carrying on a regulated activity unless authorised or exempted. Regulated activities include dealing in investments, and investments include shares. Also, if transferable shares are offered to the public, then a prospectus must be approved and published.[223]

5.42 If societies issue transferable shares, such shares may well fall within the FSMA regime.[224] Transfers might be subject to stamp duty, and any capital gains might also be taxable.[225] In contrast, non-transferable withdrawable shares are usually exempt from the FSMA regime.[226] Overall the FSMA and tax regime is detailed and complex. Societies should take advice to ensure that their share offerings are compliant.

WITHDRAWABLE SHARES

Current law and practice

5.43 The CCBS Act states that it is for the rules of a society to make "provision for the method of withdrawal and for payment of the balance due on [the shares] on

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222 For an overview, see: CCBS Handbook, ch 8.7; Community Shares Handbook, ch 7; Adderley, ch 8.

223 Community benefit societies have certain exemptions when it comes to a prospectus: FSMA, sch 11A, para 7(2)(d).

224 FCA Guide, para 6.1.14; The Financial Services and Markets Act 2000 (Regulated Activities) Order (SI 2001 No 544) r 76.

225 Community Shares Handbook, para 8.1.

226 FCA Guide, para 6.1.20; The Financial Services and Markets Act 2000 (Regulated Activities) Order (SI 2001 No 544) r 76; The Financial Services and Markets Act 2000 (Exemption) Order 2001 (SI 2001 No 1201) r 4, sch 1 para 24.

withdrawing from the society".[227] The general rule is a member may not have withdrawable shares in excess of £100k.[228] A society which has any withdrawable share capital may not be registered with the object of carrying on the business of banking.[229] It is not treated as banking to take deposits of less than £400,[230] but a society which takes deposits must not make any payment of withdrawable capital while any payment due on account of any deposit is unsatisfied.[231]

5.44 The FCA Guide says that a society should only allow the withdrawal of shares if the following conditions are met.[232]

(1) Trading surpluses must at least match the value of shares being withdrawn.

(2) The society can afford to pay its other debts, actual and likely, now and over the coming year.

(3) The society can suspend withdrawals, for example if the society's financial position becomes uncertain.

5.45 These rules in the FCA Guide have no counterpart in the CCBS Act. They may be financially sensible rules designed to protect the solvency of the society as a whole, but it seems unlikely that the FCA is empowered to insist upon them.

5.46 Having said that, point (3) is reflected in society practice. Model rules tend to provide that a society's board may, at their sole discretion, suspend the right to withdraw, with such suspension being whole or partial, and either indefinitely or for a fixed period.[233] Without this discretion, share capital provided through the sale of withdrawable shares must be accounted for as a liability rather than as capital.[234]

5.47 Some stakeholders suggest that withdrawal of society shares is also governed by the common law, by rules analogous to those which were initially developed with respect to companies.

5.48 We think that this view requires caution. While the courts can of course develop case law to regulate the withdrawal of society shares, it is not necessarily the case that the content of those rules will be held to match company case law. The latter developed within a framework of company legislation, which might have skewed how the case law developed. Also, much of the historic company case law has been overwritten by

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227 CCBS Act, s 14.

228 CCBS Act, s 24.

229 CCBS Act, ss 4(1), 67(1).

230 CCBS Act, s 67(2).

231 CCBS Act, s 67(3).

232 pa FCA Guide, paras 6.1.10 and 6.1.11.

233 For example, see: Co-operatives UK Multi-Stakeholder Model Rules, Worker Co-operative Model Rules, Community Benefit Society Model Rules. This may be necessary if withdrawable share capital is to be treated as equity (rather than a debt liability) for the accounting purposes of the International Financial Reporting Standards: IFRIC 2; Adderley, Ch 8.

234 IFRIC 2, *Members' Shares in Co-operative Entities and Similar Instruments*. https://www.ifrs.org/issued-standards/list-of-standards/ifric-2-members-shares-in-cooperative-entities-and-similar-instruments/.

modern company legislation. To the extent that modern courts seek best practice when developing society law, they might be more inclined to look at current standards in legislation rather than case law standards long since varied.

Possible definition

5.49 There is no definition of a withdrawable share in the CCBS Act, nor in the FCA Guide. The CCBS Handbook says (only) that withdrawable shares provide a mechanism for members to "sell" their shares back to the society.[235] Some stakeholders have said that it would increase clarity and hence usability if there were to be a statutory definition.

5.50 In seeking a definition of withdrawable shares, we can turn to company law for comparison.

Company law comparison

5.51 Company law does not provide for withdrawable shares. But it does have "redeemable" shares. Some stakeholders say that the company law rules on redeemable shares should apply to society shares.

5.52 Redeemable shares are defined as shares that "are to be redeemed or are liable to be redeemed" [236] – that is, those that can be bought back by the company. This can occur at the option of either the shareholder or the company.[237] Once redeemed, the shares are treated as cancelled.[238] This means that the shares no longer exist.

5.53 Redeemable shares are not the only comparison in company law. Additionally, a company can also purchase its own shares through a separate process, even if those shares were not initially labelled as redeemable.[239] Once bought back, those shares are again cancelled, unless they are held as "treasury" shares.[240]

5.54 Treasury shares are where a company buys back and holds its own shares, paying for them from the company's distributable profits.[241] With treasury shares, the company cannot vote or receive a dividend in respect of the shares, or share in the distribution of assets,[242] but it can sell the shares,[243] or cancel them.[244]

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235 CCBS Handbook, p 179.

236 Companies Act 2006, s 684(1).

237 Companies Act 2006, s 684(1).

238 Companies Act 2006, s 688.

239 Companies Act 2006, s 690.

240 Companies Act 2006, s 706.

241 Companies Act 2006, s 724.

242 Companies Act 2006, s 726.

243 Companies Act 2006, s 727.

244 Companies Act 2006, s 729.

5.55 The common theme here is that shares which are redeemed or bought back tend towards a baseline of cancellation. This coincides with society practice: some model rules for societies also say that withdrawn shares are cancelled.[245]

Discussion

5.56 We agree that the CCBS Act should provide a definition of a withdrawable share. This would provide clarity.

5.57 We think that a share is withdrawn when a society pays the value of the share, to the holder of the share, in return for the share being cancelled.

5.58 We do not suggest a move towards the language of "redeemable", as used in company law. That seems to us to compound the need for definition, rather than provide a definition. It also imports a word from company law which is not used in society law.

5.59 Also, we do not think it correct to describe members selling their shares to the society, or the society buying them back. The word "withdrawable" better accords with the idea of cashing in an entitlement, like withdrawing money from a bank account in credit, or cashing in premium bonds. When a share is withdrawn, there is no contract of sale. Rather, a member puts in money, and then takes it out again.

5.60 Usually it is the member who wishes to withdraw their shares. But some model rules provide that a society can insist on a member withdrawing their shares.[246] Thus, shares can be withdrawn at the option of either the member or the society, depending on the society's rules.

5.61 Our provisional view is that a withdrawn share should be considered cancelled. This means that the share is extinguished or no longer exists. This is consonant with company law and with society practice (noted above). The only alternative would be societies retaining the shares as treasury shares, to issue to someone else later. We are not aware of societies wishing to retain treasury shares and therefore we suggest that there is no need for this added complexity. Societies can always issue new shares to new members (without having to recycle treasury shares). Indeed, this can be a major difference from companies: the number of shares in a company tends to be fixed, although it can be changed with effort, whereas the number of shares in a co-operative can naturally fluctuate as membership changes.[247]

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245 For example, see: Co-operatives UK Multi-Stakeholder Model Rules, Worker Co-operative Model Rules, Community Benefit Society Model Rules.

246 Baywind Renewable Energy Model Rules Version 2; Sharenergy Model Rules.

247 See too: Adderley, ch 8.

Consultation Question 12.

5.62 We provisionally propose that the CCBS Act should provide a definition of a withdrawable share. Do you agree?

Consultation Question 13.

5.63 We provisionally propose the following ingredients of a definition of a withdrawable share.

(1) A withdrawable share can be cashed in, such that a society pays the value of the share, to the holder of the share, in return for the share being cancelled.

(2) A withdrawable share can be withdrawn at the option of the member or the society, depending on the society's rules.

Do you agree with each of these elements?

Rules for withdrawal

Stakeholder views

5.64 Some stakeholders have said that there is uncertainty about when a withdrawable share can be withdrawn. They say that the CCBS Act should set out rules for withdrawal, to increase certainty, and hence usability of withdrawable shares. In particular, some stakeholders have suggested that the CCBS Act should address the following.

(1) Whether societies can require long notice periods from members wishing to withdraw.

(2) Whether withdrawal might be allowed only after the member has held the shares for a certain period of time.

(3) Whether withdrawal can be restricted to certain prescribed times (like an annual window for withdrawal).

(4) Whether a society can limit or suspend withdrawals, despite a member wishing to withdraw.

(5) Whether withdrawal should only be permitted if the society can show that paying for the shares would not endanger its solvency.

5.65 Some stakeholders suggest that the rules found in the Companies Act 2006, for example in respect of redeemable shares, should govern the withdrawal of society shares.

Company law comparison

5.66 There are three comparable situations in company law: when company shares are redeemed; when company shares are bought back; and when a company reduces its share capital. We discuss all of them here.

5.67 A private limited company can issue redeemable shares unless this is excluded or restricted in its articles.[248] A public limited company may only issue redeemable shares if its articles provide for this.[249] A company cannot issue redeemable shares at a time when it has no issued shares that are not redeemable.[250]

5.68 Shares are redeemed by a public company paying from its distributable profits or another share issue.[251] In the case of a private company, they can also be paid for from the company's capital.[252] Otherwise, the articles of the company state the terms and manner of redemption,[253] or the company directors may be authorised to do so.[254] When shares are redeemed, notice must be given to the registrar.[255]

5.69 A limited company with a share capital may purchase its own shares (including redeemable shares) unless this is restricted or prohibited in the articles.[256] A company may not purchase its own shares if that would result in there being no issued shares of the company other than redeemable shares or treasury shares.[257]

5.70 As with redeemable shares, a public company must pay for the purchase of its shares from its distributable profits or a new share issue.[258] A private company may also purchase its own shares out of capital.[259] The rules for purchases out of capital do not apply if the total purchase price for the year is below the lower of £15k or 5% of share capital.[260]

5.71 Payment out of capital, whether for redeemable shares or the purchase of a company's own shares, requires a statement by the directors that, in their opinion, the company will be able to pay its debts at that time, and will be able financially to continue as a going concern, and pay its debts as they fall due, over the following year.[261] An auditor must confirm that they are not aware of anything to indicate that

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248 Companies Act 2006, s 684(2).

249 Companies Act 2006, s 684(3).

250 Companies Act 2006, s 684(4).

251 Companies Act 2006, s 687(2).

252 Companies Act 2006, s 687(1).

253 Companies Act 2006, s 685(4).

254 Companies Act 2006, s 685(1).

255 Companies Act 2006, s 689.

256 Companies Act 2006, s 690(1).

257 Companies Act 2006, s 690(2).

258 Companies Act 2006, s 692(2).

259 Companies Act 2006, s 692(1).

260 Companies Act 2006, s 692(1ZA).

261 Companies Act 2006, s 714.

the directors' opinion is unreasonable.[262] The payment must also be approved by a special resolution of the company.[263] The intended payment must be advertised. [264] An application can be made to court to challenge the payment by a creditor or any member who did not vote in its favour.[265]

5.72 Separately, a company can reduce its share capital.[266] It can do this in any way.[267] For example, a company may: extinguish or reduce the liability on any of its shares in respect of share capital not paid up; cancel any paid-up share capital that is lost or unrepresented by available assets; or repay any paid-up share capital in excess of the company's wants.[268]

5.73 A reduction in share capital requires either a solvency statement and special resolution passed by a private company, or a special resolution confirmed by the court.[269] The solvency statement is a statement by the directors that, in their opinion, the company is able to pay its debts at that time and as they fall due over the following year.[270] If the company applies to court, then creditors can object if they think that the company will not be able to pay its debts.[271]

5.74 Thus, in summary, a company can redeem or buy back shares out of its profits or a new share issue. Or a company can redeem or buy back shares out of its capital, or otherwise reduce its share capital, but this requires at least a solvency statement and a special resolution. These are all minimum conditions. The articles of a company can set further conditions about the terms and manner for redeeming shares,[272] purchasing its own shares,[273] or reducing share capital.[274]

Discussion

5.75 We provisionally conclude that the CCBS Act should prescribe minimum conditions to be satisfied for the withdrawal of society shares. Without such specification in the CCBS Act, there are two possibilities, as follows, and we think that neither is satisfactory.

5.76 One possibility is that there is simply no governing law at all. The absence of any protections seems difficult to justify, especially when company law has seen fit to

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262 Companies Act 2006, s 714(6)(c).

263 Companies Act 2006, s 716.

264 Companies Act 2006, s 719.

265 Companies Act 2006, s 721.

266 Companies Act 2006, Pt 17, ch 10.

267 Companies Act 2006, s 641(3).

268 Companies Act 2006, s 641(4).

269 Companies Act 2006, s 641(1).

270 Companies Act 2006, s 643.

271 Companies Act 2006, s 646.

272 Companies Act 2006, s 685.

273 Companies Act 2006, s 690(1)(b).

274 Companies Act 2006, s 641(6).

develop rules for similar scenarios. The FCA Guide has rules, but they do not seem to have any legal force.

5.77 The other possibility is that the courts would have to develop common law rules. Until then, the law would be uncertain. It may be that the courts never have the opportunity to identify those common law rules, as it requires cases which include the necessary issues in order for the principles to be decided. This could severely constrain societies in their ability to use withdrawable shares or raise other finance against the backdrop of withdrawable shares.

5.78 We think that the CCBS Act need only prescribe minimum conditions for withdrawing shares. Over-regulation might otherwise inhibit flexibility and the development of new practices. Society rules could set further conditions if the society saw fit (as with company law), and the CCBS Act could provide for this explicitly (again, as with company law). This could provide societies with the authority which they feel they need to impose terms like notice periods.

5.79 Our current view is that there should be one minimum condition: a society should pay for withdrawable shares only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year. This aligns suitably with company law's emphasis on solvency when reducing share capital, and there is a similar requirement in the FCA Guide (as noted above). Effectively this means that societies must suspend withdrawals if they cannot afford to pay for them. As noted above, a society's rules could allow for suspension of withdrawals in other circumstances.

5.80 We have provisionally concluded that societies need not produce a solvency statement when paying for withdrawable shares. A society can have a fluctuating membership of people joining and leaving. Those leaving might seek to withdraw small sums which have a negligible effect on the society. It may be too much to require a solvency statement each time a withdrawal is requested. Similarly, it may be too much to require all members to vote on each and every withdrawal. And we currently see no need to notify the registrar of every withdrawal.

5.81 Contrary to the FCA Guide, we do not think that withdrawable shares need only be paid for out of a trading surplus. With a company, a distributable profit is pure profit.[275] With a co-operative, for example, a trading surplus might indicate that members were overcharged in a consumer co-operative or underpaid in a worker co-operative. This could lead to a price adjustment by way of a member dividend. Put another way, an absence of trading surplus in a co-operative could be an indication of correct advance pricing. A trading surplus is not necessarily an indicator of solvency, nor does it constitute pure profit.

5.82 Instead, societies might budget responsibly for withdrawals in various ways. One obvious example might be new shares bought by new members. Similarly, company law allows shares to be redeemed or bought back by funds from new share issues (as noted above).

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[275] Companies Act 2006, ss 736 and 830.

5.83 We do not think that paying for withdrawable shares need be all or nothing. A society considering requests for withdrawal might conclude that it can only afford to pay a proportion of the sought withdrawals rather than all of them. We think that it should be possible for a society to do so, hence our provisional proposal refers to payment "to the extent" that the society can afford it.

5.84 Finally, company law prohibits companies from having only redeemable shares. That is not applicable to societies. Societies have always been able to offer only withdrawable shares – indeed, that was historically the only share type which could originally be offered. We have not heard of any need to change this.

Consultation Question 14.

5.85 We provisionally propose that the CCBS Act should set out the minimum conditions for withdrawing shares. Do you agree?

Consultation Question 15.

5.86 We provisionally propose that the CCBS Act should provide that society rules can set extra conditions for withdrawing shares. Do you agree?

Consultation Question 16.

5.87 We provisionally propose that the minimum conditions for withdrawing shares should be as follows.

A society should pay for withdrawable shares only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year.

Do you agree?

5.88 In particular, we think that a society considering requests for withdrawal should be able to pay a proportion of the sought withdrawals, rather than all or nothing, if that is what it can afford. Do you agree?

TRANSFERABLE SHARES

Definition

5.89 Some stakeholders say that a definition should be provided of what it means for shares to be transferable. They say that this would improve certainty, and hence usability of transferable shares.

5.90 There is no definition of a transferable share in the CCBS Act. The FCA Guide does not define a transferable share, nor does the CCBS Handbook.

5.91 There is no definition of transferable share in the Companies Act 2006. It simply says that company shares are transferable.[276] There is a definition of "transferable securities", which are "those classes of securities which are negotiable on the capital market…such as shares in companies".[277] This is too circuitous to be helpful.

5.92 As with withdrawable shares, so too with transferable shares, we think that the CCBS Act should provide a definition, for clarity. We think that a transferable share can be "passed" from one person (the transferor) to another person (the transferee) such that the transferee holds a share in place of the transferor. We do not suggest that transferable shares are only those that can be bought and sold. Transfer might be for other reasons: for example, sale or gift.

Consultation Question 17.

5.93 We provisionally propose that the CCBS Act should provide a definition of a transferable share. Do you agree?

Consultation Question 18.

5.94 We provisionally propose that a transferable share be defined as one that can be passed from one person to another such that the transferee holds the share in place of the transferor. Do you agree?

Rules for transfer

5.95 The transfer of shares is addressed by the CCBS Act – albeit minimally. Section 14 says (only) that society rules must make "provision for the form of transfer and registration of shares, and for the consent of the committee to transfer or registration".

5.96 Some stakeholders say that it is uncertain when a transferable share can be transferred. They say that the CCBS Act should prescribe rules as to when shares can be transferred, for certainty, and hence to increase the usability of transferable shares.

5.97 Some stakeholders suggest that, as with withdrawable shares, so too the transfer of society shares is already governed by the common law, by rules analogous to those which were initially developed with respect to companies.

5.98 Once again, we think that this view requires some caution, and we repeat our reasons. Company case law developed within a framework of company legislation

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276 Companies Act 2006, s 544.

277 Companies Act 2006, s 1173; art 2.1.24 of Regulation (EU) No 600/2014; art 4(1)(44) of Directive 2014/65/EU.

which might have skewed how the case law developed. Also, much of the historic company case law has been overwritten by modern company legislation. To the extent that modern courts seek best practice when developing society law, they might be more inclined to look at current standards in legislation rather than company case law standards long since varied.

5.99 Taking our cue from the CCBS Act, we take these points in turn: first, form of transfer; second, consent of the committee.

Form of transfer

5.100 To repeat, the CCBS Act only requires society rules to provide for the form of transfer. It does not specify a default form. Should the CCBS Act provide a default form for the transfer of shares?

5.101 In company law, the default rule is that a company may not register a transfer of shares unless a proper instrument of transfer has been delivered to it.[278] A "proper instrument" means a written instrument, but it might take any form.[279] The articles of the company might prescribe the form. Otherwise, the Stock Transfer Act 1963 provides a default form. But societies registered under the CCBS Act are excluded from the Stock Transfer Act 1963.[280]

5.102 One option might be to adapt the default form of the Stock Transfer Act 1963 to be applicable to societies, and append it to the CCBS Act. Another option might be to leave it to the sector to decide what form would be most fitting. (The sector could adapt the Stock Transfer Act form if it so desired.)

5.103 We have provisionally concluded that the form of any transfer is best left to the sector, or to individual societies, as they are likely to be a better judge of their administrative needs in this context. We have been given no guidance from stakeholders on what a form of transfer should look like.

Consultation Question 19.

5.104 We provisionally conclude that the form of transfer should be left to the sector to determine rather than prescribed in legislation. Do you agree?

If you do not agree, please detail what form you consider should be prescribed.

Consent of the committee

5.105 To repeat, section 14 of the CCBS Act says that society rules must make provision "for the consent of the committee to transfer or registration".

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278 Companies Act 2006, s 770. For computerised transfer of shares, see: Stock Transfer Act 1982; Companies Act 2006, Pt 21, ch 2; The Uncertificated Securities Regulations 2001 (SI 2001 No 3755).

279 *Boyle and Bird's Company Law* (10th edn 2019) para 9.7.

280 Stock Transfer Act 1963, s 1(4)(b).

5.106 In our view, this means that the CCBS Act requires the committee to consent to any transfer. This is also the view of the FCA Guide.[281] It is a rule recognised by the authors of the *Principles of European Cooperative Law* (PECOL).[282] Some model society rules also provide for this expressly.[283]

5.107 The question therefore arises whether society officers should be able to reject an application for the transfer of shares.

5.108 In company law, directors of private companies can be empowered to reject applications for the transfer of company shares.[284] Their discretion to do so is bounded by their general duties as directors to promote the success of the company.[285] The articles of the company might impose further restrictions on when shares can be transferred.[286]

5.109 We think that officers of a society should be able to reject a transfer of shares. This might be appropriate, for example, where they would reject an application for membership from the transferee.

5.110 Our provisional view is that it would increase certainty if the CCBS Act were to state that: consent is needed from society officers to any transfer of shares; officers can refuse to allow a transfer of shares, in their discretion; and that this discretion must be exercised consistently with their duties as officers. (Officer duties are discussed in Chapter 6.)

5.111 If instead there were no such specification in the CCBS Act, as with withdrawable shares, so too with transferable shares, either this means that there are no rules at all, so that share transfer is something of a free-for-all, or it requires the courts to develop common law rules, with the law uncertain and transferable shares potentially unusable until then. Neither of these outcomes is satisfactory.

5.112 Also, we think that the rules of a society should be able to set further conditions on the transfer of shares (as with company law). Such conditions might limit still further when transfers are allowed. We see no objection should the rules limit any discretion that an officer might otherwise have exercised.

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281 FCA Guide, paras 6.1.12 and 6.1.13.

282 PECOL, r 3.3(6).

283 For example, Co-operatives UK Multi-Stakeholder Co-operative Model Rules, Community Benefit Society Model Rules.

284 Companies Act 2006, s 771.

285 *Boyle and Bird's Company Law* (10th edn 2019) para 9.3.

286 Companies Act 2006, s 544.

Consultation Question 20.

5.113 As for transferable shares, we provisionally propose that the CCBS Act should be amended to state as follows.

(1) The consent of officers of a society is needed to transfer shares.

(2) Officers can in their discretion refuse a transfer of shares.

(3) Their discretion must be exercised consistently with their duties as officers.

(4) The rules of a society can set further conditions on the transfer of shares.

(5) The rules of a society must provide for the form of any transfer of shares.

Do you agree with each proposition?

VARIETY OF RIGHTS

5.114 What variety of shares and membership can a society offer?

5.115 As we have seen, the CCBS Act allows societies to issue shares that are withdrawable, non-withdrawable, transferable, and non-transferable. There is nothing in the CCBS Act to preclude a society offering several types of these shares. For example, a society might offer some withdrawable shares, and some non-withdrawable shares.

5.116 Also, there is nothing in the CCBS Act to preclude further subdivision. For example, a society might issue two types of non-withdrawable share, each with different terms attached. Some shares might attract a higher rate of return than others. This possible diversity of share class rights is acknowledged by the CCBS Handbook,[287] and the Community Shares Handbook.[288] International practice also sees foreign co-operatives issue a range of different classes of shares with different rights attached.[289]

5.117 Similarly, the CCBS Act allows for different classes of members with different membership rights.[290] Some model rules provide for different types of membership (such as founder members, employee members, and so on).[291]

5.118 Societies can issue shares to non-user investors. These are people who buy shares to invest in the society, and thereby become members of the society, but who otherwise do not use the services of the society. Their only relationship with the society is as an

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287 CCBS Handbook, p 179.

288 https://www.uk.coop/resources/community-shares-handbook-cs para 2.2.5.

289 Filene Research Institute, *Survey of Co-operative Capital* (2015); ICA, *The Capital Conundrum for Co-operatives* (2017).

290 CCBS Act, ss 21(2), 45(3), 49(4).

291 For example, Co-operatives UK Multi-Stakeholder Co-operative Model Rules.

investor. For example, they might not transact with a co-operative, or participate in the community serviced by a community benefit society. The FCA Guide recognises the availability of non-user investor shares.[292] Indeed, the registrar has recognised these since 2006,[293] following their recognition in European law.[294] The Community Shares Handbook even recognises different classes of investor (such as "pioneer investors").[295]

5.119 For maximum clarity, we think that the CCBS Act should state all this explicitly.

Consultation Question 21.

5.120 We provisionally propose that the CCBS Act should state as follows.

(1) A society can have different classes of membership with different rights.

(2) A society can issue different classes of shares with different rights.

(3) A society can issue shares to non-user investors.

Do you agree?

CHANGES TO CLASS RIGHTS

5.121 Society rules can identify what shares or membership rights the society offers. But society rules can be altered by the society. This means that the society can change what rights avail which shares or members.

5.122 Should the CCBS Act regulate changes to class rights? This has not been raised by stakeholders, but we think that it is an important modernisation to consider, given the comparison with company law.

5.123 Currently, there is nothing in the CCBS Act to govern changes to class rights. This means that the matter is governed only by the rules of the society, with those rules themselves setting out how they can be changed.

5.124 Changes to class rights could be dramatic. For example, withdrawable shares might be changed to non-withdrawable. That would obviously affect the holder of the shares, who can no longer recover their investment. Equally, non-withdrawable shares might be changed to withdrawable. That could affect creditors because, if shares are withdrawn, the society might have fewer assets for a creditor to enforce their debt against. It could also affect members because the society might find it harder to carry on business with reduced funding. Other changes to class rights might be less

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292 FCA Guide, paras 6.1.27 and 6.1.30.

293 CCBS Handbook, p 182.

294 Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society, art 14(1).

295 Community Shares Handbook, para 4.3.

dramatic, but still significant: for example, an interest rate paid on shares might be reduced.

5.125 As with withdrawable and transferable shares, so too with changes to class rights: if the CCBS Act remains silent, either this means that there are no rules at all, or it requires the courts to develop common law rules, with the law uncertain until then (no such rules currently exist). Neither of these positions is satisfactory when changes to class rights could potentially be so significant.

5.126 In contrast, company law has developed the following rules which govern changes to class rights.

5.127 In company law, rights attached to a class of shares, or rights of a class of members, can only be varied in accordance with the company's articles, or in the absence of such provision, through a special resolution or otherwise with the consent of at least 75% of those affected shareholders or members.[296] Even then, a minority of at least 15% of shareholders or members can apply to court to cancel the variation for unfair prejudice.[297] Unfair prejudice is a legal concept that means that the company is being run in a way that is clearly unfair in its consequences to the complainant, or contrary to their legitimate expectations (even if the company is acting in good faith).[298]

5.128 Additionally,[299] and more generally, an individual member can petition the court to complain that the company's affairs are being conducted in a manner which is unfairly prejudicial to some part of its members (including the complainant).[300] The court can make any order it thinks fit,[301] including an order that the company purchase the shares of the complainant.[302] It has been suggested that, in most cases, this will be "the most attractive choice" of remedy.[303]

5.129 Further still, a member can petition the court to wind up a company on the basis that it is just and equitable to do so.[304] Winding up is a drastic option, because the company will cease to exist. The court will not order the company to be wound up on the just and equitable basis if there is an alternative remedy available to the petitioner which makes it unreasonable to pursue the winding up.[305] An offer by the company to buy the petitioner's shares at a fair price might be such an alternative remedy.[306]

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296 Companies Act 2006, ss 630 to 631.

297 Companies Act 2006, ss 633 to 634.

298 *Boyle and Bird's Company Law* (10th edn 2019) para 18.21.

299 Companies Act 2006, s 632.

300 Companies Act 2006, s 994.

301 Companies Act 2006, s 996(1).

302 Companies Act 2006, s 996(2)(e).

303 *Boyle and Bird's Company Law* (10th edn 2019) para 18.30.

304 Insolvency Act 1986, s 122(1)(g).

305 Insolvency Act 1986, s 125(2).

306 *Boyle and Bird's Company Law* (10th edn 2019) para 18.28.

5.130 In light of the above, we think that there should be three rules governing changes to class rights for societies, as follows.

5.131 First, we think that class rights should only be changed if the change is approved by at least 75% of those affected.[307] This aligns with company law (as noted above). We think that this should be the minimum threshold; the rules of a society might set a stricter threshold.[308] We think that it would be unfair if rights were changed without a vote by those affected.

5.132 Second, if shares are changed from non-withdrawable to withdrawable, we think that this should require a solvency statement from directors confirmed by an auditor. This is because of the impact which this particular structural change could have on creditors and on the viability of the society. It is somewhat akin to a company redeeming or buying back its shares: changing society shares from non-withdrawable to withdrawable suggests that the shares are likely to be withdrawn.

5.133 Third, we note that company law allows a dissatisfied shareholder to petition the court even where the change to class rights is otherwise approved by at least 75% of those affected. We think that a similar protection might be appropriate for society shareholders. In this regard, there are four possible options.

(1) In society law, a complainant can already petition the court to wind up a society on the basis that it would be just and equitable to do so.[309] Perhaps this is sufficient, especially if a society might avoid being wound up by buying out the complainant's interest. However, it involves the time and cost of applying to court; and (the threat of) winding up is drastic.

(2) Alternatively, the CCBS Act might be amended to allow a complainant to petition the court on the basis that any change to class rights would be unfairly prejudicial. Remedies might include cancelling the change, or requiring the society to buy out the complainant's interest.

(3) A different alternative is that if the various pathways tend towards an outcome whereby the complainant's interests are bought out, then it might be more efficient simply for the CCBS Act to prescribe this remedy. In this way, a complainant who objects to any change in their class rights could insist on having their interest bought out. This would be cheaper and quicker than applying to court. On the other hand, there would be no threshold requirement of unfair prejudice, meaning that a society would always have to buy out objecting shareholders – whether a society can afford that will depend on the circumstances. Depending on the terms of the share, the price may simply be face value or may alternatively be a fair market price.

(4) A final option might be that any change, even if otherwise approved by at least 75% of those affected, takes no effect against anyone who objects in writing.

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307 A similar threshold is found in the CCBS Act, s 44 (ratification of actions of committee members).

308 We discuss how society rules might set stricter thresholds than the CCBS Act in other circumstances, in Chapter 7.

309 For discussion, see: CCBS Handbook, pp 295 to 296.

For example, it is already the case under the CCBS Act that, where the change seeks to increase the financial liability of a member, it does not bind the member unless they positively consent in writing.[310] However, this approach could hinder a society from making necessary changes, and it could result in administrative complexity if different people end up with different rights (in effect, it could multiply the subdivisions of class rights).

5.134 We think that there should be some protection for minority shareholders who object to a change in their class rights, but we seek the views of consultees on which approach would be most suitable.

Consultation Question 22.

5.135 We provisionally propose, in the context of changes to class rights of shares or members, that the CCBS Act should provide as follows.

(1) Class rights should only be changed if the change is approved by at least 75% of affected shareholders or members.

(2) Society rules could set a higher threshold.

(3) If shares are changed from non-withdrawable to withdrawable, that should require a solvency statement by the officers of the society, confirmed by an auditor.

Do you agree with each element?

310 CCBS Act, s 15(2).

Consultation Question 23.

5.136 We think that there should be some protection for shareholders who still object to any change in their class rights. Which of the following protections do you think is suitable? You can select more than one, or indicate your preferred option.

(1) A complainant could petition the court to wind up a society on the basis that it would be just and equitable to do so.

(2) A complainant could petition the court on the basis that any change to class rights would be unfairly prejudicial.

(3) A society would have to buy out an objecting shareholder.

(4) Any change would not take effect against a shareholder who objects in writing.

If you think that there should be a different protection, please explain.

WRITING DOWN SHARES

5.137 Shares have a nominal value (face value). Shares are "written down" when their nominal value is reduced. This might happen, for example, when the value of assets, bought by the money from shares, has depreciated. Written down shares then more accurately reflect the value of the corporation's assets.

5.138 Some model society rules provide for writing down shares.[311] The FCA Guide also appears to accept that shares can be written down.[312]

5.139 The CCBS Act says nothing about writing down shares. In contrast, in company law, when shares are written down, that is a reduction in share capital.[313] As noted earlier, that requires at least a solvency statement by directors, and a special resolution passed by the company. Some stakeholders have suggested that the CCBS Act should also have rules to govern the writing down of shares.

5.140 We see no reason why writing down shares should be unregulated in society law. We think that similar rules to those found in company law should apply to societies. As for the special resolution threshold, we think that writing down shares should require the approval of at least 75% of voters at a general meeting, in line with company law.[314]

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311 Sharenergy Model Rules, r 17.2; Co-operatives UK Co-operative Consortium Model Rules, r 48.

312 FCA Guide, paras 6.1.3 and 6.1.35. And see PECOL, p 75.

313 Companies Act 2006, s 641(4).

314 The definition of a special resolution can be found in the Companies Act 2006, s 283. A similar threshold can be found in the CCBS Act, s 44.

Consultation Question 24.

5.141 We provisionally propose that, when a society seeks to write down its shares, that should require a solvency statement by officers of the society, and a special resolution. Do you agree?

5.142 We provisionally propose that the special resolution should require the approval of at least 75% of voters at a general meeting. Do you agree?

REWARD FOR INVESTORS: CO-OPERATIVES

5.143 To what extent might societies reward investors or lenders? For example, profitable companies generally distribute their profits to shareholders. To what extent is a similar approach compatible with (our proposed definitions of) co-operatives and community benefit societies? Should there be limits on any interest paid by societies on investments, deposits or loans? Such issues are often discussed in the literature, and occasionally flagged by stakeholders as worthy of consideration. We think that they need to be addressed.

5.144 In this section we discuss co-operatives. In the next section we discuss community benefit societies.

Section 2(3) of the CCBS Act

5.145 Section 2(3) of the CCBS Act provides that:

> …"co-operative society" does not include a society that carries on, or intends to carry on, business with the object of making profits mainly for the payment of interest, dividends or bonuses on money invested or deposited with, or lent to, the society or any other person.

5.146 As discussed in Chapter 2, the origin of section 2(3) is the Prevention of Fraud (Investments) Act 1939. That Act was enacted in response to an inquiry into "share-pushing".[315] Fraudster were selling shares in companies to the public. The fraudsters took the money without transferring the shares, or they were selling shares in worthless companies created simply as a vehicle for fraud. This was causing millions of pounds of loss annually.[316]

5.147 The 1939 Act required all traders in shares to be licensed,[317] except that this did not apply to industrial and provident societies.[318] To avoid societies becoming a vehicle for fraud, new societies had to meet a new test for registration, and existing societies which did not meet the test could have their registration cancelled.

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315 Hansard, House of Lords Debate, 28 February 1939, Prevention of Fraud (Investments) Bill.

316 *Share-Pushing*, Report of the Departmental Committee appointed by the Board of Trade (1937) Cmd 5539.

317 Prevention of Fraud (Investments) Act 1939, s 1.

318 Prevention of Fraud (Investments) Act 1939, s 2(1)(b).

5.148 To be registered, as part of the new test a society (other than a community benefit society) had to be a "bona fide co-operative".[319] This did not include carrying on business with the object of making profits mainly for the payment of interest on money invested with the society.[320] That same proviso is replicated in section 2(3) of the CCBS Act.

5.149 The Registry of Friendly Societies (the then registrar) gave the following further guidance at the time as regards the conditions for registration:

> Interest payable on share and loan capital will under [a society's] rules not exceed a rate necessary to obtain and retain the capital required to carry out the objects of the society…

Criticisms of section 2(3)

5.150 There are three principal criticisms of section 2(3) of the CCBS Act.

5.151 First, the problem in 1939 was share-pushing. Within company law, that was addressed directly, by requiring share traders to be licensed. It was not addressed directly in society law. Instead it was addressed obliquely with a partial definition of what a co-operative is not. That partial definition arose through a debate about share-pushing, not a debate to settle the true nature of a co-operative. Indeed, in an internal note, the Registry of Friendly Societies said at the time:

> This phrase [bona fide co-operative] was used as a last resort because it had not been found possible to arrive at a satisfactory definition.

5.152 On the other hand, the authors of the *Principles of European Cooperative Law* (PECOL) repeat the definition, saying that a co-operative carries on business without profit as the ultimate purpose, that is, without making profits mainly for the payment of returns on investments, deposits or loans.[321] This might suggest that the 1939 Act hit upon a workable definition after all. However, in Chapter 3, we have proposed a positive definition of what a co-operative is. In large measure, that might remove the need for a partial negative definition of what a co-operative is not.

5.153 Second, there is a risk that section 2(3) creates uncertainty. A co-operative can pay returns on investments, deposits and loans – but this cannot be its "main purpose".[322] According to the FCA, whether it is the main purpose is judged not solely by looking at the rules of the society and its stated objects, but also by reviewing its trading patterns or accounts,[323] and generally considering "all the information available".[324] This might be burdensome for the FCA, and potentially unpredictable for societies.

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319 Prevention of Fraud (Investments) Act 1939, s 10(1)(a).

320 Prevention of Fraud (Investments) Act 1939, s 10(9).

321 PECOL, r 1.1.

322 FCA Guide, para 4.2.1.

323 FCA Guide, para 4.2.4.

324 FCA Guide, para 4.2.3.

5.154 We have suggested in Chapter 3 that the main purpose of a co-operative should be to benefit its members through transactions with its members. This would preclude the main purpose being to make profits to pay returns on investments, loans and deposits. Yet the main purpose *of profit* might still be to service loans. For example, a consumer co-operative's main purpose might be to benefit members by selling to them at the cheapest possible price. However, it might need to make a trading profit simply to service its debts. The purpose of the co-operative is one thing (benefitting members), and the purpose of a trading profit is another (servicing debts). Section 2(3) blurs this distinction.

5.155 Third, if a concern is to ensure that there are limits on what interest a co-operative might pay on investments, deposits or loans, section 2(3) does not address that directly either. Section 2(3) allows any rate of return, potentially however unreasonable, just as long as this is not the main purpose of the co-operative's profits.

5.156 None of these criticisms is conclusive. Section 2(3) does serve a function. But that function might be better served by a positive definition of what a co-operative is and by addressing interest rates on shares directly.

Concerns about profit-seeking

5.157 Within the co-operative movement there is a concern about profit-seeking. For example, the FCA Guide says:[325]

> …it would be an indicator that a society is a bona-fide co-operative where the distribution of surplus to members is in the form of a dividend based on a member's participation in the co-operative, rather than through payment of interest on shares.

5.158 Similarly, the FCA Guide says that a co-operative should not be "an association of capital with the main purpose of generating financial returns".[326]

5.159 This accords with the Third Co-operative Principle, which says that "members usually receive limited compensation, if any, on capital subscribed as a condition of membership". The International Cooperative Alliance (ICA) explains how the current version of the Third Co-operative Principle derives from an earlier version which said that "share capital should receive only a strictly limited rate of interest, if any".[327]

5.160 More generally, the ICA sounds the following warnings about profit-seeking investors. It says that labour has dignity and precedence over capital.[328] Capital should be used in service of people and labour, rather than people being in servitude to capital.[329] It warns against co-operatives becoming financially dependent on investors to the extent that democratic control by members is undermined.[330] It says that, if there is a return

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325 FCA Guide, para 6.1.23.

326 FCA Guide, para 4.2.4.

327 ICA Guidance Notes, p 29. See too: ICA, *The Capital Conundrum for Co-operatives* (2017) p 15.

328 ICA, *The Capital Conundrum for Co-operatives* (2017) p 16.

329 ICA Guidance Notes, p 30.

330 ICA Guidance Notes, pp 39 to 40; Filene Research Institute, *Survey of Co-operative Capital* (2015) pp 36 to 37.

on capital beyond a market rate, that might attract speculative investment, and the requirement to generate that return might reduce an operating surplus and the ability of the society to develop its business.[331] This in turn might make the co-operative more dependent on external investors, which it would need to attract with a good rate of return, in a vicious circle.[332]

5.161 In other words, if investor shares attract higher rates of interest, that incentivises shareholding, and builds pressure to ensure that higher rates of interest continue. The focus of the business becomes generating interest on shares, rather than generating better transactions with members.

5.162 For example, it might be more profitable for a consumer co-operative to trade with members at higher prices, or not trade with members at all (but trade instead with wealthier customers). Higher profits would allow the business to pay a higher rate of interest on its shares.

5.163 In our view, the concern is not just loss of member control over decision-making, but a risk that member transactions become less beneficial. We think that the principal goal of co-operatives is the provision of beneficial transactions with members. This is the purpose which brings co-operatives into existence. Member control might be an end in itself, but it is also a mechanism to ensure that the focus of the society remains on the needs of the members.

5.164 For example, the Rochdale Pioneers pooled their funds so that the society could buy food at bulk prices, and sell that food at those reduced prices to the members. The purpose was to ensure that members could buy food affordably. The Rochdale Pioneers did not pool their funds to buy food at bulk prices so as to sell that food as profitably as possible and then to pay a high rate of interest to members on their financial contribution to the pool.

5.165 A further concern expressed by stakeholders is as follows. If a co-operative is successful, speculators might become investor members simply to obtain a claim on the assets of the co-operative. For example, if a co-operative is dissolved, its assets might be distributed among current members. There is thus a concern to prevent "asset stripping" by investors.

Benefits of attracting investment

5.166 The previous section was headed "concerns about profit-seeking", but there is of course another side of the argument. An attractive rate of return could lead to investment in the co-operative, and with better funding the co-operative can then grow its business, providing a better service to more members. If there are concerns about profit-seeking, there are already tools which co-operatives can use to address that, as we see in the next section.

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331 ICA Guidance Notes, p 35.

332 ICA, *The Capital Conundrum for Co-operatives* (2017) p 57.

Tools to address profit-seeking

5.167 If a co-operative wishes to moderate profit-seeking, it has some tools at its disposal already. For a start, society rules can set a limit to any interest paid on shares. For example, some model rules specify a maximum rate of whichever is higher of 5%, or 3% above base rate.[333] Those rules could be entrenched (see our proposals on entrenchment of rules in Chapter 6).

5.168 Further, society rules on demutualisation might be entrenched, or a co-operative might engage an asset lock. Society rules might provide for its assets on dissolution to go to another co-operative rather than be distributed to members.

5.169 The FCA Guide says that non-user investor members might have restricted voting rights, so that non-user investor members cannot vote on certain topics (like conversion to a company).[334] However, this approach might be problematic, as follows.

5.170 The Second Co-operative Principle is democratic member control. It says that, in primary co-operatives, members have equal voting rights. In Chapter 3, we have proposed that co-operatives should have one vote per member. In our view, it is incompatible with that rule to give some members reduced voting rights, and that includes preventing investor members from voting on issues like demutualisation. After all, if voting rights can be excluded from some people for some reasons, it could mean, in theory, that voting is excluded from most people for most reasons – only a select few members might control voting on all major decisions.

5.171 Allowing investors to vote on demutualisation should not necessarily be a cause for alarm. A rule of one vote per member regardless of the size of a shareholding means that, where user members outnumber non-user investors, then the latter could not themselves muster the majority needed to pass votes. Techniques like entrenchment provide yet further protection.

5.172 Of course, if stakeholders reject the idea of one vote per member from the definition of a co-operative, then investor members might be excluded from voting on certain issues after all. Otherwise, if a co-operative wants funds without votes, those funds can be raised from non-members, like lenders, or investors in debt instruments (see further below).

5.173 To be clear, a rule of one vote per member does not preclude there being different classes of membership. For example, some shares might be withdrawable, others might attract a higher rate of interest. This is compatible with allowing all members to vote on any resolution.

A limit on interest rates?

5.174 Despite section 2(3) of the CCBS Act, there is no doubt that interest can be paid on investments, deposits and loans. For a start, the CCBS Act explicitly allows societies

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333 For example, Co-operatives UK Multi-Stakeholder Co-operative Model Rules, Community Benefit Society Model Rules.

334 FCA Guide, paras 6.1.30 and 6.1.31.

to take out loans,[335] which might thereby attract commercial rates of interest. There is widespread practice of societies paying interest on shares (see below).

5.175 If there is to be a limit on interest rates, what might that limit be?

5.176 The ICA says that a "market return" can be paid on capital invested by members other than as a condition of membership.[336] PECOL says that interest can be paid on shares, but the rate of interest cannot be higher than a reasonable rate, necessary to obtain and retain enough capital to run the business.[337] The FCA Guide says that any interest must be at the "lowest rate sufficient to obtain the necessary funds".[338]

5.177 A survey by the Community Shares Unit of 192 societies recorded that 14% paid no interest, 10% aspired to pay interest in excess of 7.5%, and some societies aspired to pay interest in excess of 10%.[339] As noted above, some model rules specify a maximum rate of whichever is higher of 5%, or 3% above base rate.[340]

5.178 In comparison, community interest companies are limited to paying an aggregate cap of 35% of their profits by way of total share dividends.[341] The interest rate on performance-related loans is capped at 20%.[342]

5.179 One stakeholder has suggested that the maximum rate of return for an investor share should be limited by reference to the rate of return on non-investor shares. They suggested that investor shares should be no more than 2% higher. In other words, co-operatives should be able to offer a specific investor class of share with a higher (but capped) rate of return, to attract investment.

5.180 In our view, the lowest rate to obtain necessary funds could be very high, for example if there is no other form of funding available. In turn, the non-availability of, say, a commercial loan, might indicate a higher level of risk in the business. Ordinarily, the greater the risk of an investment, the greater the potential reward is needed in order to attract investment which seeks profit. But the greater the reward to the investor, potentially the greater the risk to the autonomy of the co-operative.

5.181 Thus, a better approach might be to say that the rate of interest should be no more than is needed to obtain necessary funding, and even then the rate of interest should be reasonable. This would be a double limitation.

5.182 What would be a reasonable rate of return? What the actual figure might be will fluctuate in different economic conditions. The Community Shares Handbook

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335 CCBS Act, s 14(8).

336 ICA Guidance Notes, pp 30, 32.

337 PECOL, r 3.3(5).

338 FCA Guide, paras 6.1.24 and 6.1.25.

339 Community Shares Handbook, para 6.1.

340 For example, Co-operatives UK Multi-Stakeholder Co-operative Model Rules, Community Benefit Society Model Rules.

341 The Community Interest Company Regulations 2005 (SI 2005 No 1788), rr 19 and 22.

342 https://www.gov.uk/government/publications/community-interest-companies-how-to-form-a-cic

suggests comparison with commercial rates of borrowing.[343] For example, the Bank of England publishes statistics on average rates of interest for commercial loans.[344]

5.183 A reasonable rate of return might also fluctuate according to the class of share. For example, a member might hold a share as a token of their membership, and hope to benefit through transactions with the society. An investor might invest a much larger sum in order to earn interest on their shares without otherwise benefitting from any transactions with the society. A society might need to offer those differential rates of interest in order to attract investment.

Other restrictions on rewarding investors

5.184 In this section, we consider whether there might be other restrictions, beyond an interest rate cap, on how co-operatives might reward investors.

5.185 The FCA Guide lists the following additional conditions for paying interest on society shares.[345]

(1) The rate of interest is declared in advance.

(2) It is not increased if the society is more profitable than expected.

(3) If the society cannot afford to pay the interest which it had previously declared, then the society can decide to pay less interest or no interest at all. No catch-up payments are made in subsequent years.[346]

5.186 These conditions are not mandated by the CCBS Act. At best, they represent the views of the FCA as to what behaviour signals a "bona fide" co-operative. Beyond that, they may be financially sensible, but have no legal force.

5.187 In comparison, in company law, the only restriction on a company making a distribution (like a dividend payment to shareholders) is that the distribution is paid from net profits.[347]

5.188 We make the following comments on the FCA Guide. Paragraphs (1) and (2) above are concerned to detach a society's profitability from its interest payments. If a co-operative should not make profits mainly to pay interest on shares, that can be ensured if profits and interest are entirely separate. Thus, interest rates might be declared in advance, before knowing of the coming year's profitability, and they are not then increased in-year if the co-operative turns out to be (more) profitable.

5.189 Of course, section 2(3) of the CCBS Act does not require profits and interest to be *entirely* separate. At any rate, if a co-operative is profitable in year 1, it might increase the rate of interest on shares for year 2. It would still be declaring the rate in advance,

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343 Community Shares Handbook, para 6.1.

344 https://www.bankofengland.co.uk/statistics/visual-summaries/effective-interest-rates

345 FCA Guide, paras 6.1.24 and 6.1.25.

346 This is also the practice of building society core capital deferred shares – see below.

347 Companies Act 2006, s 830.

but next year's rate may well be influenced by this year's success. Further, if the rate in year 1 is low, it might be necessary to increase the rate in year 2 to retain funds. Which is to say that a perfect separation between interest rates and trading profitability is not realistic.

5.190 Further, we question why there should never be a connection between a co-operative's profitability and the returns it pays on shares. For example, the ICA records some instances of foreign co-operatives paying interest rates based on profitability.[348] We would be hesitant to preclude it in all circumstances. At any rate, we question what that exclusion would achieve if it were in addition to a requirement that any interest rate be only a reasonable return (as discussed in the previous section).

5.191 As for paragraph (3) above, making payment of interest on shares discretionary would align with the idea that paying for withdrawable shares should be discretionary. The reasons for the latter were, in summary, sound financial practice to the benefit of creditors and members. Those reasons apply equally here: interest might not be paid on shares if that jeopardises creditors or members. A requirement to withhold payments of interest which risk being unaffordable would also be consistent with societies subordinating capital to transactions with members. It also aligns with the requirement in company law that dividends be paid out of (disposable) profit.

5.192 The limit in paragraph (3) can only apply to returns paid on investments and deposits, where it is otherwise for the co-operative to offer the rate of return. It could not apply, for example, to commercial loans (unless the commercial loan itself included that term, which is most unlikely). If a co-operative takes out a commercial loan, it would have to repay it according to the terms of the contract. A co-operative should not be able to contract with third parties and unilaterally vary the terms of the contract according to its financial situation from time to time.

5.193 In other words, the CCBS Act should not empower a co-operative to override the terms of a commercial contract – but it can impose restrictions on what terms the co-operative itself offers as regards returns on investments and deposits.

5.194 However, a cap on permissible interest rates would also preclude a co-operative from taking out a commercial loan on terms which required, for example, an interest rate which was unreasonable, or more than that necessary to obtain funding from another source. Investors should not be able to circumvent the rule by structuring their investment as a loan.

Capital gains

5.195 The FCA Guide says that:

> …a market in society shares allowing capital gains for members is normally inconsistent with registration as a society. This is because it may encourage the society's members and officials to operate the business to achieve capital gains

[348] ICA, The Capital Conundrum for Co-operatives (2017).

rather than to serve either the members or the community through operating its business.[349]

5.196 We question whether there should be a prohibition of capital gains when society shares are transferred. We are aware of at least one example of a foreign co-operative where members are able to make capital gains on their shares.[350] Similarly, in some housing co-ownership or mutual ownership schemes, members who leave may receive a payment to reflect an increase in the value of the property.[351]

5.197 At any rate, shares will increase in value only if they are attractive, and that is usually a function primarily of whether they are a safe investment, and what rate of interest they offer. We have suggested a limit on any rate of interest, and that might act to calm share values. Further, the directors of a society can refuse any transfer, and that too might be used to prevent any worrying pursuit of capital gain. Indeed, the rules of a society might prescribe refusal to transfers at other than original value. Sufficient protection may therefore exist already against any worrying search for capital gains.

Discussion

5.198 Section 2(3) of the CCBS Act provides a partial definition of what a co-operative is not. It says that a co-operative does not make profit mainly to pay returns on investments, deposits or loans. We think that that formulation does not always align with practice: co-operatives can make a profit, and might conceivably seek to make a profit simply to service their investments or debts.

5.199 We think that a co-operative can be defined by what it is, rather than what it is not. We think that a co-operative carries on business mainly for the benefit of its members through transactions with its members (as discussed in Chapter 3). If that positive definition is accepted, there is no need for the negative definition in section 2(3).

5.200 We think that there should be limits to the rewards paid by co-operatives to their investors and lenders. Section 2(3) addresses that obliquely. We think that it would be better to address it directly. At the same time, we acknowledge that rewards to investors may be necessary to attract any investment, so as to enable the co-operative to operate at all.

5.201 The balance to be struck, in our view, is that any interest rate paid by a co-operative on investments or deposits with it, or loans to it, should be no more than is needed to obtain necessary funding, and even then no more than a reasonable rate. This aspect is consistent with the FCA Guide.

5.202 That said, contrary to the FCA Guide, our current view is that any rate of interest need not be declared in advance or separated entirely from the co-operative's profitability. We think that the main focus on transactions with members, and a cap on the rate of interest, sufficiently protects a co-operative's identity. Similarly, we think that co-

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349 FCA Guide, para 6.1.13.

350 With Fonterra, in New Zealand: ICA, *The Capital Conundrum for Co-operatives* (2017), ch 8. Admittedly, this is a specialised context: Fonterra is New Zealand's largest business and is regulated directly by its own legislation.

351 Adderley, ch 3.

operatives already have a useful range of other tools to protect their enterprise from any excess of profit-seeking by investors.

5.203 We do agree with the FCA Guide that a co-operative should only offer returns on investments and deposits subject to the condition that payment can be suspended when the co-operative cannot afford payment. This would align with the similar rule proposed above about a society paying out on withdrawable shares. It also aligns with company law's requirement to pay dividends to shareholders out of net profits. This rule would also underline the precedence of member transactions over returns on capital.

5.204 Additionally, as with withdrawable shares, so too with interest payments, we do not think that paying interest need be all or nothing. It may be that the co-operative can only afford a lesser payment of interest than originally declared. That too should be possible.

5.205 Overall, therefore, we are on balance inclined to propose the repeal of section 2(3), and its replacement with the positive definition of a co-operative (in Chapter 2) and a limit on the interest which a co-operative can pay on investments, deposits or loans.

Consultation Question 25.

5.206 We provisionally propose that there should be the following restrictions on interest rates paid by co-operatives on investments, deposits and loans.

(1) Any interest rate should be no more than is needed to obtain necessary funding.

(2) Any interest rate should be no more than a reasonable rate.

(3) Interest on investments and deposits should be paid only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year.

Do you agree?

5.207 In particular, we think that a co-operative considering interest payments should be able to pay a lesser rate, rather than all or nothing, if that is what it can afford. Do you agree?

REWARD FOR INVESTORS: COMMUNITY BENEFIT SOCIETIES

5.208 Section 2(3) of the CCBS Act only applies to co-operatives, but the FCA Guide makes a similar requirement of community benefit societies.[352]

5.209 A co-operative society exists mainly for the benefit of its members. An investor can be a member. So paying a rate of return to an investor can potentially benefit that

[352] FCA Guide, para 5.1.11.

member. However, we think that there should be limits on rates of return for the reasons set out above: essentially, co-operatives should benefit their members primarily through transactions, rather than through returns on capital.[353]

5.210 The position is much starker with community benefit societies. They cannot benefit their members or investors. They can only benefit the community. Therefore, as a matter of logical necessity, community benefit societies cannot pay a rate of interest higher than that necessary to obtain funding.

5.211 Any rate of interest necessary to obtain funding is a payment made for the benefit of the community (albeit indirectly): it is the cost of purchasing the funds for the community benefit project.[354] Any rate of interest above that is unnecessary, and not the cost of purchasing the funds for the community benefit project. Instead, it represents a "bonus" or private profit for the investor. But a community benefit society cannot privately benefit investors – it can only benefit the community.

5.212 In our view, it would provide clarity for the CCBS Act to state explicitly that, for community benefit societies, any rate of interest on investments, deposits or loans should be no more no more than is needed to obtain necessary funding. We think that this is the law already, flowing as a logical necessity from the nature of a community benefit society. We also think that the rate of interest should be no more than a reasonable rate, to keep the law aligned between co-operatives and community benefit societies.

5.213 Similarly, we think that, as with co-operatives, so too community benefit societies should only offer returns on investments and deposits subject to the condition that payment can be suspended when the society cannot afford payment.

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353 See too: Adderley, ch 1.

354 Returns on investments can be treated as the cost of raising funds, and so as an expense to be deducted from profits before tax: PECOL, p 77; Community Shares Handbook, para 8.2.

Consultation Question 26.

5.214 We provisionally propose that there should be the following restrictions on rates of interest paid by community benefit societies on investments, deposits and loans.

(1) Any interest rate should be no more than is needed to obtain necessary funding.

(2) Any interest rate should be no more than a reasonable rate.

(3) Interest on investments and deposits should be paid only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year.

Do you agree?

5.215 In particular, we think that a community benefit society considering interest payments should be able to pay a lesser rate, rather than all or nothing, if that is what it can afford. Do you agree?

DO SOCIETIES NEED A NEW TYPE OF SHARE?

5.216 Some stakeholders say that there is need for a new type of non-user investor share which is non-withdrawable but transferable. A non-user investor is someone who invests in a society by buying shares, and so becomes a member, but otherwise does not use the services of the society.

5.217 Some stakeholders say that such a new type of share might help to raise permanent capital (which does not have to be repaid, unlike withdrawable shares). They say that a new type of share might help raise large amounts from a few (perhaps institutional) investors, rather than small amounts across lots of members (which can be more like crowd-funding).

5.218 Some stakeholders say that it might be necessary to give non-user investors a better rate of return to reflect the fact that they are investors and not users. (Remember, users also benefit through their transactions with the society.) Examples of better returns, as suggested by stakeholders, include: higher interest rates; profit-related payments; premiums on redemption; the ability to resell shares at a profit.

5.219 Other stakeholders say that they have no difficulty raising large amounts of money under the current regime. They can already pay interest at such a rate as is necessary to obtain funding. At any rate, as we note above, any transferable share will be subject to the financial services regulatory regime.

5.220 According to our terms of reference, in Appendix 1, we are asked to set out options on this topic.

Comparable models?

5.221 Some stakeholders have pointed to some initiatives that they think might stand as precedent for the recognition of a new type of investor share for societies.

5.222 A first comparison is the Mutuals' Deferred Shares Act 2015. It recognises the legitimacy of "deferred shares" issued by a friendly society or a mutual insurer (and not a society registered under the CCBS Act). These are shares that can be transferred but not withdrawn, and which prohibit repayment of the principal except on dissolution after the payment of other creditors.[355] The 2015 Act says that there is to be no more than one vote per member, whether they only hold deferred shares or also hold other shares,[356] and that holders of deferred shares cannot vote on conversion, transfer of engagements, or amalgamation.[357]

5.223 However, when HM Treasury consulted on the regulations needed to give effect to the 2015 Act, respondents said that they had no plans to issue such shares. This is because such shares would not provide the type of capital necessary to meet the regulatory needs of mutual insurers.[358] (Non-financial societies registered under the CCBS Act are not subject to that regulatory regime.)

5.224 A second comparison is the Mutual Capital Instrument (MCI) in Australia. Amending legislation[359] enables a mutual entity to issue share capital. A mutual entity is defined as a company with one vote per member.[360] It can issue an MCI if the mutual entity is a non-charitable public company without voting shares which are publicly listed.[361] The mutual entity must not pay a dividend on the shares unless the dividend is fair and reasonable to all members.[362]

5.225 This innovation does not apply to co-operatives, which have their own separate legislation.[363] The purpose of the innovation was to permit a mutually-run company to issue shares, including in particular where the mutual was a company limited by guarantee. A company limited by guarantee does not otherwise have shares. In contrast, in the United Kingdom, a co-operative is not a company, but it does already have shares.

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355 Mutuals' Deferred Shares Act 2015, s 1(2).

356 Mutuals' Deferred Shares Act 2015, s 2(1).

357 Mutuals' Deferred Shares Act 2015, s 2(2).

358 https://www.gov.uk/government/consultations/mutual-deferred-shares-consultation-on-technical-policy-details

359 Treasury Laws Amendment (Mutual Reforms) Act 2019 (Australia). The explanatory notes to the legislation are here: https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=s1177#:~:text=Implements%20certain%20recommendations%20of%20the,friendly%20societies%20that%20the%20demutualisation

360 Corporations Act 2001 (Australia), s 51M.

361 Corporations Act 2001 (Australia), ss 167AC to 167AF.

362 Corporations Act 2001 (Australia), s 254WA(2).

363 Co-operatives National Law, given effect separately in each State or Territory: for example, the Co-operatives (Adoption of National Law) Act 2012 (NSW).

5.226 A third comparison are the core capital deferred shares successfully issued by Nationwide Building Society (building societies are not registered under the CCBS Act).[364] These shares come with no right of redemption, and no guaranteed right to any "distribution" (payment on the shares). The board of the society has an absolute discretion whether to make any distribution, and if so how much, subject to an upper limit set by the society. There is no accrual, meaning that any distribution missed in one year does not carry forward to the next year. There are no voting rights; limited or no rights of pre-emption; and they rank after the payment of other creditors upon any dissolution (which is what makes them deferred). They are transferable, and they were sold initially at a price significantly above their nominal value.

5.227 In fact, Nationwide has made a distribution every year, at a steady rate of return (around 10% per year). The rate is declared in advance. The rate is said to reflect the profitability of the society, its outlook, liquidity – and the value of the capital to the society. It thereby contains an element of "rewarding investment…in a commercially responsible manner".[365]

5.228 In summary, the 2015 Act applies to mutual insurers, and has not yet been a success. The Australian MCI applies to companies which otherwise lack shares. Nationwide's core capital deferred shares have been successful, but did not appear to require any legislative amendment of building society law.

Other ways of raising funds

5.229 The ICA commissioned a report on how co-operatives around the world raise money.[366] It reveals that there is a wide range of available sources of funding already. Member contributions and retained earnings are a significant source of funds; trade credit is an important manner of financing; and bank loans and sale of debt instruments are very common. Investor shares are less common.

5.230 The report repeats the warning that, with external financing, members might risk losing control of the co-operative. Even when investors have limited voting rights, it says, investors can retain a significant influence, so societies might want to set a limit on their dependency on external financing. The report suggests a limit of 25% of funds being raised from external sources.[367]

5.231 Some stakeholders have suggested other limits, varying from 25% to 50% of shares. They have suggested that this limit on investor shareholding should be part of the definition of a co-operative. In similar vein, European law sets a limit such that non-user investor members can only have 25% of votes.[368] In New Zealand, at least 60%

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364 https://www.nationwide.co.uk/investor-relations/ccds-terms-of-access/ccds-market-data-and-investor-information/

365 See the Distribution Policy.

366 Filene Research Institute, *Survey of Co-operative Capital* (2015).

367 Filene Research Institute, *Survey of Co-operative Capital* (2015) pp 36 to 37.

368 Council Regulation (EC) No 1435/2003 of 22 July 2003 on the Statute for a European Cooperative Society, art 59(3).

of voting rights must be held by transacting shareholders (rather than non-user investors).[369]

5.232 The ICA report also says that co-operatives should make more effort to fund each other. As an example, the report suggests the idea of the co-operative sector creating a fund, for investors to buy into, which consists of a diversified portfolio of co-operative debt instruments.[370]

5.233 The ICA also appointed a Commission to advise on how co-operatives might raise capital while retaining member control.[371] The Commission acknowledged the existence of investor shares, without voting rights, sometimes with payments linked to business performance. Again, the Commission warned about members losing control to external financing sources.[372] It stressed the need for co-operatives to be better at funding each other, given the wealth of co-operative capital generally available. We note, for example, that in the UK there are more than 7000 co-operatives with a total revenue of more than £40bn.[373]

Is there any gap to be filled by a new investor share?

5.234 Societies can already issue shares which are non-withdrawable but transferable. Societies can already issue shares to non-user investors. Societies can already issue shares which come with different rates of return. The FCA Guide already acknowledges the availability of non-user investor shares.[374] All this is also in line with the international practice of foreign co-operatives.[375] In short, non-withdrawable transferable non-user investor shares with varied rates of return are already allowed.

5.235 There appear to be four motives behind the request for a new type of investor share. First, some stakeholders say that there is uncertainty over the availability of non-withdrawable but transferable shares. As noted above, such shares are already allowed (and we have proposed above making this even more explicit in the legislation).

5.236 Second, some stakeholders say that there is uncertainty over whether shares can be issued to non-user investors. As noted above, such non-user investor shares are already allowed. Nevertheless, we ask stakeholders whether expressly identifying in the CCBS Act at least this type of shareholder would improve certainty.

5.237 Third, some stakeholders say that there is uncertainty over what rates of return are available for shares. We have addressed this directly in our proposals above. It is

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369 Co-operatives Companies Act 1996, s 2(1)(a).

370 Filene Research Institute, *Survey of Co-operative Capital* (2015) p 39.

371 ICA, *The Capital Conundrum for Co-operatives* (2017).

372 ICA, *The Capital Conundrum for Co-operatives* (2017) p 57.

373 https://www.uk.coop/understanding-co-ops/what-co-op/quick-facts-about-co-ops

374 FCA Guide, para 6.1.30.

375 PECOL, rr 1.3 and 3.3(5); Filene Research Institute, *Survey of Co-operative Capital* (2015); ICA, *The Capital Conundrum for Co-operatives* (2017).

something that we think needs to be addressed whether or not there should be a new type of share.

5.238 Fourth, some stakeholders say that a new type of share is an opportunity to market societies and attract new types of investor. We think that reform which clarifies the availability of non-withdrawable transferable investor shares and their permissible rate of return is itself sufficient opportunity for marketing.

5.239 For these reasons, it is not clear to us whether any new type of investor share is needed given the flexibility that already exists. We seek the views of stakeholders on what options for a new type of share should be considered, if any.

Consultation Question 27.

5.240 Do you think that societies need a new type of share? If so, what would be its characteristics?

Chapter 6: Society officers

6.1 This chapter considers a range of topics concerning the officers of a society. It addresses the following.

(1) Whether the Co-operative and Community Benefit Societies Act 2014 (CCBS Act) should refer to them as officers, or directors (as with company law), or by some other label.

(2) Whether the Mutuals Public Register should include a list of the current officers of a society.

(3) What information should be required in the list of officers and members.

(4) Whether the CCBS Act should set out a list of duties owed by officers.

(5) Whether the CCBS Act should prescribe the remedies for any breach of duty by society officers.

WHICH LABEL?

6.2 This section considers which label should be used by the CCBS Act, whether officers, or directors (as with company law), or something else. Choosing the best label is the precursor to discussing the substantive issues in the rest of this chapter.

6.3 The CCBS Act refers to a society's "committee (by whatever name)" and its "managers or other officers",[376] and specifically to a "secretary".[377] It defines "committee" as the "management committee or other directing body", and "officer" as including "any treasurer, secretary, member of the committee, manager".[378] It appears to equate company directors with society committee members.[379] The Company Directors Disqualification Act 1986 also equates company directors and officers with society committee members and officers.[380]

6.4 The FCA Guide uses the word "director".[381] The CCBS Handbook titles its chapter "directors and officials",[382] and says that it is the board or committee, which includes

376 For example, CCBS Act, s 14(6).

377 For example, CCBS Act, s 3(1)(a).

378 CCBS Act, s 149.

379 CCBS Act, s 49(5)(a).

380 Company Directors Disqualification Act 1986, ss 22E(3)(b).

381 FCA Guide, paras 8.1.5 to 8.1.11.

382 CCBS Handbook, ch 7.

officers, which owe duties to the society akin to the directors of a company.[383] PECOL refers to "directors or managers".[384]

6.5 Some model rules refer to a "board of directors" and a "director by whatever name called", also "officer" and "secretary". They define an officer as a member of the board appointed to a particular role, while the secretary is separately appointed by the board.[385] Other model rules have a management committee, with separate officers of chair, secretary and treasurer.[386] In some cases, the society is governed by the general meeting, and only a secretary is appointed.[387]

6.6 By comparison, in company law, "director includes any person occupying the position of director, by whatever name called",[388] which is somewhat circular, whereas an officer includes a director, manager or secretary.[389] The Companies Act 2006 requires registers of members,[390] directors,[391] and secretaries,[392] whereas the CCBS Act requires a register of members and officers.[393]

6.7 Overall, the picture is not entirely clear, but that is in part also a reflection of the diversity of practice among societies. We think it best to refer to officers, since that is the language principally used in the CCBS Act. The word "officer" is itself defined expansively as including a treasurer, secretary, committee member or manager – to put the matter beyond doubt, we would propose adding "director" to that list.

Consultation Question 28.

6.8 We provisionally propose that an officer be defined in section 149 of the CCBS Act as including a director. Do you agree?

383 CCBS Handbook, p 139.

384 PECOL, r 2.5.

385 Co-operatives UK Multi-stakeholder Co-operative Model Rules, Co-operative Consortium Model Rules, Worker Co-operative Model Rules, Community Benefit Society Model Rules

386 Co-operatives UK and Confederation of Co-operative Housing Fully Mutual Housing Co-op Model Rules, Tenant Management Housing Co-op Model Rules; Co-operatives UK and Confederation of Co-operative Housing and Wales Co-operative Centre Mutual Home Ownership Society Model Rules

387 Co-operatives UK and Confederation of Co-operative Housing and Wales Co-operative Centre Co-operative (General Meeting Governed) Model Rules

388 Companies Act 2006, s 250.

389 Companies Act 2006, s 1173.

390 Companies Act 2006, s 113.

391 Companies Act 2006, s 162.

392 Companies Act 2006, s 275.

393 CCBS Act, s 30.

LIST OF OFFICERS

6.9 Should the Mutuals Public Register contain the identity of the current officers of a society? Should a society be required to update the Financial Conduct Authority (FCA) when there is a change of officer?

6.10 Some stakeholders support such suggestions. They say that it would be useful for societies, when dealing with third parties, to be able to show who the officers are (that is, those whom third parties can trust to be genuine representatives of the society). They also say that this would generally improve transparency.

6.11 The FCA have said that a list of current officers also assists in exercising the FCA's powers, for example, in relation to director disqualification,[394] or enforcing an asset lock.

6.12 Currently, societies are required to keep their own register of officers.[395] We note that, in practice, officers for the past year are recorded on the annual return AR30, which is published on the Mutuals Public Register. So what is missing is in-year updates of changes as they happen, and perhaps a list of officers directly on the Mutuals Public Register (rather than reading uploaded society returns in order to identify officers).

6.13 In comparison, companies must keep a register of directors,[396] or a private company can elect for that list to be kept on the central register.[397] Either way, companies must update the registrar within 14 days of any changes.[398] Directors are listed on the Companies House register.

6.14 We suggest that current officers of societies should be listed on the Mutuals Public Register, and that societies should be required to notify the FCA of any changes within 14 days, so that the Mutuals Public Register can be updated.

Consultation Question 29.

6.15 We provisionally propose that officers of a society should be listed on the Mutuals Public Register. Do you agree?

394 Company Directors Disqualification Act 1986, s 22E.

395 CCBS Act, s 30.

396 Companies Act 2006, s 162.

397 Companies Act 2006, ss 128A and 167A.

398 Companies Act 2006, ss 167(1) and 167G(6).

Consultation Question 30.

6.16 We provisionally propose that a society should notify the registrar of any changes concerning its officers within 14 days. Do you agree?

REQUIRED INFORMATION

6.17 What information should be included on any register of officers? This is relevant, both to any register kept by a society, and any possible list of officers published on the Mutuals Public Register.

6.18 Currently, a society must keep a register of members and officers.[399] The register must list an officer's name, postal address, and electronic address.[400] The annual return AR30 lists officers' names, and their month and year of birth. The register must also list the name, postal address, and any electronic address for members.[401] The register may be inspected by any person authorised by the FCA.[402] Additionally, a member of the society, and any person having an interest in its funds, may inspect the duplicate register at all reasonable hours.[403] The society itself can also make its own rules allowing for the inspection of its books.[404]

6.19 In comparison, in company law, there are registers of members, secretaries, and directors, as follows.

6.20 The register of members only includes name and address,[405] and that can be a service address rather than a residential address.[406] Further, when a person requests inspection of the register, that person must give their own name and address, and the purpose for which the information is sought.[407] Upon receiving a request for inspection, the company may apply to court, who may direct the company not to disclose any information, on the basis that the request was not for a proper purpose.[408] Regulations may require a company to refrain from revealing an individual's information at all, except in specified circumstances.[409]

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399 CCBS Act, s 30(1).

400 CCBS Act, s 30(3).

401 CCBS Act, s 30(2).

402 CCBS Act, s 30(8).

403 CCBS Act, s 103. The duplicate register omits information about a member's shares or other property in the society: s 30(7).

404 CCBS Act, s 104.

405 Companies Act 2006, s 113(2).

406 Companies Act 2006, s 113A(1)(b).

407 Companies Act 2006, s 116(4).

408 Companies Act 2006, s 117.

409 Companies Act 2006, s 120A.

6.21 The principal concern here was to prevent direct mail companies using the list of shareholder names and addresses for commercial purposes.[410] In theory, that same concern could apply to society members. Note that it was similarly the ability of fraudsters to use the public list of shareholders to target victims with "share pushing" which led to the Prevention of Fraud (Investments) Act 1939 and its amendment to the definition of a co-operative.[411]

6.22 For companies, the register of secretaries must contain their name and address,[412] but again this may be a service address, which may be the company's registered office.[413]

6.23 The register of directors includes name, service address, nationality, country of residence, and date of birth.[414] The service address can be the company's registered office.[415] The company must keep a register of directors' residential addresses,[416] but this is protected information.[417] The company cannot use or disclose it, except with the director's consent, or except for communicating with the director, or fulfilling a statutory duty, or under court order.[418] Similarly, the registrar must omit such protected information from the register,[419] and cannot use it except for communicating with the director, and cannot supply it except to a credit reference agency.[420] However, the registrar may put the residential address on the public record after all if communications are going unanswered or there is evidence that the service address is ineffective; but the registrar must first give notice to the director and hear representations.[421] The court may order disclosure where there is evidence that the service address is not effective, or it is necessary or expedient in connection with the enforcement of another court order or decree.[422]

6.24 The reason for this approach to the residential address of directors in company law was a concern that directors might be targeted by activists, for example if their

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410 House of Commons Trade and Industry Committee, *White Paper on Modernising Company Law* (HC 439) (2003), p 42.

411 *Share-Pushing*, Report of the Departmental Committee appointed by the Board of Trade (1937) Cmd 5539. See further Chapter 3.

412 Companies Act 2006, s 277(1).

413 Companies Act 2006, s 277(5).

414 Companies Act 2006, s 163(1).

415 Companies Act 2006, s 163(5).

416 Companies Act 2006, s 165.

417 Companies Act 2006, s 240.

418 Companies Act 2006, s 241.

419 Companies Act 2006, s 242.

420 Companies Act 2006, s 243.

421 Companies Act 2006, s 245.

422 Companies Act 2006, s 244.

company is involved with animal testing.[423] We think that the same concern might arise with members too.

6.25 More generally, we think that there might be concerns about invasion of privacy, and possibly even identity theft, if a public register includes such details as name and address, nationality, country of residence, and date of birth. This is not the same as data protection. Data protection law requires that confidential data must be protected against disclosure. We are here discussing which data should be publicly available.

6.26 In our view, the scheme in company law is more complicated than required for societies. If only appropriate material is made public in the first place, there is less need for further rules about exceptions or applications to court.

6.27 We think that it is appropriate for a society to make available for inspection a register of members and officers which lists their name and an address by which they can be contacted. That might be an electronic address or a postal address. The postal address need not be their residential address. We do not think it appropriate that an officer must also give their date of birth. We acknowledge the requirement that any officer be 16 or older,[424] but that can merely be confirmed on any register (for example, with a tick box), rather than evidenced with a date of birth.

6.28 Additionally, we think it proper that the FCA be notified of the residential address of officers, to enable the FCA to make contact with the officer, for example to enforce duties under the CCBS Act. The residential address would otherwise be confidential. This means that it would not be made public except as allowed by the law of confidentiality, which includes, for example, when a court order permits disclosure.[425]

6.29 The other details currently required to be kept on the register of members and officers are: what shares are held by a member,[426] and what other society property is held by the member,[427] except that these two pieces of information are kept off the duplicate register;[428] the date when the member joined,[429] and the date when they ceased to be a member;[430] the specific office held by an officer (for example, treasurer or secretary),[431] and the date they took up that office.[432] We have not yet heard of any

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423 *Boyle and Bird's Company Law* (10th ed, 2019) [15.21]; House of Commons Trade and Industry Committee, *White Paper on Modernising Company Law* (HC 439) (2003), p 41.

424 CCBS Act, s 31(3).

425 The exceptions to confidentiality are currently summarised in *Emmott v Michael Wilson & Partners Ltd* [2008] EWCA Civ 184.

426 CCBS Act, s 30(2)(c).

427 CCBS Act, s 30(2)(d).

428 CCBS Act, s 30(7).

429 CCBS Act, s 30(2)(e).

430 CCBS Act, s 30(2)(f).

431 CCBS Act, s 30(3)(c).

432 CCBS Act, s 30(3)(d).

need to alter these details, and there are no privacy concerns here, so we do not currently propose any change in their regard.

Consultation Question 31.

6.30 We provisionally propose that a society's register of members and officers, available for inspection, should include their name and a contact address. Do you agree?

Consultation Question 32.

6.31 We provisionally propose that the contact address for members and officers might be an electronic address. Do you agree?

Consultation Question 33.

6.32 We provisionally propose that any contact address for members and officers which is a postal address need not be the residential address. Do you agree?

Consultation Question 34.

6.33 We provisionally propose that the residential address of an officer should be notified to the FCA. This would be confidential, but the FCA may use it to make contact with the officer. Do you agree?

OFFICER DUTIES

6.34 Should the CCBS Act set out the duties of an officer?

6.35 Some stakeholders say that the CCBS Act should list the same duties for officers as are found in the Companies Act 2006 for company directors. They argue that the duties must already be the same for society officers as for company directors; both are businesses and there is no reason to think that officer duties for societies are different. Some say that only the principal duties need be codified. Some say that containing the duties in the CCBS Act might improve professionalism among society officers. In contrast, some stakeholders say that the duties of officers are well understood already and do not need inclusion in legislation.

6.36 Some model rules merely provide that the board of directors will prepare and enforce a code of conduct for directors.[433] This is potentially a case of officers setting their own standards. Other model rules provide that the committee will abide by a code of conduct set by the society.[434] Co-operatives UK has also produced a Corporate Governance Code,[435] which includes as an appendix a code of conduct for directors.

6.37 Under the CCBS Act, officers' duties are sparse. Members of a society's committee must observe any limitations on their powers flowing from the society's rules.[436] Any action by the members of the committee which would be beyond the society's capacity may be ratified by the society,[437] but this does not affect any liability incurred by a member of the committee.[438] Further, a transaction is voidable by the society when entered into by the committee in excess of its powers with a member of the committee or with a person connected with a member of the committee.[439] The misappropriation of society property is prohibited.[440]

6.38 In comparison, the general duties of company directors extend to several pages of detail. We set out in Appendix 5 the relevant provisions of the Companies Act 2006.[441] We think that they can be abbreviated as follows, using the same language as the Companies Act 2006 but made applicable to societies.

(1) The duties are owed by an officer of a society to the society.

(2) An officer of a society must act in accordance with the society's rules, and only exercise powers for the purposes for which those powers are conferred.

(3) An officer of a society must act in the way they consider, in good faith, would be most likely to achieve the purposes of the society. In the case of a co-operative, this would include promoting the success of the society for the benefit of its members as a whole.

(4) An officer of a society must exercise independent judgement.

(5) An officer of a society must exercise reasonable care, skill and diligence.

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433 Co-operatives UK Multi-stakeholder Co-operative Model Rules, Co-operative Consortium Model Rules, Worker Co-operative Model Rules, Community Benefit Society Model Rules.

434 Co-operatives UK and Confederation of Co-operative Housing Fully Mutual Housing Co-op Model Rules, Tenant Management Housing Co-op Model Rules; Co-operatives UK and Confederation of Co-operative Housing and Wales Co-operative Centre Mutual Home Ownership Society Model Rules.

435 https://www.uk.coop/code

436 CCBS Act, s 43(4).

437 CCBS Act, s 43(5).

438 CCBS Act, s 43(6).

439 CCBS Act, s 48.

440 CCBS Act, s 130.

441 Companies Act 2006, Pt 10 ch 2.

(6) An officer of a society must avoid situations in which they have a direct or indirect interest that may possibly conflict with the interests of the society.

(7) An officer of a society must not accept a benefit from a third party conferred by reason of their being an officer or their doing (or not doing) anything as an officer.[442]

(8) If an officer of a society is in any way interested in a proposed transaction with the society, they must declare the nature and extent of that interest.

6.39 In our view, there are three main options as regards the duties of an officer: say nothing in the CCBS Act; use language which is different from the Companies Act 2006; adopt those in the Companies Act 2006. We consider each option in turn.

Option 1 – no statement

6.40 The first option is not to have any statement of officers' duties in the CCBS Act. In our view, this is the least attractive option. The inclusion of directors' duties in the Companies Act 2006 followed recommendations to that effect from the Law Commission,[443] and from the Company Law Review Steering Group,[444] principally so as to set clear standards. Society officers should similarly be subject to clear standards of behaviour. Put bluntly, if the persistent view was that company directors should have their duties set out in statute, we cannot see any reason why society officers should be treated differently.

Option 2 – different language

6.41 The second option is a list of duties set out in the CCBS Act, which might add to or depart from the list found in the Companies Act 2006, or it might use different language.

6.42 For example, the CCBS Handbook lists the following further duties:[445]

(1) A duty to obey the law.

(2) A duty to act fairly between different classes of membership.

(3) A duty of confidentiality.

(4) A duty not to misapply society assets.

6.43 Alternatively, the FCA Guide uses the following language:[446]

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442 Similarly, a partner must account for private profits from any transaction with the partnership without the consent of other the partners, and must pay over profits if they compete with the firm: Partnership Act 1890, ss 29 and 30.

443 Law Com No 261, *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties* (1999), ch 4.

444 *Boyle and Bird's Company Law* (10th ed, 2019) [16.1].

445 See CCBS Handbook, p 146.

446 FCA Guide, paras 8.1.5 to 8.1.9.

(1) Directors must not use society assets for their own benefit.

(2) Directors must act in the best interests of the society.

(3) Directors must deal with conflicts of interest according to the law and the society's rules.

(4) Directors should act prudently, lawfully and comply with the society's rules.

(5) Directors should use their powers only for the purpose they were given.

(6) Directors have a duty to bring to the role of director the skills that they have and the skills reasonably required to perform the role.

6.44 As a further alternative, to the extent that an officer of a society holds a fiduciary position (that is, a position of trust), then fiduciary duties might be articulated as follows.[447] (These are in addition to any other non-fiduciary duties an officer might owe in tort, contract or equity.)[448]

(1) A fiduciary must act in good faith.

(2) They must not make a profit out of their office.

(3) They must not place themselves in a position where their duty and their interest may conflict.

(4) They may not act for their own benefit or the benefit of a third person without the informed consent of their principal (which in this case would be the society).

6.45 Similarly, the authors of the *Principles of European Cooperative Law* (PECOL) refer to "duties of honesty, loyalty, good faith, care and skill".[449]

6.46 Overall, if there is to be legislation, we think it best to keep faith with the list and language of the Companies Act 2006. It seems to us that the alternative approaches set out above are largely the same in principle – and the diversity of language may simply be a consequence of the absence of a list of duties in the CCBS Act. In which case, it is better to borrow language from the Companies Act 2006 which is tried and tested in the specific setting of directors' duties.

6.47 Also, any statutory list need not be taken as exhaustive. Resort could be had, if necessary, to other duties variously articulated in the case law. For example, authors say that the Companies Act 2006 is only a partial codification of the underlying case

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447 *Snell's Equity* (34th ed, 2022) [7-008], citing *Bristol & West Building Society v Mothew* [1998] Ch 1, 18 (Millett LJ).

448 *Snell's Equity* (34th ed, 2022) [7-009].

449 PECOL, r 2.5(8).

law – detailed, but still not exhaustive.[450] This view is also expressed in the Explanatory Notes to the Companies Act 2006.[451]

Option 3 – apply the Companies Act 2006

6.48 The third option is that the CCBS Act might apply the full provisions of the Companies Act 2006. This is the option we prefer. If society officers owe the same duties as company officers, then the same language should be used. Different language might lead to confusion and inconsistency. The language in the Companies Act 2006 is tried and tested, and further developed in the case law.

Consultation Question 35.

6.49 We provisionally propose that duties owed by officers to their society should be addressed by the CCBS Act. Do you agree?

Consultation Question 36.

6.50 We provisionally propose that the CCBS Act should adopt the director duties set out in the Companies Act 2006. Do you agree?

REMEDIES FOR BREACH OF DUTY

6.51 Should the CCBS Act prescribe the remedies for any breach of duty by a society officer?

6.52 To begin with, we note that director disqualification law already applies equally to officers of societies as it applies to directors of companies.[452] Disqualification could be appropriate, for example, where an officer regularly fails to comply with their duties under the CCBS Act.[453]

6.53 Further, where an officer by their misbehaviour commits a crime under the CCBS Act, proceedings can be brought by the society, or the FCA, or any person aggrieved.[454] Further still, if a member has personal rights which are transgressed by an officer acting in breach of duty, then the member can sue the officer.[455]

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450 *Boyle and Bird's Company Law* (10th ed, 2019) [16.4].

451 Explanatory Notes, Companies Act 2006, para 306.

452 Company Directors Disqualification Act 1986, s 22E.

453 Company Directors Disqualification Act 1986, s 22E(4)(b).

454 CCBS Act, s 132.

455 See too: CCBS Handbook, p 159; *Boyle and Bird's Company Law* (10th ed, 2019) [18.3].

6.54 Otherwise, the officer duties discussed in the previous section are owed by the officer to the society. The society itself could sue the officer for breach of duty.

6.55 In company law, such a claim (by the company against the director) was problematic.[456] For example, there was no point in one person agitating to sue a director for behaviour which the majority of shareholders could ratify.[457] A difficulty arose in particular where the impugned director was themselves the majority shareholder.

6.56 To address this difficulty, the Companies Act 2006 introduced a statutory "derivative claim".[458] This is where a minority shareholder can bring a claim, in the name of the company, against a director for breach of duty owed to the company. The permission of the court is needed to continue the claim.[459] The court has a wide discretion and, in broad terms, asks whether the claim is worthwhile (for example, in terms of its impact on company operations).[460]

6.57 We question whether any statutory derivative claim is needed in society law. For example, if a society operates on the basis of one vote per member, there is no majority shareholder to overcome. Instead, a meeting of members could be called to discuss or approve action by the society against an officer. No stakeholder has yet asked for a statutory derivate claim instead. We do not currently propose any reform here.

6.58 Otherwise, the duties owed by officers, even if they are to be codified in statute, are based on common law and equitable duties and remedies developed in the case law. The Companies Act 2006 says that the remedies for breach of director duties are those provided by the case law.[461] The 2006 Act itself does not set out a list of remedies. We propose that the same approach should be taken for the duties of officers of societies. In other words, the CCBS Act would not attempt to list definitively what remedies are available, instead leaving that question to the case law (as with company law). This also allows the law to develop over time, if necessary, rather than fixing it in the statute.

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456 *Boyle and Bird's Company Law* (10th ed, 2019) [18.2] to [18.6]; CCBS Handbook, pp 158 to 159.

457 *Foss v Harbottle* (1843) 2 Hare 461.

458 Companies Act 2006, s 260.

459 Companies Act 2006, s 261.

460 Companies Act 2006, ss 263 and 172.

461 Companies Act 2006, s 178.

Consultation Question 37.

6.59 We provisionally propose that the CCBS Act should follow company law and state that the consequences of a breach of duty by an officer would be those provided by common law or equity. Do you agree?

6.60 We do not propose the creation of any statutory derivative claim, such that a member can sue an officer in the name of the society. Do you agree?

Chapter 7: Further proposed reforms

7.1 Stakeholders have suggested a long list of issues for possible reform. This is not surprising, given the long passage of time since society law was last reviewed. We have grouped together in this chapter all those further suggestions where we propose reform.

APPEALING DECISIONS OF THE REGISTRAR

Right to appeal

7.2 Some stakeholders have suggested that it should be possible to appeal decisions of the registrar about registration.

7.3 We agree that it should be possible to appeal decisions fundamental to a society's ability to exist at all. We propose that a society should be able to appeal against the following decisions: not to register an applicant society; not to register a change in the rules of a society; and to cancel the registration of a society. In comparison, for example, it is possible to appeal those decisions by the Charity Commission.[462]

7.4 Currently, under the Co-operative and Community Benefit Societies Act 2014 (CCBS Act), there is already a right to appeal a decision not to register a change of rules.[463] Further, there is a right to appeal decisions not to register an applicant society, and to cancel a society,[464] except as follows.

(1) There is no right to appeal when the decision is because the registrar is not satisfied that the society is a bona fide co-operative, or that the business of the society is conducted for the benefit of the community.[465]

(2) There is no right to appeal against a cancellation which was made:[466]

(a) at the society's request;[467] or

(b) after a certificate has been lodged with the registrar confirming that all society property has been conveyed:[468]

(i) following a transfer of engagements to another society;[469]

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462 https://www.gov.uk/guidance/appeal-against-a-charity-commission-decision-about-your-charity.

463 CCBS Act, s 17.

464 CCBS Act, s 9.

465 CCBS Act, s 9(3).

466 CCBS Act, s 9(4).

467 See CCBS Act, s 5(2).

468 See CCBS Act, s 126.

469 See CCBS Act, s 110.

(ii) following conversion to, amalgamation with, or transfer of engagements to a company;[470] or

(iii) when a society is dissolved by an instrument of dissolution,[471] or on its being wound up.[472]

7.5 Thus, there is no right to appeal the decision of the registrar who is not satisfied that the society is a bona fide co-operative or conducting its business for the benefit of the community, and declines to register the society on this basis. It seems to us that reform might be warranted here.

7.6 So the question now becomes: should there be a right to appeal the registrar's decision about whether a society meets the definition of a co-operative or community benefit society? Without a definition, it becomes much harder to determine whether the registrar's decision is wrong on whether, for example, a co-operative is bona fide.

7.7 Some stakeholders support the idea of a right to appeal here. Some say that it would be useful to develop a body of guiding case law on what constitutes a co-operative or community benefit society.

7.8 In Chapters 3 and 4, we proposed new definitions for co-operatives and for community benefit societies. If these new definitions are adopted, it will reduce the scope for subjective judgements by the registrar about whether a society is truly a co-operative or community benefit society.

7.9 Nevertheless, we think that a decision by the registrar about whether a society satisfies the definition of a co-operative or community benefit society is so fundamental – it determines a society's ability to access this legal form at all – that there should be a right to appeal the registrar's decision, whatever the definition of a co-operative or community benefit society.

Consultation Question 38.

7.10 We provisionally propose that there should be a right to appeal decisions by the registrar on whether a society meets the definition of a co-operative or community benefit society. Do you agree?

[470] See CCBS Act, s 112.

[471] See CCBS Act, s 119.

[472] See CCBS Act, s 123.

Where to appeal

7.11 The CCBS Act currently provides for appeal to the High Court in England and Wales, or the Court of Session in Scotland. Similarly, for example, appeals from the Regulator of Social Housing also go to court.[473]

7.12 Some stakeholders have suggested that an appeal should instead go before a tribunal. For example, an appeal against a decision by the Charity Commission in England and Wales is heard by a tribunal in the General Regulatory Chamber.[474] An appeal against a decision by the Office of the Scottish Charity Regulator (OSCR) is heard by the General Regulatory Chamber of the First-tier Tribunal for Scotland.[475] A tribunal might be able to provide shorter lead times to a hearing, lower fees,[476] and reduced exposure to paying the other side's legal costs if an applicant loses.[477] A tribunal might also develop more personal expertise because it is staffed by fewer judges.

Consultation Question 39.

7.13 Do you think that an appeal against a decision by the registrar should be heard by the court (as is currently the case) or by a tribunal?

SUSPENSION

7.14 Should the power to suspend a society's registration be repealed?

7.15 Currently, under the CCBS Act, the Financial Conduct Authority (FCA) as registrar may suspend a society's registration,[478] for example where a society has wilfully violated provisions of the CCBS Act. Initial suspension is for a period not exceeding three months.[479] There is no right to appeal a decision to suspend, but there is a right to appeal a decision to renew a suspension beyond three months.[480]

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473 Housing and Regeneration Act 2008, s 121. That section does also say that the Secretary of State may by order provide for the First-tier Tribunal to have jurisdiction instead of the High Court.

474 https://www.gov.uk/guidance/appeal-against-a-charity-commission-decision-about-your-charity.

475 https://www.oscr.org.uk/media/1531/review-procedures.pdf.

476 https://www.gov.uk/court-fees-what-they-are.

477 The Tribunal Procedure (First-tier Tribunal) (General Regulatory Chamber) Rules 2009 (SI 2009 No 1976), para 10.

478 CCBS Act, s 8(1).

479 CCBS Act, s 8(1)(a).

480 CCBS Act, s 9(1).

7.16 During suspension, a society is not entitled to any of the privileges of the CCBS Act.[481] Importantly, this means that a society would no longer be a body corporate with limited liability.[482]

7.17 The problem with suspension is the legal uncertainty which it creates. It is unclear what happens to a society when it is suspended.[483] In our view, a society probably becomes a general partnership, or possibly an unincorporated association. This view is shared by the FCA Guide.[484]

7.18 An unincorporated association is when two or more people join together for a common purpose, not a business purpose, by mutual undertakings, in an organisation which has rules.[485] It is not a corporate body, and it does not have limited liability. In dealing with third parties, a member of an unincorporated association might incur personal liability. Their ability to bind other members, or to require an indemnity from other members, depends on the law of agency and the rules of the association.

7.19 An unincorporated association might not be a perfect fit for a suspended society. An unincorporated association does not have a business purpose, and yet a society by definition carries on business.[486] Then again, if a society is no longer carrying on business – which might trigger its suspension or cancellation – then perhaps an unincorporated association is a suitable label.

7.20 A general partnership is where people carry on a business in common with a view of profit.[487] It is not a corporate body and does not have limited liability. Each partner can bind the others.[488] Each partner is jointly liable for all debts and obligations of the partnership,[489] and for any wrongs committed by a partner.[490]

7.21 It is not usual to describe a co-operative or community benefit society as seeking profit, although they do seek to be financially viable, and they might produce a trading surplus. This trading surplus might be reinvested, or in the case of a co-operative it might be distributed to members as a member dividend. Perhaps a trading surplus might be considered "profit" without stretching that concept too far.[491] In which case, a suspended society might be carrying on business as a partnership.

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481 CCBS Act, s 8(6).

482 CCBS Act, s 3(3).

483 CCBS Handbook, pp 323 to 325.

484 FCA Guide, para 8.17.4.

485 *Conservative and Unionist Central Office v Burrell* [1982] 1 WLR 522, 525 (Lawton LJ).

486 CCBS Act, s 2(1).

487 Partnership Act 1890, s 1.

488 Partnership Act 1890, s 5.

489 Partnership Act 1890, s 9.

490 Partnership Act 1890, ss 10, 12.

491 *English and Scottish Joint Co-operative Wholesale Society v Commissioner of Agricultural Income Tax, Assam* [1948] AC 405 (PC).

7.22 One solution to this uncertainty is simply for the CCBS Act to specify that, upon suspension, a society becomes a general partnership if it carries on business or otherwise an unincorporated association. However, even if a suspended society is deemed to be a general partnership or unincorporated association, there are further problems and uncertainties, as follows. Such characterisations would expose members to potential personal liability well beyond the value of their investment in the society, because of the loss of limited liability.

7.23 If a society holds a bank account in the name of "Co-operative Society Ltd", for example, but is then suspended, there is now no corporate body with limited liability to which that name can attach. Presumably that property is held on trust for the general partnership or unincorporated association. But the creation of that trust creates an added layer of legal complexity, and it creates practical difficulties, such as who can access the funds.

7.24 Similarly, contracts entered into with "Co-operative Society Ltd" might terminate due to the absence of any existing such contractual party. Likewise, for example, the contractual right of a tenant management organisation to manage property is usually conditional on the organisation being incorporated. If so, suspension, which in theory might only be temporary, has potentially long-term consequences if contracts are lost.

7.25 The CCBS Act says that suspension "does not affect any liability incurred by the society (which may be enforced against it as if the suspension had not occurred)".[492] In our view, this means that liability existing prior to suspension can be enforced against the society as if it were still a body corporate. This appears also to be the view of the FCA Guide.[493] For example, a claim could be issued against a suspended society using the name of the society.

7.26 In contrast, we think that liabilities incurred during suspension probably cannot be so enforced. A suspended society surely cannot incur any new liabilities as if it were not suspended. It would simply defeat the purpose of suspension if the society could carry on as before, acting as a corporate body with limited liability, having the benefit of registration under the CCBS Act. Rather, if the society becomes a general partnership, then new liabilities are incurred according to that law. It is only old liabilities that continue as if the society were not suspended.

7.27 Another solution here might be for the CCBS Act to provide that, after suspension, the society is deemed to have continued throughout as if registered.[494] However, that only achieves certainty by depriving suspension of any meaning. Why worry about suspension if at the end it was as if it never happened?

7.28 It is because of all these uncertainties that the question arises of whether to repeal the power to suspend. Some stakeholders are content with repealing the power of suspension. Some say that suspension serves as a warning prior to cancellation, so

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492 CCBS Act, s 8(6). The same wording is used in the context of cancellation: s 6(7).

493 FCA Guide, para 8.17.5.

494 Companies Act 2006, s 1028(1).

that repealing the power of suspension needs to be accompanied by improvements to the process of cancellation. We discuss cancellation below.

7.29 We note that the FCA has not used its power of suspension in recent years, even though it has used its powers of cancellation. In practice, suspension is not routinely used as a warning prior to cancellation.

7.30 We provisionally propose that the power of suspension be repealed. Its consequences are legally uncertain, it is not used in practice, and it can have drastic and permanent effects (rather than merely suspensory ones).

Consultation Question 40.

7.31 We provisionally propose that the power of the registrar to suspend a society's registration be repealed. Do you agree?

CANCELLATION

Procedure

7.32 Does the procedure for cancelling a society's registration need reform?

7.33 Currently, the registrar can cancel a society's registration.[495] The registrar must usually give the society at least two months' notice.[496] Upon cancellation, a society ceases to be entitled to any privileges under the CCBS Act.[497] Again, this means that the society will no longer be a body corporate with limited liability.[498]

7.34 The registrar can cancel a society's registration for various reasons.

(1) The registrar can cancel registration if it appears to the registrar that the society no longer meets the statutory definition of a co-operative or community benefit society.[499]

(a) The society has no right to appeal this decision,[500] although we have proposed otherwise above. The registrar must currently consider any representations which the society makes and accord the society a hearing if requested.[501]

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495 CCBS Act, s 5.

496 CCBS Act, s 6(1).

497 CCBS Act, s 6(7).

498 CCBS Act, s 3(3).

499 CCBS Act, s 5(5).

500 CCBS Act, s 9(3)(b).

501 CCBS Act, ss 7(2) and 7(3).

(b) After one month, if the society has not taken steps to convert into a company or dissolve, then the registrar may give directions to wind up the society's affairs.[502]

(2) The registrar can cancel registration where a society has requested this,[503] or where the society has converted into a company.[504] In these circumstances, there is no right to appeal the decision.[505]

(3) For other cancellations, a society has a right to appeal within the notice period.[506] While an appeal is pending, a society's registration cannot be cancelled, but it can be suspended.[507]

7.35 As with suspension, so too with cancellation, it seems that a society then becomes a general partnership or an unincorporated association.

7.36 This framework creates the following possible contradiction. On the one hand, the registrar is required to give at least two months' notice of cancellation, with the society able to question the decision to cancel. On the other hand, the registrar can direct the winding up of the society after only one month.

7.37 We provisionally propose that only after the notice period has passed should the registrar be able to give directions to wind up the affairs of the society. Such a minor amendment would avoid contradiction.

Consultation Question 41.

7.38 We provisionally propose that only after the notice period for cancellation has passed should the registrar be able to give directions to wind up the affairs of the society. Do you agree?

Notice period

7.39 What should be the notice period? As stated above, the registrar must currently give "at least" two months' notice. Where there is a right to appeal, that appeal can be brought at any time during that period. However, we think that a fixed period provides clarity, especially when its end triggers the ability of the registrar to cancel or give directions to wind up the society.

7.40 Is a fixed period of two months too short? This is the current minimum specified by the CCBS Act, and no stakeholder has yet told us that this needs to change. In

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502 CCBS Act, s 7(4).

503 CCBS Act, s 5(2).

504 CCBS Act, s 112(2).

505 CCBS Act, s 9(4).

506 CCBS Act, ss 9(1) and 9(5).

507 CCBS Act, s 6(3).

comparison, a housing body has 28 days to appeal against a decision of the Regulator of Social Housing to deregister it;[508] and an appeal to the First-tier Tribunal against a decision of the Charity Commission to deregister a charity must be brought within 42 days.[509] Thus, we think that a notice period under the CCBS Act of two months (about 60 days) is reasonable, especially if the society is given prior warning (discussed below).

Consultation Question 42.

7.41 We provisionally propose that the notice period for cancellation be fixed at two months. Do you agree?

Warnings

7.42 Some stakeholders have said that there needs to be a warning by the registrar before it invokes its power to cancel a society's registration. They also say that a society should have the opportunity to make any changes necessary to retain its registration.

7.43 It may be that under the current system the two months' notice of cancellation is itself the warning. It is not the case that, having given notice of cancellation, the registrar must inevitably proceed to cancellation. For example, the CCBS Act says that it is notice of a "proposed" cancellation;[510] an appeal suspends the cancellation;[511] and the registrar must give the society an opportunity to make representations that it meets the conditions for registration.[512] It must necessarily be the case that those representations could persuade the registrar not to cancel the society's registration; and of course a successful appeal will definitely have that effect. Furthermore, if at the time of the hearing the society can satisfy the registrar or the court that it *now* meets the requirements for registration – that is, that it has corrected any deficiencies – we think it would be perverse to insist on the cancellation anyway.

7.44 Having said that, we do acknowledge the good sense of giving societies warning of any deficiencies so that they can correct them rather than be faced immediately with the serious prospect of cancellation. It might provide greater clarity if the CCBS Act were to provide expressly for a prior warning. For its part, the FCA says that it is already its usual practice only to issue a notice of intended cancellation after earlier rounds of correspondence.

7.45 We do not propose to give a fixed time period for any warning (like a further two months, for example). Some deficiencies might be so serious that immediate

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508 Housing and Regeneration Act 2008, s 121.

509 The Tribunal Procedure (First-tier Tribunal) (General Regulatory Chamber) Rules 2009 (SI 2009 No 1976, s 26(1). See too: https://www.gov.uk/guidance/appeal-against-a-charity-commission-decision-about-your-charity

510 CCBS Act, s 6(1).

511 CCBS Act, s 6(3).

512 CCBS Act, ss 7(1) to (3).

compliance is necessary, and others might fairly take longer to correct. We think that the registrar should give a period of warning which is reasonable in the circumstances.

Consultation Question 43.

7.46 We provisionally propose that the CCBS Act should require the registrar to give a society reasonable warning before issuing any notice of proposed cancellation. Do you agree?

ENTRENCHMENT

Power to entrench

7.47 Should it be possible for a society to entrench any of its rules? Entrenchment is when a rule or rules can only be changed by a super-majority of votes.

7.48 For example, a company can change its articles by special resolution.[513] This requires a majority of not less than 75%.[514] However, section 22(1) of the Companies Act 2006 says that a company's articles may provide that certain of its articles can only be amended if conditions are met which are more restrictive than a special resolution. In this way, section 22 allows for entrenchment of certain articles.

7.49 Under the CCBS Act, there is no equivalent to section 22. Some stakeholders say that an equivalent would be useful. They say that it could enable a society to entrench its purposes or guard against de-mutualisation.

7.50 Some stakeholders say that, as a matter of common law, it might not be possible for a society to change rules in a way beyond the contemplation of the parties when originally agreeing to join the society and abide by its rules. In this way, it is said, rule changes which fundamentally alter the nature of the society might already be impermissible.[515]

7.51 In our view, there must be a risk in relying on this approach, for three reasons. First, the CCBS Act acknowledges that societies can change their rules.[516] Second, the CCBS Act says that amendments cannot require a member to incur greater liability without their consent.[517] The express inclusion of this principle might be taken as suggesting that all other changes are possible. Third, the CCBS Act allows that societies can take the drastic step, for example, of converting to a company. This surely counts as a fundamental change to the nature of the society.

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513 Companies Act 2006, s 21.

514 Companies Act 2006, s 283.

515 CCBS Handbook, pp 98 to 100.

516 CCBS Act, s 14(5).

517 CCBS Act, s 15.

7.52 Some stakeholders who supported the idea of entrenched rules nevertheless expressed concerns about whether this might conflict with the co-operative value of democracy if it enabled a member, in effect, to exercise a power of veto.

7.53 In our view, the co-operative value of democracy is best characterised as one vote per member (see Chapter 3). Beyond that, we see nothing objectionable in requiring different thresholds of support for different decisions. For example, there is nothing necessarily anti-democratic in requiring a unanimous or consensus vote.

7.54 One stakeholder was concerned that some societies might struggle to get a sufficient percentage of members to vote on an entrenched rule. However, what threshold should be set is a matter for each society. For example, a rule change need not require the approval of 80% of all members; it might only require the approval of 80% of all members who vote, as long as 50% of members vote. That might be more achievable. At any rate, the whole point of an entrenched rule is to make changing it difficult.

7.55 Overall, we think that it could be beneficial to give societies the same power as companies to entrench rules. We also think that it might be more fitting in some circumstances to entrench rules rather than engage an asset lock. This is because an asset lock is of general application, whereas entrenchment can target specific concerns. (We discuss asset locks further below.) Naturally a society would be well advised to think carefully about how it might wish to exercise any power to entrench rules.

Consultation Question 44.

7.56 We provisionally propose that societies be given a statutory power to entrench their rules. Do you agree?

Consultation Question 45.

7.57 We provisionally propose that it should be for the rules of a society to decide the voting threshold needed to change an entrenched rule. Do you agree?

When to entrench

7.58 The Companies Act 2006 says that provision for entrenchment can only be made in the company's articles on formation or by a later amendment to the company's articles agreed to by all members.[518] We are not currently persuaded to apply this restriction to the CCBS Act, for the following reasons.

[518] Companies Act 2006, s 22(2).

7.59 First, requiring unanimous consent of all existing members would likely prove impossible for many societies, making this power unusable, and any reform therefore ineffective.

7.60 Second, any amendment to a society's rules, to provide for entrenchment, would itself have to comply with the society's rules about how to amend those rules. This ensures that any amendment is democratic and consistent with the reasonable expectations of members who agreed to those rules in the first place.

7.61 Third, a community benefit society can impose a restriction on the use of its assets – the so-called asset lock. The CCBS Act says that the asset lock can be applied after formation by special resolution.[519] It does not require the approval of all members. We think that the same approach should apply to entrenchment.

Consultation Question 46.

7.62 We provisionally propose that a society's rules should be capable of being entrenched on registration or later by special resolution. Do you agree?

Meaning of special resolution for entrenching rules

7.63 We have proposed that a society's rules should be capable of entrenchment on registration or later by special resolution. What is required of a special resolution in order to entrench a rule?

7.64 In company law, a special resolution is defined in the Companies Act 2006.[520] In broad terms, it requires a majority of not less than 75% of voters.

7.65 The CCBS Act prescribes different voting thresholds for special resolutions in different instances, as follows.

(1) Ratification of actions by committee members beyond their capacity.[521] This requires one meeting where at least 75% of voters are in favour.[522]

(2) Amalgamation with or transfer of engagements to other societies.[523] This requires a first meeting where at least two thirds of voters are in favour, followed by a second meeting where over half of voters are in favour.[524]

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519 The Community Benefit Societies (Restriction on Use of Assets) Regulations 2006 (SI 2006 No 264), r 4(2).

520 Companies Act 2006, sch 8 and s 283.

521 CCBS Act, s 43.

522 CCBS Act, s 44.

523 CCBS Act, ss 109 and 110.

524 CCBS Act, s 111.

(3) Dissolution of a dormant society or credit union.[525] This also requires a first meeting where at least two thirds of voters are in favour, followed by a second meeting where over half of voters are in favour.[526]

(4) Conversion into a company.[527] This requires a first meeting where at least 75% of voters are in favour and at least 50% of members vote, followed by a second meeting where over half of voters are in favour.[528]

7.66 It is perhaps a little unusual that, in those instances where the CCBS Act prescribes that a society must act by special resolution, it then gives a different definition of special resolution for each of those instances. Nevertheless, the CCBS Act is clear in itself. No stakeholder has yet asked for these to be replaced by a single definition.

7.67 We think it would be useful to specify what is meant by a special resolution needed to entrench a rule. When a community benefit society chooses an asset lock by special resolution, that special resolution requires the same threshold as is required for conversion to a company.[529] In the CCBS Act, this corresponds with (4) above. It is the highest threshold of special resolution in the CCBS Act. We think that this high level is also appropriate when a rule is being entrenched: an entrenched rule is very hard to amend, so its adoption should require scrutiny and a very high level of support.

Consultation Question 47.

7.68 We provisionally propose that the special resolution threshold which must be exceeded in order to entrench a rule should be the same as the threshold required for adopting an asset lock, that is:

(1) a first meeting where at least 75% of voters are in favour and at least 50% of members vote, followed by

(2) a second meeting where over half of voters are in favour (see section 113 of the CCBS Act).

Do you agree?

525 CCBS Act, ss 119(3)(b) and (c).

526 CCBS Act, s 120.

527 CCBS Act, s 112.

528 CCBS Act, s 113.

529 The Community Benefit Societies (Restriction on Use of Assets) Regulations 2006 (SI 2006 No 264), r 4(2).

Overriding statutory thresholds

7.69 Society rules cannot override the default thresholds set out in the CCBS Act.[530] For example, a society can convert to a company by special resolution.[531] There is no provision in the CCBS Act for a society to require a higher threshold.

7.70 We think that some of the thresholds set in the CCBS Act should be minimums. One of the purposes of enabling entrenchment is, for example, to allow a society to set stricter voting thresholds to guard against demutualisation.

7.71 We think that a society should be able to set stricter thresholds for member votes than those in the CCBS Act in the following circumstances.

A higher minimum of supporting votes might be prescribed by society rules when:

(1) Ratifying action by members of the committee which would otherwise be beyond the capacity of the society.[532]

(2) Amalgamating societies or transferring engagements to another society.[533]

(3) Converting to, amalgamating with, or transferring engagements to a company.[534]

(4) Approving an instrument of dissolution.[535]

A lower maximum of dissenting votes (that is, a lower threshold for veto) might be prescribed by society rules when:

(5) Disapplying the duty to appoint auditors.[536]

7.72 There are two further points to make. First, there are other thresholds in the CCBS Act which are irrelevant to society rules. For example, the CCBS Act requires a special resolution to convert from a company to a society.[537] This has nothing to do with entrenchment of society rules.

7.73 Second, there are yet further thresholds in the CCBS Act which we do not think society rules should be able to change. For example, at least 10 society members must join in an application to the FCA for the FCA to appoint an accountant to inspect the society's books;[538] and at least 10% of members must join in an application to the FCA for the FCA to appoint inspectors to examine the society's affairs, or for the FCA

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530 FCA Guide, para 3.4.5.

531 CCBS Act, s 112.

532 CCBS Act, ss 43 and 44.

533 CCBS Act, ss 109 to 111.

534 CCBS Act, ss 112 to 113.

535 CCBS Act, ss 119 and 120.

536 CCBS Act, s 84.

537 CCBS Act, s 115.

538 CCBS Act, s 105.

to call a special meeting.[539] We do not think it should be possible for individual societies to tailor divergent powers for FCA intervention.

7.74 Because of these two points, we think that a society should not be able to set rules which override all statutory thresholds. We think that the CCBS Act should set out an exhaustive list of thresholds which might be overridden by society rules. We think that only the five situations identified above should be in that list.

Consultation Question 48.

7.75 We provisionally propose that a society should be able to set voting thresholds in its own rules which are stricter than those in the CCBS Act in the following circumstances.

(1) Ratifying action by members of the committee which would otherwise be beyond the capacity of the society.

(2) Amalgamating societies or transferring engagements to another society.

(3) Converting to, amalgamating with, or transferring engagements to a company.

(4) Approving an instrument of dissolution.

(5) Disapplying the duty to appoint auditors.

Do you agree?

ASSET LOCK

Asset locks and community benefit societies

7.76 Are the assets of community benefit societies already "locked"? Some stakeholders have said that the requirements that a society conduct its business solely for the benefit of the community, and that its assets be applied solely for the benefit of the community, makes the statutory asset lock redundant. In evaluating this claim, first, we will consider what the statutory asset lock entails, then we can compare this to what is expected of community benefit societies anyway aside from the statutory asset lock.

What is an asset lock?

7.77 Section 29 of the CCBS Act provides that HM Treasury may by regulations make provision enabling a community benefit society to ensure that its assets cannot be dealt with except for prescribed purposes. This is known colloquially as an asset lock.

[539] CCBS Act, s 106.

HM Treasury has made such regulations – for ease of reference, we will call them the Asset Lock Regulations.[540]

7.78 The Asset Lock Regulations provide that a community benefit society may impose a restriction on the use of its assets upon registration or later by special resolution.[541] The restriction on use which a community benefit society can adopt is only as follows.[542] The society must not use or deal with its assets except for a purpose which is directly or indirectly for the benefit of the community. The society may also deal with its assets to address a number of administrative scenarios, like repaying a member their withdrawable shares. The society may also transfer its assets to other bodies with similar asset-lock restrictions, including another community benefit society, or a community interest company, or a charity.

7.79 The restriction on use is not available to a registered social landlord or a charity.[543] A restriction on use, once implemented, is unalterable.[544] The registrar can issue an enforcement notice if it considers that the restriction on use has been contravened.[545] The registrar can require an officer to make good any loss if the officer was knowingly concerned in the contravention.[546] An enforcement notice can be appealed.[547]

What is expected of community benefit societies even aside from the statutory asset lock?

7.80 The FCA Guide says that a community benefit society must conduct its business entirely for the benefit of the community, without any secondary purpose.[548] Profits must be applied for the benefit of the community.[549] If the society sells its assets, the proceeds must be applied to benefit the community.[550] If the society dissolves, or converts to a company, the assets cannot be distributed to members.[551] Instead, the society could transfer its assets to a similar organisation with similar objects.[552]

7.81 The CCBS Act says that an instrument of dissolution must set out the intended distribution of the society's assets, or otherwise leave it to the award of the FCA.[553] Some model rules provide that, upon dissolution, any surplus assets are not to be

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540 The Community Benefit Societies (Restriction on Use of Assets) Regulations 2006 (SI 2006 No 264).

541 Asset Lock Regulations, r 4.

542 Asset Lock Regulations, rr 2 and 3, and sch 1.

543 Asset Lock Regulations, r 5.

544 Asset Lock Regulations, r 7.

545 Asset Lock Regulations, r 9.

546 Asset Lock Regulations, r 10.

547 Asset Lock Regulations, r 14.

548 FCA Guide, para 5.1.3.

549 FCA Guide, para 5.1.9.

550 FCA Guide, para 5.1.12.

551 FCA Guide, para 5.1.13.

552 FCA Guide, para 5.1.13.

553 CCBS Act, s 119(2)(d).

distributed to members, but shall be transferred, as members may decide, to a non-profit body subject to the same restriction on its distribution of profits.[554]

7.82 In line with the current approach in the FCA Guide, we provisionally proposed in Chapter 3 a definition of a community benefit society such that it carries on business for the sole benefit of the community. Does all this make the asset lock redundant?

7.83 We agree that if a community benefit society is defined as carrying on business for the sole benefit of the community, then that definition imposes a restriction on the use of its assets. In other words, an asset lock is not optional, but automatic. It flows inevitably from our proposed definition of a community benefit society that its assets can only be applied for the benefit of a community.

7.84 Nevertheless, we also think that the Asset Lock Regulations remain useful. First, regulations 8 to 16 give the registrar additional enforcement powers to protect the assets of a community benefit society. Second, regulation 6 lists the exceptions when assets can be used other than for the benefit of the community. These are pragmatic exceptions, and we have not yet heard any objections to them. It provides clarity to have those exceptions listed.

7.85 Given our view that, in effect, a community benefit society's assets are already "locked", we think that the Asset Lock Regulations should apply to all community benefit societies, and not simply those who submit to them by invoking the statutory asset lock via section 29 of the CCBS Act.

7.86 We think that there is little substantive difference between a community benefit society which invokes section 29, and one which does not – both must apply their assets only for the benefit of the community. We think that the Asset Lock Regulations should similarly be applicable to all community benefit societies.

7.87 Thus, we think that it would be beneficial to have the added value elements of the Asset Lock Regulations incorporated into the CCBS Act to indicate expressly when a community benefit society can deal with its assets other than for the benefit of the community, and to preserve the enforcement powers of the registrar. These rules would be applicable to all community benefit societies.

7.88 As with our other proposals, we think that this change would need to apply to all community benefit societies already in existence, and not only those registered after the change was introduced. We do not consider that this would be overly burdensome on societies given that the main restriction – the asset lock itself – effectively already applies to all community benefit societies.

[554] Co-operatives UK Community Benefit Society Model Rules.

Consultation Question 49.

7.89 We provisionally propose that the restrictions on the use of the assets of a community benefit society, and the enforcement powers in that regard, as set out in the Asset Lock Regulations, be included in the CCBS Act as applicable to all community benefit societies. Do you agree?

Asset locks and interest on share capital

7.90 One stakeholder has suggested that the wording of the Asset Lock Regulations be amended to confirm expressly that community benefit societies can pay interest on non-withdrawable share capital.

7.91 The Asset Lock Regulations currently allow a society to pay out the value of withdrawable share capital and any interest on it.[555] The Asset Lock Regulations do not say anything about interest on non-withdrawable shares.

7.92 The CCBS Handbook suggests that paying interest on non-withdrawable share capital is of at least indirect benefit to the community because it makes it more likely that the society can raise capital if interest is paid.[556]

7.93 Dealing with assets in a way which is indirectly for the benefit of the community is already permitted by the Asset Lock Regulations.[557]

7.94 Since withdrawable share capital is already expressly mentioned, it may provide certainty to address non-withdrawable share capital expressly as well. In our view, it should be permissible for a community benefit society to pay interest on non-withdrawable shares.

7.95 We discuss shares further in Chapter 5, where we have proposed that any rate of interest should be no more than necessary to obtain funding, and no more than a reasonable rate.

Consultation Question 50.

7.96 We provisionally propose that the CCBS Act should expressly allow for asset-locked community benefit societies to pay interest on non-withdrawable shares. Do you agree?

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555 Asset Lock Regulations, r 6(a)(1).

556 CCBS Handbook, p 91.

557 Asset Lock Regulations, sch 1 para 2(a); CCBS Act, s 29(2).

Asset locks and charitable status

7.97 Some stakeholders have said that a community benefit society with a statutory asset lock should be able to become a charity.

7.98 Currently, a community benefit society without a statutory asset lock can become a charity. In our view, as discussed above, community benefit societies are already asset locked in practice. So we see no reason to preclude a community benefit society with a statutory asset lock from becoming a charity. Indeed, becoming a charity tends to impose *greater* restrictions on the use of assets – it is not so much a loosening of a statutory asset lock, but a tightening.

7.99 However, a statutory asset lock, which is unalterable, allows assets to be distributed to non-charitable entities – and this makes it inconsistent with charity law. A community benefit society with a statutory asset lock wishing to become a charity would have to, for example, set up a charitable society and transfer engagements or amalgamate (it could not become a charity itself). Indeed, the Asset Lock Regulations allow a community benefit society with a statutory asset lock to transfer assets to a charity.

7.100 We think it inconsistent that a statutory locked asset can be held by a community benefit society, or transferred to a charity, but it cannot be held by a community benefit society with a statutory asset lock becoming a charity. It seems even more inconsistent when a community benefit society without a statutory asset lock can become a charity, even though the community benefit society is in effect asset-locked (albeit not by invoking the statute).

Consultation Question 51.

7.101 We provisionally propose that it should be possible for a community benefit society with a statutory asset lock to become a charity. Do you agree?

Asset locks and co-operatives

7.102 As we note above, section 29 of the CCBS Act provides that HM Treasury may by regulations make provision enabling a community benefit society to ensure that its assets cannot be dealt with except for prescribed purposes, and relevant regulations have been laid. In any case, we think that community benefit societies are effectively asset-locked even without the Asset Lock Regulations.

7.103 The CCBS Act does not provide for an asset lock for co-operatives. In Chapter 2, we provisionally proposed a definition of a co-operative such that it carries on business mainly for the benefit of its members. This does not automatically entail a restriction on the use of its assets. We discussed how any trading surplus might be variously applied: for example, to provide for education or to assist other co-operatives in fulfilment of the Fifth and Sixth Co-operative Principles respectively. In other words, any asset lock would be optional for a co-operative.

7.104 The Co-operatives, Mutuals and Friendly Societies Act 2023 allows for a statutory asset lock to be introduced for co-operatives by secondary legislation. HM Treasury has not yet made any regulations under the 2023 Act. Some stakeholders have suggested consolidating the 2023 Act into the CCBS Act.

7.105 There might be less need for an asset lock if societies are able to entrench their rules, as we have proposed above. However, no-one has suggested repeal of the 2023 Act. In which case, we think that it could make the CCBS Act more comprehensive and user-friendly if the asset lock provisions for co-operatives are contained within it, rather than in the separate 2023 Act.

7.106 Also, if the Asset Lock Regulations are to be incorporated into the CCBS Act in respect of community benefit societies, it may be more efficient simply to repeat them as applicable to co-operatives, rather than await possible future regulations. We see no reason why the provisions of the current Asset Lock Regulations would not also be suitable for co-operatives. Their application to both forms of society would also promote consistency and clarity. The incorporated Asset Lock Regulations would then apply mandatorily to all community benefit societies, and also to those co-operatives who choose a statutory asset lock.

Consultation Question 52.

7.107 We provisionally propose that the asset lock provisions of the Co-operatives, Mutuals and Friendly Societies Act 2023, as far as they apply to co-operatives, should be consolidated into the CCBS Act. Do you agree?

Consultation Question 53.

7.108 We provisionally propose that the Asset Lock Regulations which apply to community benefit societies should also apply to co-operatives which choose a statutory asset lock. Do you agree?

CONVERSIONS, TRANSFERS, AMALGAMATIONS

Conversion from a company

7.109 A company can convert to a society by special resolution.[558] Once registered under the CCBS Act, the registration under the Companies Acts becomes void and must be cancelled.[559]

7.110 Under section 115 of the CCBS Act, the special resolution must appoint three members of the company to carry out the following two functions relevant to

[558] CCBS Act, s 115(1).

[559] CCBS Act, s 115(10).

conversion. First, to sign the society's rules.[560] Second, to accept amendments to the rules required by the FCA, or to lay the amendments before the company in a general meeting.[561]

7.111 Additionally, the society will need to comply with section 2(2)(b) of the CCBS Act. That requires either three members, or two members if both are registered societies. We have not heard any argument that section 2(2)(b) needs reform.

7.112 One stakeholder has suggested that conversion from a company to a society registered under the CCBS Act should only require two members, not three.

7.113 We agree that it should be possible to convert from a company to a society with only two members, as long as both members are already registered societies. This would then be consistent with registering a society in the first place. That said, we doubt how often a company would have two members which are registered societies.

Consultation Question 54.

7.114 We provisionally propose that section 115 of the CCBS Act should be amended so that, when a company converts to a society, it must appoint either three members, or two members if both are registered societies. Do you agree?

Partial transfers of engagements

7.115 A society registered under the CCBS Act may by special resolution transfer its engagements to any other registered society that undertakes to fulfil them.[562] A transfer of engagements means a transfer of business, which includes contracts with their attendant rights and liabilities.[563] Should the CCBS Act clarify that partial transfers of engagements are possible?

7.116 Section 110(1) of the CCBS Act says simply that a society may "transfer its engagements" to another society. It does not say either way whether a society can transfer only some of its engagements. In contrast, it does say that the transfer of engagements can be accompanied by a transfer of "all or part" of the property of the transferring society.[564]

7.117 On the one hand, the statutory context of Part 9 of the CCBS Act might be described as dealing with total transformation of societies: the amalgamation of societies; the dissolution of a society; the conversion of a society into a company. This context

560 CCBS Act, s 115(3).

561 CCBS Act, s 115(4).

562 CCBS Act, s 110(1).

563 CCBS Handbook, p 301.

564 CCBS Act, s 110(2).

would suggest that a society must transfer all engagements – in contrast to the explicit reservation that property need only be transferred in part.[565]

7.118 On the other hand, section 112(1) provides that a society can convert to a company, amalgamate with a company, or "transfer its engagements" to a company. Section 112(2) then says that the society's registration becomes void if it is registered as a company, amalgamates with a company, or "transfers all its engagements" to a company (emphasis added). The word "all" in section 112(2) suggests that section 112(1) can include partial transfers. And section 112(1) uses the same language as section 110(1).

7.119 On balance, we see no reason in principle to exclude partial transfers of engagements to another society. We think that this is contemplated by section 112 in the context of transfers to a company. We think that it would improve certainty if the CCBS Act said explicitly that partial transfers of engagements are possible (whether to another society or to a company).

Consultation Question 55.

7.120 We provisionally propose that the CCBS Act should provide expressly that partial transfers of engagements are possible, to companies or to other registered societies. Do you agree?

Conveyancing

7.121 When two societies amalgamate, the CCBS Act says expressly that property vests in the amalgamated society without the need for any conveyance.[566] Similarly, where engagements are transferred to another society, the CCBS Act says expressly that any property also transferred vests in the receiving society without conveyance.[567]

7.122 Where a society converts to, or amalgamates with, or transfers engagements to a company, the CCBS Act says nothing about whether property vests without conveyance. Should property vest here too without conveyance?

7.123 In our view, where a society converts into a company, no conveyance is possible. There is no time when both the society and the company exist so as to enable the former to make a conveyance to the latter.[568] A single corporate body with a set of property holdings persists throughout – it just changes its legal clothes from society to company.[569] We are reinforced in this view by the fact that the CCBS Act says that

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565 A view shared by the CCBS Handbook, p 300.

566 CCBS Act, s 109(3).

567 CCBS Act, s 110(2).

568 See too: CCBS Handbook, p 306.

569 *Mount Wellington Mine Ltd v Renewable Energy Co-operative Ltd* [2021] EWHC 1486 (Ch) at [28] to [41] by HHJ Paul Matthews.

any pre-conversion right, claim or penalty against the society has priority as against the *company's* property.[570]

7.124 Similarly, when a society amalgamates with a company, it might again be said that there is no time when both the society and the amalgamated company exist so as to enable the former to make a conveyance to the latter.

7.125 Nevertheless, we think that it would be preferable, to increase certainty, for the CCBS Act to say explicitly that transfers of property vest without conveyance when a society converts to or amalgamates with a company (just as the CCBS Act says so explicitly for a society amalgamating with another society).

7.126 This leaves a transfer of engagements from a society to a company. This may or may not entail the transfer of property. After a transfer of engagements, a society can continue to exist. In these circumstances, a conveyance is possible. Dispensing with the need for a conveyance in these circumstances is something which the CCBS Act could do.

7.127 To repeat, where a society transfers its engagements to another society, the CCBS Act already says that no conveyance is needed. It would therefore be consistent if no conveyance were needed where a society transfers its engagements to a company.

7.128 The CCBS Act is already consistent in how it protects creditors, whether it is a society-to-society event or a society-to-company event, as follows. Where two societies amalgamate,[571] or one society transfers its engagements to another society,[572] the CCBS Act says expressly that this does not prejudice any right of a creditor of either society. Where a society amalgamates with a company, or transfers its engagements to a company, again the CCBS Act says expressly that this is without prejudice to any right of a creditor of the society.[573] Similarly, where a society converts to a company, the CCBS Act says expressly that this does not affect any right or claim or penalty against the society,[574] which can be enforced against the society as if the society had not been registered as a company.[575] There does not appear to be any gap in the protection of third parties.

Consultation Question 56.

7.129 We provisionally propose that, where a society converts to, amalgamates with, or transfers its engagements to a company, any transfer of the society's property should vest without conveyance. Do you agree?

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570 CCBS Act, s 114(5).

571 CCBS Act, s 109(5).

572 CCBS Act, s 110(4).

573 CCBS Act, s 112(5).

574 CCBS Act, s 114(3).

575 CCBS Act, s 114(4).

Automatic cancellation

7.130 One stakeholder has suggested that registration should be void automatically when a society amalgamates with another society or transfers all its engagements to another society.

7.131 Currently, when a society converts to a company, or amalgamates with a company, or transfers all its engagements to a company, the society's registration under the CCBS Act becomes void (automatically) under section 112.[576] Yet the registration will still need to be manually cancelled by the registrar.[577] In the case of transfer of engagements, cancellation must not happen until a certificate has been lodged with the registrar, under section 126, certifying that all society property has been duly conveyed or transferred.[578]

7.132 There is no provision, equivalent to the provision in section 112, that registration is automatically void when a society amalgamates or transfers all its engagements to another society.

7.133 We question how a registration can be void but not cancelled – indeed, how registration can be void when cancellation is forbidden until a further event (a certificate lodged under section 126). We consider this to be a contradiction in terms. Further, it cannot mean void as if the registration were never valid, since section 112 only applies when there is a change (from a society to a company); it does not impugn the society's original registration. We question therefore how the provision for automatic voidness in section 112 works in practice.

7.134 One explanation we have been given is that the registration becomes void only once all the procedures have been complied with, which includes lodging the certificate. Even on this reading, the statute still says that the "registration…becomes void and…must be cancelled", which still suggests two different events, with cancellation being subsequent to voiding.

7.135 In our view, rather than extending any provision which renders registration automatically void but not cancelled, we think it would be better to repeal any reference to registration becoming automatically void as it is not clear what this means in the context or how it works.

7.136 Further, we have heard doubt as to whether the cancellation happens under section 112, or section 126, or section 5, for example on the basis that the society has ceased to exist.[579]

7.137 In our view, section 126 only says when cancellation "must not" occur, rather than providing any power to cancel. Otherwise, section 5 says when the FCA "may" cancel

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576 CCBS Act, s 112(2).

577 CCBS Act, s 112(2) says that the registration becomes void "and must be cancelled".

578 CCBS Act, s 126.

579 CCBS Act, s 5(3)(c).

a society, and section 112 says when the FCA "must" cancel a society. We think that the CCBS Act is sufficiently clear here without any need for reform.

Consultation Question 57.

7.138 We provisionally propose that section 112 (conversion of a society to a company) be amended to remove reference to a society's registration being void. Do you agree?

POWERS OF THE REGISTRAR

7.139 Our Terms of Reference (in Appendix 1) ask us to consider how reform might create a "more proportionate and effective regulatory environment". The FCA has requested the following issues be considered for consultation.

Advertising

7.140 The CCBS Act requires the FCA to advertise cancellation in the Gazette and a local newspaper.[580] The FCA say that advertising in a local newspaper is an unnecessary cost (ultimately funded by societies through FCA fees). The FCA says that it has never once received any inquiry deriving from an advertisement in a local newspaper. We note that under the CCBS Act, cancellation takes effect from the date of cancellation in the Gazette, regardless of when the advertisement is published by the local newspaper.[581]

7.141 We are sympathetic to this request to simplify the process and reduce its cost. On the other hand, we doubt that members of societies regularly read the Gazette. Given the often local nature of co-operatives and community benefit societies, advertising in a local newspaper is more likely to inform members of what is happening. A member might want to act on that information in ways other than contacting the FCA.

7.142 We think that whatever rule applies to advertising cancellation should similarly apply to advertising dissolution (which also currently requires advertising in the Gazette and a local newspaper).[582]

Consultation Question 58.

7.143 Do you think that the registrar should advertise the cancellation of a society's registration or its dissolution in a local newspaper as well as in the Gazette?

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580 CCBS Act, s 6(6).

581 CCBS Act, s 6(7).

582 CCBS Act, s 122(1).

Forbearance on filing accounts

7.144 During the Covid-19 pandemic, all companies were given an automatic three-month extension for filing their reports.[583]

7.145 Currently, for societies, if the FCA offers a period of forbearance for the late filing of reports, that cannot override the statutory duties in the CCBS Act. Technically, failing to comply with such statutory duties would remain a criminal offence.

7.146 In company law, the Secretary of State can, on an application, extend deadlines for filing annual reports "for any special reason",[584] and otherwise make regulations about the time for filing annual reports.[585] The FCA has suggested that a similar mechanism be available for societies.

7.147 We agree that, as a lesson learned from the pandemic, it could be useful to have a provision in the CCBS Act which allows HM Treasury by regulation to disapply duties under the CCBS Act temporarily for special reason.

Consultation Question 59.

7.148 We provisionally propose that the CCBS Act should enable HM Treasury by regulation to disapply duties under the CCBS Act temporarily for special reason (such as a pandemic). Do you agree?

Electronic submission

7.149 Should it be possible for the registrar to require societies to submit their reports electronically?

7.150 Currently, the registrar can prescribe what form any electronic submission should take, but cannot require electronic submission.[586] Historically, we are told, paper submissions were made in duplicate: one for the registrar to retain, the other to stamp and return to the society. The FCA would like to be able to require electronic submission of documents. They say that this would make their processes more efficient, and could feed into returns for HMRC. In comparison, Companies House can

583 https://www.gov.uk/government/news/companies-to-receive-3-month-extension-period-to-file-accounts-during-covid-19.

584 Companies Act 2006, s 442(5).

585 Companies Act 2006, s 468.

586 CCBS Act, s 144.

require electronic filing,[587] and are moving to electronic-only filing because, they say, it is more efficient and transparent (searchable).[588]

7.151 Some stakeholders support a move to electronic submission. They would also like to see returns searchable online. Presumably at present, those societies who wish to submit electronically, do so. In contrast, other stakeholders were concerned that some small societies might struggle with the technology if electronic submission were mandatory. This might especially affect societies run by older people.[589]

7.152 We can see the efficiency and transparency benefits of requiring electronic submission, but we are wary about making any proposal which will disadvantage the digitally poor to the point where they might be incapable of continuing to comply with legislation. We seek the views of consultees.

Consultation Question 60.

7.153 Do you think that the CCBS Act should empower the registrar to require electronic-only filing of documents?

Signatures

7.154 The FCA want to dispense with the need for signatures on filed accounts. Currently under the CCBS Act, any revenue account or balance sheet must be signed.[590] The FCA say that signatures can inhibit some electronic transmission processes. Also, they wish to avoid signatures appearing publicly on documents, for example to avoid those signatures being copied fraudulently. In comparison, the need for signatures on filed accounts was withdrawn for companies, as an aid to electronic filing.[591]

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587 Previously, under s 1068 of the Companies Act 2006, the registrar could impose requirements as to the manner of delivery of documents, including a requirement of electronic delivery. However, that was seemingly modified by s 1069, which provided that the Secretary of State may make regulations requiring documents to be delivered to the registrar by electronic means. Now, s 1069 has been repealed by section 75 of the Economic Crime and Corporate Transparency Act 2023, explicitly so as to facilitate electronic delivery. With that repeal, all that remains is the general power under s 1068. The only constraint on that power is that the requirement must be imposed by "registrar rules" (s 1068(4A)) – which is no real burden at all (see s 1117).

588 For the commitment to electronic-only filing, see: https://companieshouse.blog.gov.uk/2023/02/10/changes-to-accounts-part-1-moving-to-software-only-filing/; and https://changestoukcompanylaw.campaign.gov.uk/changes-to-accounts/.

589 For example, Age UK report that around 22% of people aged over 65 do not use the internet: https://www.ageuk.org.uk/latest-press/articles/2023/age-uk-research-finds-many-older-people-are-struggling-to-access-local-public-services-in-an-increasingly-digital-world/#_edn4.

590 CCBS Act, s 82(1) row 1.

591 *Buckley on the Companies Acts* para 1707.

7.155 Societies are already under a duty to prepare accounts,[592] and to ensure that their accounts are true and fair.[593] Breach of that duty can incur criminal liability.[594] We question whether signatures on filed accounts add any further value. For these reasons, we provisionally propose repealing the need for signatures on filed accounts.

Consultation Question 61.

7.156 We provisionally propose repealing the need for signatures on a society's filed accounts. Do you agree?

Fines for late submissions

7.157 The FCA would like to have the power to fine societies who are late with their annual returns.

7.158 A society is under a duty to provide an annual return.[595] It is a criminal offence to fail to do anything required by the CCBS Act.[596] Continuing default produces a new offence every week.[597] Any offence committed by the society can also be treated as an offence by the responsible society officer or even every committee member.[598] These are all criminal offences. There is currently no civil sanction for late submission.

7.159 By way of comparison, companies are similarly under a duty to file annual returns.[599] Failure to do so can result in criminal liability for any director.[600] In addition, late filing of annual returns can result in the company incurring liability for a civil penalty (a fine), paid to the registrar.[601] When companies file late, the fine for a private company ranges from £150 to £1500,[602] and can double for late submission in successive years.[603]

7.160 Some stakeholders agree that there should be a less serious consequence than criminal prosecution for late submission of annual returns. They say that societies should be taking their responsibilities seriously and making returns, and that there should be consequences for failing to do so, but that criminal prosecution is likely to

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592 CCBS Act, ss 75 and 79.

593 CCBS Act, s 80.

594 CCBS Act, s 80(4); ss 127 and 128; s 131.

595 CCBS Act, s 89.

596 CCBS Act, s 127.

597 CCBS Act, s 129.

598 CCBS Act, s 128.

599 Companies Act 2006, s 441.

600 Companies Act 2006, s 451.

601 Companies Act 2006, s 453.

602 < 1 month late, £150; 1 to 3 months, £375; 3 to 6 months, £750; > 6 months, £1500.

603 The Companies (Late Filing Penalties) and Limited Liability Partnerships (Filing Periods and Late Filing Penalties) Regulations 2008 (SI 2008 No 497).

be justifiable only in very extreme circumstances. Some stakeholders say that the registrar should send out reminders prior to issuing fines. Some say that small societies might not be able to afford fines. At any rate, stakeholders tend to say that fines should be modest, or at least in line with company law.

7.161 We are sympathetic to the demands placed on small societies. However, even small societies must abide by their legal obligations. An annual return need not be too demanding, especially where a small society might opt out of an audit (we discuss audits below). An annual return is simply one of the reciprocal duties of benefitting from the bestowal of the legal form. It may be that small societies cannot afford fines, but a criminal prosecution is likely to have yet more severe consequences.

7.162 We are told that the FCA does provide an email reminder service for any society which signs up. We do not think that the FCA should be under a statutory duty to send out reminders. Similarly, Companies House provides an email reminder service for companies to file their accounts, but this is not a statutory requirement either.[604] The CCBS Act is clear about the duty to submit an annual return, and the FCA Guide provides further information. It is for societies who choose to register under the CCBS Act to appreciate and comply with their duties thereunder.

7.163 On the one hand, it could be appropriate to have a lesser sanction for late submission than criminal prosecution. The civil penalty of a fine might be more appropriate, and more efficient administratively for the registrar (and without burdening the criminal courts). The threat of fines might still provide a sufficient incentive towards compliance.

7.164 On the other hand, civil fines for late submissions are not currently available, and prosecutions seem to be rare. We note that the FCA has not brought any prosecutions between 2020 and 2022. If civil fines were available, they may well be regularly imposed – so any reform here would in practical terms increase the exposure of societies to penalty. We also think that there should be a mechanism for appealing any decision to impose a fine.

Consultation Question 62.

7.165 Do you think that the registrar should have the power to impose a civil penalty in the form of a fine on a society which is late in filing their annual return (in line with equivalent penalties under company law)?

Name changes

7.166 The FCA has asked for a power to direct a society to change its name after registration.

7.167 Some stakeholders support the idea that the registrar should be able to require a name change after registration. They say that this might be appropriate, for example,

604 https://www.gov.uk/government/publications/late-filing-penalties/late-filing-penalties#avoiding-a-penalty

where a society has changed its purposes. Some stakeholders say that such a power should be used sparingly, for example only where the society's name is now misleading, offensive, or unlawful.

7.168 Other stakeholders warn that the process requirements for a name change in a society's rules are cumbersome and should not be engaged lightly. They say that a name change could cause practical problems: for example, it would require changes with the society's bank. We would add that a change of name could also impact negatively upon a society's goodwill, if it has built up a reputation or presence under a previous name.

7.169 Currently, a society may not be registered under a name which in the opinion of the registrar is undesirable.[605] According to the FCA Guide, this might be because the name is too similar to another, or is misleading or offensive.[606]

7.170 A society can change its name after registration.[607] Also, a society must have the word "limited" in its title, or "cyfngedig" if Welsh and preferred.[608] This is not a requirement if the society is wholly charitable.[609] If a society is no longer wholly charitable, the registrar can direct a change of name after registration to include "limited".[610]

7.171 Thus, the registrar can refuse a name at registration, or refuse a name after registration when the society wishes to change its name, and it can require a name change after registration when the society was charitable but is no longer. There is otherwise no power to direct a change of name after registration more generally.

7.172 In comparison, in charity law, the Charity Commission can require a charity to change its name or working name if, for example, it is liable to mislead the public as to the charity's activities or purposes.[611]

7.173 We can see the sense of empowering the registrar to direct a name change, for example if the activities of the society have since changed. We agree that this power should be used sparingly. We think it would be preferable for the powers to direct a name change at registration and after registration to align. This encourages consistency and understanding. We also think that there should be a right to appeal a direction to change name after registration, given the potentially significant consequences to the society discussed above. Accordingly, we make the following provisional proposals.

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605 CCBS Act, s 10(1).

606 FCA Guide, para 3.8.2.

607 CCBS Act, s 13.

608 CCBS Act, s 10(2).

609 CCBS Act, s 10(3).

610 CCBS Act, s 10(4).

611 Charities Act 2011, s 42.

Consultation Question 63.

7.174 We provisionally propose as follows.

(1) The registrar should be able to direct a society to change its name after registration if the name has since become undesirable in the opinion of the registrar.

(2) There should be a right to appeal such a direction.

Do you agree?

Mutuals Public Register

7.175 The FCA maintains the Mutuals Public Register and provides copies of documents held by the FCA.[612] The FCA has suggested that the Mutuals Public Register be identified explicitly in the CCBS Act as the sole register which the FCA must keep in this regard. In comparison, the register of companies is explicitly identified in the Companies Act 2006.[613]

7.176 We agree that it could improve clarity if the CCBS Act were to identify explicitly the Mutuals Public Register as the register which the FCA should maintain.

Consultation Question 64.

7.177 We provisionally propose that the Mutuals Public Register be identified explicitly in the CCBS Act as the sole register which the registrar of societies is to maintain. Do you agree?

Registrar's seal

7.178 The FCA have suggested that their seal as registrar of co-operatives and community benefit societies should be provided for under the CCBS Act.

7.179 Co-operative and community benefits societies used to register under the Industrial and Provident Societies Act 1965. Under the 1965 Act, the registrar was the Registrar of Friendly Societies. That Registrar was given a seal under the Friendly Societies Act 1974. New friendly societies can no longer register under the 1974 Act; they must instead register under the Friendly Societies Act 1992. The 1992 Act created the Friendly Societies Commission to replace the Registrar of Friendly Societies. In 2001, the responsibilities of the Friendly Societies Commission were transferred to the

612 FCA Guide, para 2.3.1.

613 Companies Act 2006, s 1080.

Financial Services Authority,[614] and then transferred again in 2013 to the FCA.[615] The FCA is of course the registrar under the CCBS Act, but the FCA's seal for its role under the CCBS Act remains under the 1974 Act.[616]

7.180 We question how much practical difference it might make to provide the registrar of the CCBS Act with a seal under the CCBS Act rather than under the 1974 Act. This might seem little more than an exercise in tidying. However, any change would require amending legislation, and this might be the best opportunity. We currently see no objection in acceding to the idea that the seal of the registrar of co-operative and community benefit societies be provided for under the statute which regulates the registration of such societies.

Consultation Question 65.

7.181 Do you think that the seal of the registrar of co-operative and community benefit societies be provided for under the CCBS Act?

Threshold for intervention

7.182 Some stakeholders would like the registrar to intervene more in the running of societies, for example when members perceive a society to be acting less than democratically. In contrast, some stakeholders think that the registrar should have a more administrative and less interventionist role. Here we consider whether the threshold for intervention by the registrar need revisiting.

7.183 Under the CCBS Act, the registrar may, on the application of at least 10 members of a society, appoint an accountant to inspect the society's books and report on them.[617] Also, on the application of 10% of members, the registrar can appoint an inspector to examine the society's affairs.[618] The registrar can also call a special meeting of the society.[619] An inspector can examine a society's officers on oath.[620] The special meeting has all the powers of a meeting called in accordance with the society's rules.[621] If those inspections or examinations reveal that a society or its officers have been failing to fulfil their duties under the CCBS Act, this might constitute a criminal offence.[622] The registrar may be able to bring a prosecution.[623]

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614 The Financial Services and Markets Act 2000 (Mutual Societies) Order (SI 2001 No 2617).

615 The Financial Services Act 2012 (Mutual Societies) Order (SI 2013 No 496).

616 CCBS Act, s 149.

617 CCBS Act, s 105.

618 CCBS Act, s 106(1)(a).

619 CCBS Act, s 106(1)(b).

620 CCBS Act, s 107(2)(b).

621 CCBS Act, s 107(4)(a).

622 For example, see: CCBS Act, ss 127 and 128.

623 CCBS Act, s 132.

7.184 The registrar has additional powers under the Asset Lock Regulations. Thereunder, the registrar can issue an enforcement notice requiring a community benefit society to take steps to ensure that its assets are used only for the benefit of the community.[624] It can require an officer complicit in a society's default to make restitution.[625] It can also require the officer to be removed.[626] In the meantime, the registrar can apply to the court for an injunction.[627] Any decision of the registrar in these regards can be appealed.[628]

7.185 Further, the registrar has some of the same powers in respect of societies as are available against companies under Part 14 of the Companies Act 1985.[629] For example, the registrar can appoint inspectors where circumstances suggest that the society is defrauding creditors, is engaged in misconduct towards its members, or is withholding information from its members.[630] A warrant can be issued to enter and search premises.[631]

7.186 The Asset Lock Regulations,[632] and the powers under Part 14 of the Companies Act 1985,[633] require the registrar to exercise its powers thereunder "only to the extent necessary to maintain confidence" in societies.

7.187 We question whether this threshold is appropriate. It is highly abstract, and very difficult to evaluate except in hindsight. It also appears to be a relatively high bar for intervention. Will any singular instance of misbehaviour by a society, if left without response, cause the public to lose confidence in societies in general? For example, history is full of rogue companies, and yet the company remains a popular choice of form, and most consumers and businesses seem sufficiently content to trade with companies.

7.188 We provisionally propose a change of threshold for intervention. We think that the registrar should be able to use its powers of intervention, where the statutory conditions for their exercise are otherwise fulfilled (such as an application by at least 10 members), simply if the registrar believes that intervention is appropriate in the circumstances.

7.189 We recognise that this is a lower bar for intervention than the current threshold. We do not think that the registrar need intervene in every instance of misbehaviour or breach

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624 Asset Lock Regulations, r 9.

625 Asset Lock Regulations, r 10.

626 Asset Lock Regulations, r 11.

627 Asset Lock Regulations, r 15.

628 Asset Lock Regulations, r 14.

629 The Co-operative and Community Benefit Societies and Credit Unions (Investigations) Regulations (SI 2014 No 574).

630 Companies Act 1985, s 432.

631 Companies Act 1985, s 448.

632 Asset Lock Regulations, r 8.

633 The Co-operative and Community Benefit Societies and Credit Unions (Investigations) Regulations (SI 2014 No 574), r 3.

of statutory rules, but we think our proposed standard gives a suitable level of discretion to the registrar.

Consultation Question 66.

7.190 We provisionally propose that the registrar should be able to use their available powers of intervention where the registrar believes that intervention is appropriate in the circumstances (rather than "only to the extent necessary to maintain confidence" in societies). Do you agree?

AUDITS

Simplifying audit

7.191 Some stakeholders have said that the audit rules in the CCBS Act should be simplified.

7.192 The current position is as follows. A society must appoint a qualified auditor to audit its accounts and balance sheet for each year of account.[634] A qualified auditor is a person eligible for appointment as a statutory auditor under Part 42 of the Companies Act 2006.[635] However, a small society may instead appoint at least two people who are not qualified auditors to audit its accounts.[636] A small society is, in rough terms, one worth less than £5k.[637] Nevertheless, the registrar may direct a small society to appoint a qualified auditor anyway.[638] By section 84, a society may by resolution disapply the duty to appoint auditors, where the society's assets are less than £5.1m and its annual turnover is less than £10.2m[639] – or where its annual turnover is less than £250k in the case of a charity.[640] But this does not avail certain societies: credit unions, registered social landlords, holding and subsidiary societies, and those taking deposits.[641]

7.193 The registrar can disapply a society's power to seek such a resolution,[642] and can again require the appointment of qualified auditors.[643] Even if such a resolution is passed, a society with a turnover exceeding £90k must still appoint a qualified auditor

634 CCBS Act, s 83(1).

635 CCBS Act, s 91.

636 CCBS Act, s 83(2).

637 Specifically, its receipts and payments for the previous year do not exceed £5k, and its assets do not exceed £5k, and it has fewer than 500 members: CCBS Act, s 83(4).

638 CCBS Act, s 83(3) and s 86.

639 CCBS Act, s 84(1).

640 CCBS Act, s 84(5).

641 CCBS Act, s 84(3).

642 CCBS Act, s 84(4).

643 CCBS Act, s 86.

to make a report on its accounts.[644] That report requires the auditor to say whether the revenue account and balance sheet are in agreement with the books of account and whether they are properly prepared – these things are also required in a full audit[645] – and whether the financial threshold for disapplying the duty to audit has been met.[646]

7.194 This creates the following situation. A society smaller than £5k must audit, unless it resolves not to, with a professional auditor or with two non-professionals. A society between £5k and £90k must audit, unless it resolves not to, with a professional auditor. A society between £90k and £10.2m must audit, unless it resolves not to, but must still appoint a professional auditor to issue a "report" which at the least overlaps with some of the requirements of an audit. A society over £10.2m must audit. The registrar can always insist upon an audit.

7.195 Some of the audit thresholds in the CCBS Act can be amended. The CCBS Act provides that HM Treasury may by order make such modifications to the CCBS Act as they consider appropriate for the purpose of assimilating society law with any updates to company law.[647] Indeed, the current threshold in section 84 was updated in this way.[648] The £5k threshold can similarly be updated by regulations.[649] Other thresholds in the CCBS Act cannot be updated in this way, since they do not purport to align with company law.

7.196 In comparison, a company's accounts must be audited, by a qualified auditor,[650] unless it is a small company, a subsidiary, dormant, or subject to public sector audit.[651] A small company has turnover less than £10.2m and a balance sheet less than £5.1m.[652] The small company exception is not available to certain types of company, like insurers or banks.[653] Members of a small company can require the company to obtain an audit anyway, by notice from not less than 10% of members.[654]

7.197 In further comparison, larger charities must have their accounts audited by a professional auditor; a larger charity has gross income in excess of £1m or assets in excess of £3.26m.[655] For smaller charities, if a charity has a gross income in excess of £25k, it must appoint an auditor or an independent examiner – and that independent examiner must have a specified qualification if the charity's gross income exceeds

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644 CCBS Act, s 85(1).

645 CCBS Act, s 87(4). Indeed, the auditor even has similar powers as under a full audit: compare the powers under s 87 (full audit) and s 88 (lesser "report"); and see FCA Guide, para 7.2.23.

646 CCBS Act, s 85(2).

647 CCBS Act, s 134.

648 The Co-operative and Community Benefit Societies Act 2014 (Amendments to Audit Requirements) Order 2018 (SI 2018 No 322).

649 CCBS Act, s 83(5).

650 Companies Act 2006, Pt 42.

651 Companies Act 2006, s 475.

652 Companies Act 2006, ss 477 and 382.

653 Companies Act 2006, s 478.

654 Companies Act 2006, s 476.

655 Charities Act 2011, s 144.

£250k. The Charity Commission can nevertheless require an audit.[656] Where the charity is a company, if the Companies Act 2006 requires an audit, that trumps the rules under the Charities Act 2011.[657] None of these rules apply to exempt charities.[658]

7.198 In our view, the audit rules which apply to societies could be simplified. We provisionally propose that the CCBS Act provide as follows:

(1) Any person appointed to audit the accounts should be a qualified auditor.

(2) A society should be able to opt out of the duty to audit accounts when the society is below a certain size.

(a) There should be a single threshold (above which a society cannot opt out of the requirement to audit).

(b) That threshold should be both that turnover is not in excess of £10.2m and assets are not in excess of £5.1m.

(c) That threshold should be capable of revision by statutory instrument.

(3) The registrar should be able to insist upon an audit.

7.199 These are our reasons.

(1) Where a society chooses to audit, or is required to audit, we think that the audit should be done by a qualified auditor. The audit is for the benefit of members and the public. It should be reliable.

(2) An audit may be an expense which small societies cannot sustain. Some stakeholders say that this expense can even encourage societies to convert to companies. Therefore we propose a limit below which societies can opt out of the requirement to audit. This principle is already found consistently in the CCBS Act, in company law, and in charity law.

The CCBS Act provides that a small society can opt out of an audit. In comparison, a small company has no duty to audit, although its members can vote to audit (they can opt in). For societies, we propose to keep the current opt out approach. Similarly, we propose to keep the current list of societies which cannot opt out. In both cases, we have not heard of any need for reform.

(a) We think that having a single threshold makes for greater clarity, instead of the current regime of multiple overlapping thresholds.

(b) The threshold we propose is that currently found in section 84 of the CCBS Act. (The same threshold applies in company law.) Below this threshold, some societies might choose not to opt out. For example,

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656 Charities Act 2011, s 146.

657 Charities Act 2011, s 147.

658 Charities Act 2011, s 160.

some stakeholders have said that this might be a requirement of their funding.

(c) We think that the threshold in the CCBS Act should be capable of being updated whenever an update is thought necessary, and not solely after an update has occurred in company law.

(3) We do not propose to reduce the registrar's current powers to insist upon an audit. We think that this is a valuable supervisory power, especially with community benefit societies whose assets must be applied for the benefit of the community. We note that the Charity Commission can likewise insist upon an audit for a charity.

7.200 It may be that a society is regulated, not just by the CCBS Act, but also by other legislation which provides additional auditing requirements, for example those relating to public interest entities. If so, a society will still need to comply with that additional legislation. The CCBS Act audit requirements will provide the baseline for co-operatives and community benefit societies. We do not intend it to displace additional requirements in other specialist contexts.

Consultation Question 67.

7.201 We provisionally propose that the CCBS Act should provide the following regime for society audits.

(1) Any person appointed to audit the accounts should be a qualified auditor.

(2) A society should be able to opt out of the duty to audit accounts when the society is below a certain size.

(a) There should be a single threshold (above which a society cannot opt out of the requirement to audit).

(b) That threshold should be both that turnover is not in excess of £10.2m and assets are not in excess of £5.1m.

(c) That threshold should be capable of revision by statutory instrument.

(3) The registrar should continue to be able to insist upon an audit.

Do you agree?

Reporting on objectives

7.202 Should co-operatives and community benefit societies report on how their activities pursue their objectives?

7.203 Charities are required to make such a report,[659] as are community interest companies.[660] Societies who complete the FCA's annual return AR30 form are also asked to do this.[661] Some stakeholders are content with the current practice, saying that it is good practice for societies to remind themselves of their objectives.

7.204 On community benefit societies, some stakeholders say that such societies should report on their objectives, like other social enterprises. After all, they say, such societies are supposed to be acting for the wider benefit of the community. Consistency of approach, they say, increases transparency and understanding. We add, if societies are also charities, they will anyway have to report on how their activities pursue their objectives.

7.205 On co-operatives, some stakeholders say that co-operatives are businesses and should not have to report on their objectives. After all, they say, companies do not have to produce such a report. They say that co-operatives operate for the benefit of their members, and those members can control what reports they want to receive. In contrast, other stakeholders say that co-operatives should also report on their objectives – and even show how their activities align with each of the co-operative principles.

7.206 The question is whether the current practice of reporting on objectives should be required by legislation. We see arguments on both sides, and potentially differing arguments for co-operatives and community benefit societies which could lead to different outcomes for each. We have not reached a view. We seek the views of consultees.

Consultation Question 68.

7.207 Do you think that co-operatives should be required by legislation to report on how their activities pursue their objectives?

7.208 Do you think that community benefit societies should be required by legislation to report on how their activities pursue their objectives?

Accounting year

7.209 One stakeholder has suggested that a society should be able to choose its accounting year.

7.210 Currently, the CCBS Act provides different default accounting years depending on whether a society is registered before[662] or after[663] 12 January 2012. We agree that

659 Charities Act 2011, s 162.

660 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 34; Community Interest Company Regulations 2005 No 1788, r 26.

661 AR30, section 7.

662 CCBS Act, s 78.

663 CCBS Act, s 77.

this difference in approach seems unnecessary. Nevertheless, in both cases a society can notify the FCA to alter its accounting date.[664]

7.211 However, under section 390 of the Companies Act 2006, a company's financial year can end up to seven days later or earlier than the previous year. For example, if a company's financial year ends on the first Saturday of January, the calendar date will move year on year. Section 390 gives the company flexibility, when filing its statutory accounts, to reflect that movement.

7.212 The CCBS Act has no equivalent to section 390. Instead, the year of account ends on the last day of the month in which the anniversary of the society's registration falls.[665] The year of account can be shortened – but it can only be extended once every five years.[666] We seek the views of consultees as to whether further flexibility is needed here.

Consultation Question 69.

7.213 Do you think that the CCBS Act should allow a society's financial year to end up to seven days earlier or later than the previous year (as with company law)?

Displaying balance sheet

7.214 Under section 81 of the CCBS Act, a registered society must, at all times, display a copy of its latest balance sheet in a conspicuous position at its registered office. One stakeholder has suggested this provision be repealed.

7.215 We question the utility of section 81. All the more so, for example, with community benefit societies which might be run out of a private residence. We note that, under the CCBS Act, there is already a duty to provide an annual return on demand free of charge.[667] Also, annual returns are available on the Mutuals Public Register. We question whether a paper display in an office is useful. Accordingly, we make the following provisional proposal.

Consultation Question 70.

7.216 We provisionally propose that section 81 of the CCBS Act be repealed (to remove the duty to display a balance sheet at a society's registered office). Do you agree?

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664 CCBS Act, ss 77(5) and 78(4). The FCA Guide does acknowledge the ability of societies to change their accounting date: § 8.5.

665 CCBS Act, s 77(4).

666 CCBS Act, ss 77(5) to (7).

667 CCBS Act, s 90.

EXECUTING DOCUMENTS

Signatories

7.217 In England and Wales, under the CCBS Act, a society executes a document by affixing its common seal, or if signed by two authorised signatories.[668] This includes deeds.[669] (In Scotland, the Requirements of Writing (Scotland) Act 1995 apply.[670] That statute is beyond the scope of this review.)

7.218 In comparison, under the Companies Act 2006, a document can be executed: by affixing the common seal; or by two authorised signatures; or by one authorised signatory attested by a witness.[671] This also applies to deeds.[672]

7.219 Some stakeholders are in favour of aligning society law with company law by allowing for one authorised signatory. Some stakeholders think it preferable to require more signatories rather than fewer, to prevent fraud.

7.220 We see no particular reason why society law should be stricter in this respect than company law. We think that it should be possible for a society to execute a document by one authorised signatory attested by a witness. But we also think that a society should be able to set a higher threshold in its rules, for example if the society wishes to require the signatures of two officers.

Consultation Question 71.

7.221 We provisionally propose that, subject to its rules, a society should additionally be able to execute a document by one authorised signatory attested by a witness. Do you agree?

Appointing attorneys

7.222 In company law, by instrument executed as a deed, a company may empower a person, either generally or in respect of specified matters, as its attorney to execute deeds or other documents on behalf of the company.[673]

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668 CCBS Act, s 53.

669 CCBS Act, s 53(4). A deed is a document which is executed with a high degree of formality, and by which an interest, a right, or property passes or is confirmed, or an obligation binding on some person is created or confirmed. We discuss deeds and their formality requirements in detail in Electronic Execution of Documents (2019) Law Com No 386, Ch 5, https://lawcom.gov.uk/project/electronic-execution-of-documents/.

670 CCBS Act, s 55.

671 Companies Act 2006, s 44.

672 Companies Act 2006, s 46.

673 Companies Act 2006, s 47.

7.223 Some stakeholders say that it would be useful for societies to have this power. Some stakeholders say that the appointment of an attorney should only be possible when the appointing document is signed by more than one officer.

7.224 Again, we see no particular reason why society law should be stricter here than company law. We think that it should be possible for a society to appoint an attorney to execute documents. We also think that a society should be able, through its rules, to lay down stricter requirements about when an attorney can be appointed.

Consultation Question 72.

7.225 We provisionally propose that, subject to its rules, a society should be able to appoint, by deed, an attorney to execute documents on its behalf. Do you agree?

NAMES

Protected names

7.226 Some stakeholders suggest that the following words should be protected: co-operative, cooperative, co-op, and coop. They say that these words should only be used by societies which are registered under the CCBS Act. Similarly, some stakeholders say that the phrase "community benefit society" should also be available only to those societies registered as such under the CCBS Act. PECOL says that words like "cooperative" and "coop" should not be included in the name of entities not formed and managed as co-operatives in accordance with co-operative law and universally recognised co-operative values and principles.[674]

7.227 In contrast, some stakeholders say that a company should also be able to call itself a co-operative if it operates on co-operative principles. Some say that they apply the co-operative badge to other institutions within their group to communicate branding or ethos or funding. Some say that foreign co-operatives might earn the right to use that label under foreign legislation with different definitions, and that it would be improper to deny them that label when trading in the UK.

7.228 Currently, a company seeking registration,[675] and a person carrying on business in the UK, needs approval from the Secretary of State for a name which includes "sensitive" words.[676] Those controlled words are designated by regulations (which we will refer to as the Sensitive Words Regulations).[677] "Co-operative" (but not cooperative, co-op, or coop) is a sensitive word.[678] Had that word been marked in the Sensitive Words Regulations with an asterisk, it would have included the "grammatically mutated"

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674 PECOL, r 1.1(4).

675 Companies Act 2006, s 55.

676 Companies Act 2006, s 1194.

677 Company, Limited Liability Partnership and Business Names (Sensitive Words and Expressions) Regulations 2014 (SI 2014 No 3140).

678 Sensitive Words Regulations, sch 1.

forms of that word.[679] In our view, that would probably have included cooperative, co-op and coop but these are not sensitive words in the Sensitive Words Regulations as drafted. "Society" is also listed as a sensitive word.[680]

7.229 Permission for approval to use a sensitive word is sought via Companies House. Their guidance on obtaining approval[681] says that "co-operative society",[682] and "community benefit society",[683] can only be used by societies registered under the CCBS Act. The guidance also states that "co-operative" (without "society") can be used in a company or business name if, in broad terms, the business is carried on compatibly with the co-operative principles.[684]

7.230 Under the CCBS Act, the registrar can refuse to register a society with a name which in its opinion is "undesirable".[685] The FCA says that it would be undesirable to use a name which gives an incorrect impression of the firm's legal form.[686] We would agree.

7.231 The FCA also says that use of certain words would be undesirable without "permission".[687] It lists those words in the FCA Guide, Appendix 1. This includes the word "co-operative". The FCA says that this restriction applies equally to the words cooperative, co-op and coop.[688]

7.232 On the one hand, the list of sensitive words in Appendix 1 of the FCA Guide seems to be a list of the FCA's own making. It is not a list created by statutory instrument. HM Treasury have the power to make regulations to apply company law rules on names to societies,[689] but this does not appear to have been done.[690]

7.233 On the other hand, the contents of the list in Appendix 1 of the FCA Guide coincides with the list of sensitive words in the Sensitive Words Regulations. Although the latter do not include the "grammatically mutated" forms of the word "co-operative", we think it reasonable and sensible of the FCA to include those forms as equally worthy of scrutiny. After all, "co-operative" and "co-op", for example, might be seen as interchangeable to very many people.

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679 Sensitive Words Regulations, r 3(c).

680 Sensitive Words Regulations, sch 1.

681 Companies House, Guidance: Incorporation and names (Apr 2022) § 7 and § 9. https://www.gov.uk/government/publications/incorporation-and-names.

682 Companies House, Guidance: Incorporation and names (Apr 2022), Annex A, para 37.

683 Companies House, Guidance: Incorporation and names (Apr 2022), Annex C, para 10.

684 Companies House, Guidance: Incorporation and names (Apr 2022), Annex A, para 36.

685 CCBS Act, s 10(1).

686 FCA Guide, para 3.8.2(5).

687 FCA Guide, paras 3.8.2(7) and 3.8.3.

688 FCA Guide, para App 1.1.

689 CCBS Act, s 135(2)(b).

690 CCBS Handbook, p 98.

7.234 On the use of the word "co-operative", the FCA Guide says this:[691]

> You can use this expression if you are a bona fide co-operative society. You cannot use this expression if you are a community benefit society … unless the use of the word describes the business of the society, rather than the society itself e.g. [Place name] Co-operative Development Centre Limited.

7.235 "Community benefit society" does not appear in Appendix 1 of the FCA Guide.

7.236 Overall, we note that this scheme is not as easy to navigate as might be desired. Nevertheless, any company or business calling itself a co-operative society, or a community benefit society, will be refused permission to use that name by Companies House unless registered under the CCBS Act. The FCA will not register a society with the words co-operative, cooperative, co-op or coop unless it is indeed a co-operative, or a community benefit society which seeks to develop co-operatives. However, a company or business using the plain word "co-operative" will be approved by Companies House if the business is run on co-operative principles.

7.237 In our view, that scheme is sufficient as far as it goes. However, we think that the mutated forms of cooperative, co-op and coop should be added to the list of sensitive words. After all, the law already recognises co-operative as a sensitive word, so it should for consistency recognise its variant spellings and abbreviations. All this would help protect the co-operative identity.

Consultation Question 73.

7.238 We provisionally propose that "cooperative", "co-op" and "coop" should be included alongside "co-operative" on the list of sensitive (protected) business names. Do you agree?

Plaques

7.239 Currently, a society must ensure that its registered name appears in a conspicuous position outside its registered office and every place where it carries on business.[692] Failure to comply can incur criminal liability.[693]

7.240 Some stakeholders have said that this is not appropriate, for example when a community benefit society is run for the time being out of the private residence of one member or another. Other stakeholders say that this requirement is rarely adhered to and never enforced.

7.241 We note that societies are anyway required to put their registered name on all notices, business correspondence and documentation, and websites.[694] We think that that

691 FCA Guide, app 1.

692 CCBS Act, s 11(1).

693 CCBS Act, s 127.

694 CCBS Act, s 11(2).

should be enough. We are not currently persuaded that there is further need for a plaque outside a building, especially a home. Nor do we think it appropriate to criminalise any failure to put up a plaque when non-compliance is seemingly so widespread and without consequence – in other words, when the practice is perhaps moribund.

Consultation Question 74.

7.242 We provisionally propose that the requirement to display a society's registered name outside every place where it carries on business be repealed. Do you agree?

ONLINE MEETINGS

7.243 Currently, the rules of a society must make provision for the method of holding meetings, and the scale and right of voting.[695] The CCBS Act also prescribes voting thresholds for special resolutions for: ratifying acts done by committee members beyond their capacity;[696] amalgamation with or transfer of engagements to other societies;[697] conversion into a company;[698] and dissolution.[699] Those provisions in the CCBS Act refer to "voting in person" or by proxy.[700]

7.244 Some stakeholders say that it should be possible to hold meetings online. Some are surprised that this is not already possible. Some say that it should be a matter for society rules.

7.245 In our view, the lockdowns during Covid-19 showed the importance of adapting to circumstances through the use of technology. Virtual and hybrid meetings can be convenient, and are increasingly popular. We think that it should be possible for meetings to be held virtually, whether as a hybrid meeting or fully online.

7.246 The rules of a society could already provide for – or preclude – online meetings. There is nothing in the CCBS Act which would seem to prevent that in general. But where the CCBS Act prescribes meeting and voting arrangements in specific circumstances, we think that it should be possible to hold those meetings virtually too.

7.247 More generally, it seems to us that "voting in person" could at least arguably be read as including voting while present either in the same physical meeting room or in the same virtual meeting room, and this is reflected in some authorities.[701] Other

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695 CCBS Act, s 14.

696 CCBS Act, s 43(5).

697 CCBS Act, s 111.

698 CCBS Act, s 113.

699 CCBS Act, ss 119 and 120.

700 CCBS Act, ss 44(3)(b), 111(3)(b), 113(3)(b), and 120(3)(b).

701 CCBS Handbook, pp 121 to 122; *Boyle and Bird's Company Law* (10th ed, 2019), para 13.11. Both put reliance upon *Byng v London Life Assurance Ltd* [1990] Ch 170 (CA).

authorities suggest that "voting in person" cannot be online.[702] To put the matter beyond doubt, we think that statute should expressly permit virtual or hybrid meetings.

Consultation Question 75.

7.248 We provisionally propose that, subject to the rules of a society, the CCBS Act should expressly allow meetings to be virtual or hybrid. Do you agree?

CHANGES TO SOCIETY RULES

7.249 One stakeholder has questioned whether the method of changing the rules of a society needs modernisation.

7.250 The CCBS Act stipulates that the rules of a society must themselves provide how to alter the rules.[703] In our view, this provides societies with full flexibility.

7.251 To be valid, any amendment must be registered with the FCA. This requires giving the FCA two copies of the amendments, signed by the society's secretary, and also signed by other members, two of them if all members are societies themselves, otherwise three of them.[704] This aligns with the requirement that a society must have at least two members if both are societies, or otherwise at least three members.[705] Application for initial registration similarly requires such signatures.[706]

7.252 There are additional requirements for regulated providers of social housing, and for Scottish charities.[707] A society can appeal if the FCA refuses to register an amendment.[708]

7.253 In our view, since a society must lodge its rules with the FCA when first registering,[709] it is appropriate that the society lodge any subsequent changes to its rules.

7.254 However, we do note one discrepancy, as follows. When registering, a society must send the FCA two copies of its rules, or only one copy if the application is made by electronic submission.[710] Yet with amendment, it must always be two copies.[711] We think that, for consistency, the rule for initial registration should apply to subsequent

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[702] Companies Act 2006, s 360A; *R v Secretary of State for Housing* [2021] EWHC 1093 (Admin), [2022] 1 All ER 1058.

[703] CCBS Act, s 14.

[704] CCBS Act, s 16(2).

[705] CCBS Act, s 2(2)(b).

[706] CCBS Act, s 3(1).

[707] FCA Guide, paras 8.6.7 and 8.6.8; CCBS Handbook, p 101.

[708] CCBS Act, s 17.

[709] CCBS Act, s 3(1)(b).

[710] CCBS Act, s 3(1)(b).

[711] CCBS Act, s 16(2).

amendment. Beyond that, we do not currently think that any further amendment to the CCBS Act is needed.

Consultation Question 76.

7.255 We provisionally propose that, when a society notifies the FCA of an amendment to the society's rules, the society need send only one copy of the amendment if this is sent by electronic means. Do you agree?

INDIVISIBLE RESERVES

7.256 A trading surplus which is not distributed to members as a dividend might instead be allocated to the indivisible reserve. This is held as common property for the benefit of the society itself (rather than being divisible or distributable).[712] The indivisible reserve can be further protected from distribution to members upon dissolution through society rules (which might be entrenched) or an asset lock.

7.257 Some stakeholders have suggested that indivisible reserves receive statutory acknowledgment. We question whether there is really any doubt about the fact that a society can have an indivisible reserve. The indivisible reserve is mentioned in the Third Co-operative Principle, as acknowledged by the FCA.[713] On the other hand, to allay any residual uncertainty, it might be appropriate for the CCBS Act to state explicitly that a society's rules can make provision for indivisible reserves. This might even provide a "hook" for policy initiatives, such as favourable tax treatment for indivisible reserves (for example, as found in Italy).[714]

Consultation Question 77.

7.258 Do you think that the CCBS Act should explicitly provide that society rules may provide for an indivisible reserve?

BANKING AND CREDIT UNIONS

Banking

7.259 Do the rules for society banking need reform? Banking was an excluded activity in the (first) Industrial and Provident Societies Act 1852.[715] The subsequent Industrial and Provident Societies Act 1876 allowed societies to carry on the business of banking if they had no withdrawable share capital.

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712 ICA Guide to the Co-operative Principles, p 33.

713 FCA Guide, para 4.3.3.

714 Adderley, ch 8; PECOL, p 8.

715 For an historical overview of societies' legislation, see CCBS Handbook, Ch 2.

7.260 Current rules on society banking are set out in sections 67 to 70 of the CCBS Act.[716] A registered society which has any withdrawable share capital must not carry on the business of banking.[717] This also means taking no more than £400 per depositor.[718] A society which carries on banking must display a statement in its office.[719] That statement, rewritten every six months, must include details about the capital of the society, and its assets and liabilities.[720]

7.261 Some stakeholders say that these provisions are out of date compared to modern banking requirements. They say that it is practically impossible for a society to meet the modern capital requirements of banking with the equity tools currently available.

7.262 We do not know what demand there is for societies to carry on the business of banking. We note that there are other forms of financial mutual like credit unions, building societies, and friendly societies,[721] all of which have their own legislation.[722] Separate legislation for society banking might be necessary, but it would be beyond the scope of this review. Nevertheless, this review provides a fact-finding opportunity to assess what demand there is for a review of society banking.

7.263 Further, any co-operative society which currently carries on the business of banking will be registered under the CCBS Act. Changes to the CCBS Act will affect them, so we also ask whether there are any consequences unique to co-operative banks which we need to consider.

Consultation Question 78.

7.264 Do you think that there is a need to reform the law relating to co-operative banks? If so, what reforms do you think are needed?

7.265 Do any of the proposed changes to the CCBS Act have particular consequences for co-operative banks that we need to consider?

Credit unions

7.266 Currently, credit unions are governed by both the CCBS Act and the Credit Unions Act 1979. In comparison, in Northern Ireland, the legislation for credit unions is separate.[723] Similarly, in England and Wales, building societies have their own

716 Partially repeated in s 4 of the CCBS Act.

717 CCBS Act, s 67(1).

718 CCBS Act, s 67(2).

719 CCBS Act, s 69.

720 CCBS Act, s 70.

721 The Law Commission is also reviewing the law of friendly societies: https://lawcom.gov.uk/project/friendly-societies/.

722 Credit Unions Act 1979 (see CCBS Handbook ch 13); Building Societies Act 1986; Friendly Societies Act 1992.

723 The Credit Unions (Northern Ireland) Order 1985 (SI 1985 No 1205 (NI 12)).

separate legislation.[724] Some stakeholders have suggested that credit union legislation be separated entirely from the CCBS Act. This would be beyond the scope of the current review, but we take the opportunity to canvass the opinion of consultees as to whether a review of credit union law is needed.

7.267 Further, credit unions registered under the CCBS Act will of course be affected by the proposed changes to the CCBS Act. In that regard, we also ask whether there are any consequences unique to credit unions which we need to consider.

Consultation Question 79.

7.268 Do you think that there is a need to reform the law relating to credit unions? If so, what reforms do you think are needed?

7.269 Do any of the proposed changes to the CCBS Act have particular consequences for credit unions that we need to consider?

[724] Building Societies Act 1986.

Chapter 8: Other stakeholder suggestions

8.1 We have so far received many suggestions for reform from stakeholders. We have considered them all. This chapter sets out those suggestions where we have provisionally concluded not to propose any reform. Rather than asking about each individual point, we ask consultees whether they think any of these suggestions do require reform and should therefore be revisited.

Consultation Question 80.

8.2 As regards the topics set out in Chapter 8, we have provisionally concluded against reform. Do you think that any of those topics needs revisiting, and if so why?

IDENTITY OF THE REGISTRAR

8.3 Some stakeholders have suggested that the registrar for societies should be moved to Companies House. Some have suggested that a new registrar be created, perhaps by combining with the Office of the Regulator of Community Interest Companies. Some complain that the FCA brings the depth of scrutiny associated with financial regulation to what should largely be an administrative registration of (mainly non-financial) societies. In contrast, some stakeholders wish to retain the FCA as registrar.

8.4 In our view, the efficacy of a registrar will depend on various factors including its personnel and resourcing, and its legal framework. There is no reason to assume that a different registrar will necessarily and always have better personnel or resources. Resourcing is a matter for Government priorities rather than legislation. We have been impressed by the personnel currently at the FCA and the sincerity of their commitment to their work. Our role is to review the legal framework that will guide the work of any registrar; the right legal framework will assist both the registrar (whoever they are) and societies operating within it.

8.5 Some stakeholders have suggested that responsibility for societies be moved from HM Treasury to the department with responsibility for companies and other organisational forms – currently the Department for Business and Trade (Department for Business).

8.6 Which Government department "owns" any piece of legislation is a matter for Government, and is not specified in the legislation itself. Government departments can and do change shape. This is not a matter for the Law Commission. Nevertheless, stakeholders have made representations to us which we think are sensible and forceful, and we record them here so that Government can give them due consideration.

8.7 Stakeholders say that business policies developed by Government tend to overlook societies because societies do not fall within the remit of the Department for Business.

They say that, just because some societies will be financially regulated – which is part of the core business of HM Treasury – it does not follow that all responsibility for societies need fall within HM Treasury. For example, many companies require financial regulation, but they are still registered at Companies House, and policy for them is still developed by the Department for Business.

8.8 Some stakeholders say that if societies are to reach their full potential, they need to be given due consideration when business policy is developed. Societies need to be mainstreamed, they say, to optimise their contribution to the economy and society.

8.9 Some stakeholders say that it is not simply in the development of general policy that societies can be forgotten. Rather, this can go all the way down to the details of everyday practicalities. Here are some examples which stakeholders have shared with us. Employee Ownership Trusts are granted tax breaks, so why not worker co-operatives? Similarly, they say, community-owned sports clubs should have the same tax breaks as amateur sports clubs. The right to manage residential properties requires a company limited by guarantee, they say, but why not also a co-operative? The Making Tax Digital initiative from HMRC is designed for companies, they say, and is not available for societies. Similarly, they say, Single Account Filing is available at Companies House and HMRC, without there being an equivalent for societies.

8.10 We do not comment on these individual examples. However, societies are businesses by definition. We fully endorse the simple proposition that if societies are to achieve their potential, they need to be given due consideration in the development of business policy.

PRINCIPAL REGULATOR FOR CHARITABLE COMMUNITY BENEFIT SOCIETIES

8.11 Should the Office of the Regulator of Community Interest Companies be designated as the principal regulator for charitable community benefit societies?

8.12 We discuss charitable community benefit societies in Chapter 4, where we provisionally propose that they cease to be exempt charities. This means that they could register with the Charity Commission – although we noted that it might be preferable for the Financial Conduct Authority (FCA) to be designated the lead regulator.

8.13 In our view, it would be a less attractive option to keep charitable community benefit societies as exempt charities, and designate the Office of the Regulator of Community Interest Companies as the principal regulator. The Regulator of Community Interest Companies is no doubt an expert in community interest companies, but otherwise lacks the general expertise of the Charity Commission in charity law, or the specific expertise of the FCA in community benefit societies.

DEFINITION OF CHARITABLE COMMUNITY BENEFIT SOCIETY

8.14 Should the Co-operative and Community Benefit Societies Act 2014 (CCBS Act) list what requirements a community benefit society must meet in order to be charitable?

8.15 Under section 149 of the CCBS Act, a "charitable registered society" is defined as a registered society which is a charity, and charity "has the meaning given by section 1(1) of the Charities Act 2011".

8.16 In other words, the CCBS Act confirms that charitable status remains governed by charity law, even as regards societies, and that the CCBS Act does not change that.

8.17 The CCBS Act sets out what rules societies must comply with to be registered, and charity law will set out additional rules which societies must comply with to achieve charitable status. Society law may be more permissive than charity law. For example, an asset-locked society might be able, under society law, to transfer its assets to another asset-locked organisation, but charity law might only allow transfer to another charity. A charitable society must comply with both society law and charity law – it cannot simply pick the lowest common denominator.

8.18 Otherwise, we think that societies should be governed by charity law in the same way as other forms of organisation. We do not currently propose that the CCBS Act should contain charity law rules bespoke only to community benefit societies.

BUYING BACK SHARES

8.19 The CCBS Act does not say anything about the ability of societies to buy back their shares, although of course where shares are withdrawable at the option of the society then this is effectively a buy-back provision.

8.20 Some stakeholders have said that societies should be able to issue redeemable shares. Some stakeholders have said that societies should be able to buy back their shares. For example, they say, a society should be able to buy back shares when there is no further need for the capital, because the inability to buy back shares and return the capital amounts to an (unchosen) asset lock.

8.21 The Community Shares Handbook explains that too many shares can be undesirable when there is interest to pay on shares. Some societies might want to reduce their shares as the assets of the society depreciate. For example, says the Handbook, this is common in the community energy sector.[725]

8.22 It has been suggested that, without statutory permission, it would not be possible for societies to buy back shares, by analogy to a common law rule which was developed in the context of company shares.[726] That common law rule is now codified in the Companies Act 2006,[727] but with major derogations in terms of redeemable shares and a company buying its own shares (we discussed this in detail in Chapter 4).

8.23 Ultimately, we question what need there is for societies to be able to buy back their shares as a separate mechanism. While company law has developed redeemable shares, and the concept of buying back shares, society law has developed withdrawable shares, even withdrawable at the insistence of the society. Society

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725 Community Shares Handbook, para 2.3.

726 *Trevor v Whitworth* (1887) LR 12 App Cas 409.

727 Companies Act 2006, s 658.

shares can also be written down to reflect depreciation in the value of the society's assets. We are not yet persuaded that there is any gap for which the ability to buy back shares as a separate mechanism is necessary.

8.24 For example, if a society wished to buy back non-withdrawable shares, it might instead change its rules to render them withdrawable at the behest of the society. This would engage the rules for changing class rights, discussed above. We think that that would be appropriate, and need be no more burdensome than the equivalent company law rules for reducing share capital.

NUMBER OF OFFICERS

8.25 Should the CCBS Act prescribe a minimum number of officers, and a minimum number who are people (rather than corporations)?

8.26 For example, a private company must have at least one director,[728] and a public company must have at least two.[729] At least one director must be a natural person (human).[730] There is no comparable requirement in the CCBS Act.

8.27 Some model society rules provide for a minimum of three directors to form a board of directors.[731] Other rules provide for between five and twelve directors.[732] Some model rules state that the society is governed by the general meeting, and so only appoint a secretary.[733] The CCBS Handbook says that, with some small societies, everyone might play a role, with the result that such societies are run closer in form to a partnership.[734] Some secondary co-operatives might have members who are only corporations (no human members).

8.28 Because of the variety of ways in which societies are organised, we would be hesitant to lay down a fixed rule about officer numbers. We are not aware of any problem in practice which needs addressing here, and so we do not currently propose any reform.

CHALLENGING GUIDANCE ISSUED BY THE REGISTRAR

8.29 Should it be possible to bring a legal challenge against any guidance which the registrar publishes?

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728 Companies Act 2006, s 154(1).

729 Companies Act 2006, s 154(2).

730 Companies Act 2006, s 155.

731 Co-operatives UK Multi-stakeholder Co-operative Model Rules, Co-operative Consortium Model Rules, Worker Co-operative Model Rules, Community Benefit Society Model Rules.

732 Co-operatives UK and Confederation of Co-operative Housing Fully Mutual Housing Co-op Model Rules, Tenant Management Housing Co-op Model Rules; Co-operatives UK and Confederation of Co-operative Housing and Wales Co-operative Centre Mutual Home Ownership Society Model Rules.

733 Co-operatives UK and Confederation of Co-operative Housing and Wales Co-operative Centre Co-operative (General Meeting Governed) Model Rules.

734 CCBS Handbook, p 140.

8.30 In our view, any guidance issued by the registrar might be challenged through judicial review on usual public law principles. However, we do not currently propose any alternative process of challenge through the CCBS Act. We would not wish to discourage the registrar from issuing guidance. If any guidance is followed to produce a decision, there may be a right to appeal that decision (as we discuss in Chapter 7). Overall, we think this scheme is strikes the right balance between protecting societies without unduly constraining the registrar.

NOTICE OF CANCELLATION

8.31 In Chapter 7, we provisionally proposed a fixed notice period of two months before cancellation of a society's registration. Should the CCBS Act specify what is to happen at the end of that notice period?

8.32 One stakeholder says that they would welcome clarity over whether, at the end of the notice period, the society's registration must be cancelled, or whether the FCA can then issue directions to wind up the society, or whether any further period before cancellation must be covered by a new notice of cancellation.

8.33 In our view, this does not call for legislation. The FCA can simply write to a society giving it notice that it intends to cancel the society's registration. The letter could state that the society has two months in which to appeal, and that after those two months, and unless the society has appealed, the registrar might give directions to wind up the society, or might cancel the society's registration. We think that the CCBS Act merely requires the registrar to give two months' notice of cancellation. The CCBS Act does not otherwise require the registrar to commit to a definitive time period thereafter during which it will issue directions or cancel a registration. We think that this flexibility is appropriate.

RESTORING TO THE REGISTER

8.34 Should it be possible to restore to the register a society's whose registration has been cancelled?

8.35 For comparison, the position in company law is as follows. A company which the registrar believes is not carrying on business can be struck off the register.[735] So too a company which has been wound up, or where no liquidator is acting,[736] or where the company has been registered on a false basis.[737] A company can also ask to be struck off.[738] Upon publication in the Gazette that the company has been struck off, it

[735] Companies Act 2006, s 1000.

[736] Companies Act 2006, s 1001.

[737] Companies Act 2006, s 1002A.

[738] Companies Act 2006, s 1003.

is dissolved.[739] Upon dissolution, all company property goes bona vacantia to the Crown,[740] unless disclaimed by the Crown.[741]

8.36 A company which has been struck off other than at its request can apply to the registrar for administrative restoration to the register.[742] It must show that it was a going concern before being struck off;[743] it must update its paperwork and pay its fines.[744] The application must be served upon the Government Legal Department and the Crown must consent,[745] and return any property or its proceeds of sale.[746] An application can also be made to court to restore a company to the register.[747]

8.37 Upon restoration, it is as if the company had never been struck off.[748] The court can give directions to place the company and others in the same position as they were in prior to the striking off.[749]

8.38 A company whose name has been struck off the register still exists and so can be wound up by the court.[750] Once the company has been dissolved, it no longer exists, so it must be restored to the register (and existence) before it can be wound up.[751]

8.39 The position under the CCBS Act is as follows. A society cannot be restored to the register.[752] If a society wishes to resume its business, it can apply to re-register anew. This will result in a different registered name and number.[753]

8.40 Otherwise, HM Treasury is already empowered by the CCBS Act to make regulations to apply to societies the company law on restoration to the register.[754] This power has not been used.

8.41 There are three difficulties in applying company law to societies in this respect, as follows. First, when a company is struck off, it continues to exist as a company. Restoring the company to the register at this point is just an administrative exercise. In

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739 Companies Act 2006, ss 1000(6), 1001(4), 1002A(5), 1003(5).

740 Companies Act 2006, s 1012.

741 Companies Act 2006, ss 1013, 1014.

742 Companies Act 2006, s 1024.

743 Companies Act 2006, s 1025(2).

744 Companies Act 2006, ss 1025(5) and (5A).

745 Companies Act 2006, s 1025(3).

746 Companies Act 2006, s 1034. Property not otherwise dealt with might automatically re-vest: *Re C W Dixon Ltd* [1947] Ch 251.

747 Companies Act 2006, ss 1029, 1031.

748 Companies Act 2006, ss 1028(1), 1032(1).

749 Companies Act 2006, ss 1028(3) and (4), 1032(3).

750 Companies Act 2006, ss 1000(7)(b), 1001(5)(b), 1002A(6)(b), 1003(6)(b).

751 *Re Cambridge Coffee Room Association Ltd* [1952] 1 All ER 112.

752 FCA Guide, paras 8.17.1 and 9.6.3.

753 FCA Guide, para 8.17.10.

754 CCBS Act, s 135.

contrast, when a society's registration is cancelled, it ceases to be a society. Most likely, it changes form to a partnership or unincorporated association.

8.42 Second, when a company is struck off, it is usually soon after dissolved, at which point it ceases to exist. Restoring a company to the register at this point means taking something non-existent and making it exist again. In contrast, because a society continues as a partnership or unincorporated association, restoring it to the register would involve changing its form again. However, a partnership or unincorporated association cannot simply "switch" to being a society. Ordinarily, the process would involve: setting up the society; transferring the business or assets of the partnership or association to the society; then dissolving the partnership or association. We question whether the consents involved in that process can be substituted simply by the administrative task of restoring the society's name to the register. Similarly, even where the CCBS Act provides for conversion of form, for example, from a society to a company or vice versa, that still requires voting (a special resolution).

8.43 Third, when a company is dissolved, its assets go to the Crown, who can then return them. In contrast, with a co-operative, for example, unless its rules provide otherwise, assets would be distributed upon dissolution among the members.[755] It could be difficult in some cases to require many members to return their distributed share. More generally, we think that it is probably wrong in principle to require people compulsorily to revive their membership and fund the co-operative. We recall, for example, that the First Co-operative Principle provides for voluntary membership.

8.44 Ultimately, even if these difficulties could be overcome, we question whether there is any pressing need for a function of restoring a society to the register. Either an application to re-register anew can be made, if people are willing to re-animate their society. Or if the society is defunct, but its affairs need putting in order, it can be wound up, whether as a partnership,[756] or as an unincorporated members' club.[757] Otherwise, cancellation does not affect any liability previously incurred by the society, which may be enforced against the society as if cancellation had not occurred.[758]

8.45 For these reasons, we do not currently propose any reform to the CCBS Act such that a society can be restored to the register after its registration has been cancelled.

CONVERSION FROM A COMMUNITY INTEREST COMPANY

8.46 Should community interest companies should be able to convert to community benefit societies?

8.47 By section 115 of the CCBS Act, a company registered under the Companies Acts can convert to a community benefit society. "Companies Acts" includes the 2004

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755 *Boyle v Collins* [2004] EWHC 271, [2004] 2 BCLC 471, [2004] All ER (D) 287 (Feb); *Re Finch* [2018] EWHC 329 (Ch), [2018] BCC 366; *Qureshi v Association of Conservative Clubs Ltd* [2019] EWHC 1165 (Ch), [2019] All ER (D) 68 (May).

756 The Insolvent Partnerships Order 1994 (SI 1994 No 2421).

757 Halsbury's Law, *Clubs*, vol 13 (2021) para 291, citing *Re Lead Co's Workmen's Fund Society* [1904] 2 Ch 196.

758 CCBS Act, s 6(7).

legislation which provides for community interest companies.[759] However, the 2004 legislation itself provides that a community interest company cannot convert to a community benefit society unless regulations provide otherwise.[760] Subsequent regulations did indeed allow such a conversion.[761] Thus, the FCA Guide says that a community interest company can convert into a community benefit society.[762]

8.48 At any rate, there does not appear to be anything in the CCBS Act which prevents a community interest company converting into a community benefit society. Accordingly, we do not currently propose any reform of the CCBS Act here.

DISTRIBUTION ON DISSOLUTION: CO-OPERATIVES

8.49 Currently, the procedures of company law are followed when a co-operative is dissolved upon its winding up.[763] Thereby, any surplus assets of the co-operative will be distributed among members according to their "rights and interests" in the society.[764] If the rules of the co-operative prescribe what is to happen, then distribution will be according to those rules. If the rules do not so prescribe, then the case law suggests that the default is to distribute assets in proportion to the shareholdings of members.[765]

8.50 One stakeholder has suggested that, upon solvent dissolution, surplus co-operative assets should be distributed among members in proportion to their transactions with the co-operative over the previous five years. Another has suggested that no surplus should ever be distributed to members; instead it should be given to another co-operative.

8.51 Model rules tend to address dissolution. For example, Co-operatives UK Multi-Stakeholder Co-operative Model Rules give an option between common ownership, so that surplus assets go to another co-operative, or co-ownership, where surplus assets are distributed among members "either equally or in accordance with some other equitable formula which recognises the relative contribution made" by members over the previous six years.

8.52 Thus, distribution of surplus assets upon solvent dissolution can be and is often addressed in the rules of a co-operative. We do not think that there is an obvious "best" solution that should be a default rule in legislation. We are not persuaded that there is any need for statutory reform here to the long-stop rules of insolvency law.

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759 CCBS Act, s 149; Companies Act 2006, s 2(1)(b).

760 Companies (Audit, Investigations and Community Enterprise) Act 2004, s 56.

761 The Community Interest Company (Amendment) Regulations 2009 (SI 2009 No 1942), r 5.

762 FCA Guide, § 3.7.

763 CCBS Act, s 123.

764 Insolvency Act, s 107.

765 *Re Merchant Navy Supply Association Ltd* [1947] 1 All ER 894 (Ch); *Boyle v Collins* [2004] EWHC 271; *Re Finch* [2018] EWHC 329 (Ch), [2018] BCC 366; *Qureshi v Association of Conservative Clubs Ltd* [2019] EWHC 1165 (Ch); CCBS Handbook, pp 313 to 314.

DISTRIBUTION ON DISSOLUTION: COMMUNITY BENEFIT SOCIETIES

8.53 One stakeholder has suggested that, upon solvent dissolution, surplus assets of a community benefit society should only ever be applied to the benefit of that community.

8.54 As discussed in Chapter 4, a community benefit society cannot distribute its assets to its members. The FCA Guide says that, upon dissolution, surplus assets could be transferred to "a similar organisation with similar objects".[766] Some model rules provide that surplus assets should go to a non-profit body with at least the same restrictions on the distribution of profits and assets, as may be decided by members at the time of dissolution.[767] If a society is dissolved by an instrument of dissolution, the CCBS Act requires the instrument to specify the intended distribution or leave it to the choice of the registrar.[768]

8.55 If a community benefit society were to dissolve, there may be no other asset-locked vehicle serving that community to which the society's assets could be transferred. Overall, we think it more in keeping with the original raising of funds for community benefit that those assets do go to another public cause like a charity, even if it is serving another constituency, rather than go bona vacantia to the Crown. Accordingly, we are not yet persuaded to propose any reform here.

DISSOLUTION: NOTIFICATION TO THE REGISTRAR

8.56 Do the rules on notifying the registrar of dissolution need reform?[769]

8.57 A society may be dissolved by an instrument of dissolution.[770] The instrument of dissolution must be sent to the registrar,[771] which the registrar must register in the same way as an amendment of the society's rules.[772] The registrar must advertise the dissolution in the Gazette.[773] By default, dissolution occurs on the date of the advertisement, or if later when a certificate under section 126 is lodged with the registrar.[774]

8.58 Section 126 provides that a society must not be dissolved, and its registration must not be cancelled, until a certificate has been lodged with the registrar certifying that all property in the society has been duly transferred to the persons entitled.

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766 FCA Guide, para 5.1.13.

767 Co-operatives UK Community Benefit Society Model Rules.

768 CCBS Act, s 119(2)(d).

769 The provisions in the CCBS Act are a restatement of the previous law in the Industrial and Provident Societies Act 1965, ss 55 to 59, albeit presented differently.

770 CCBS Act, s 119.

771 CCBS Act, s 121(2).

772 CCBS Act, s 121(5).

773 CBBS Act, s 122(1).

774 CCBS Act, s 122(2).

8.59 Alternatively, a society can be dissolved on its being wound up, either in pursuance of a court order, or through a voluntary winding up.[775] Company law rules on winding up apply.[776] In a voluntary winding up, the society must send a copy of the resolution to the registrar.[777] This process is similarly subject to section 126.[778]

8.60 A society can also be dissolved following administration.[779] This only occurs where the administrator thinks that the society has no property to distribute, and notifies the registrar accordingly.[780] That notice is registered by the registrar,[781] and the society is deemed dissolved three months later.[782] This process is not subject to section 126 because there is in this instance no property to certify as properly transferred. We do not currently perceive any inconsistency here in need of reform.

DORMANT SOCIETIES

8.61 In the case of a "dormant" society, an instrument of dissolution must be approved by a special resolution.[783] A dormant society is defined as one: whose last three years of account show no transactions except fees paid to the registrar or the payment of dividends or interest; and which has notified the registrar that it is dormant.[784]

8.62 One stakeholder has questioned how a society can ever be dormant when, by definition in section 2 of the CCBS Act, it must be carrying on business.

8.63 One answer is that section 2 applies to a society "for" carrying on any business. This could be read as stipulating that the purpose of the society must be to carry on business. In which case, section 2 does not require a society to be actually carrying on business. Similarly, section 2 says that a community benefit society need only "intend" (that is, in the future) to carry on its business for the benefit of the community.

8.64 Further, a society can be cancelled when it "ceases to exist",[785] which is different from dormancy.

8.65 Further still, a society can request its cancellation by the registrar. The registrar must consider this to be appropriate.[786] The FCA requires the society to "have ceased" to

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775 CCBS Act, s 123(1).

776 CCBS Act, s 123(2).

777 CCBS Act, s 123(3).

778 CCBS Act, ss 123(5) and 126(1).

779 CCBS Act, s 125.

780 Insolvency Act 1986, s 8, and sch B1, para 84(1), applicable by virtue of the Co-operative and Community Benefit Societies and Credit Unions (Arrangements, Reconstructions, and Administration) Order 2014 (SI 2014 No 229), art 2(2).

781 Insolvency Act 1986, sch B1, para 84(3).

782 Insolvency Act 1986, sch B1, para 84(6).

783 CCBS Act, s 119(3)(b). What such a special resolution entails is set out in section 120.

784 CCBS Act, s 119(6).

785 CCBS Act, s 5(3)(c).

786 CCBS Act, s 5(2).

carry on business.[787] In other words, the society must already have stopped carrying on business.

8.66 Another answer is simply that the rules for dissolving a dormant society are merely pragmatic. If a society finds itself dormant, it may wish to dissolve, and these rules allow it to do so. Otherwise the society might have struggled to meet the rules which govern the dissolution of a society which is still a going concern.

8.67 We are not currently persuaded that there is any need for reform on this issue.

REGISTRAR POWERS OF INTERVENTION

8.68 Some stakeholders would like the registrar to intervene more in the running of societies, for example when members perceive a society to be acting less than democratically. In contrast, some stakeholders think that the registrar should have a more administrative and less interventionist role. This raises two issues: the power to intervene, and the threshold for intervention. We discussed the threshold for intervention in Chapter 7. Here we discuss powers to intervene.

8.69 Under the CCBS Act, the registrar may, on the application of at least 10 members of a society, appoint an accountant to inspect the society's books and report on them.[788] Also, on the application of 10% of members, the registrar can appoint an inspector to examine the society's affairs.[789] The registrar can also call a special meeting of the society.[790] An inspector can examine a society's officers on oath.[791] The special meeting has all the powers of a meeting called in accordance with the society's rules.[792] If those inspections or examinations reveal that a society or its officers have been failing to fulfil their duties under the CCBS Act, this might constitute a criminal offence.[793] The registrar may be able to bring a prosecution.[794]

8.70 The registrar has additional powers under the Asset Lock Regulations. Thereunder, the registrar can issue an enforcement notice requiring a community benefit society to take steps to ensure that its assets are used only for the benefit of the community.[795] It can require an officer complicit in a society's default to make restitution.[796] It can also require the officer to be removed.[797] In the meantime, the registrar can apply to the

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787 FCA Guide, para 8.17.12.

788 CCBS Act, s 105.

789 CCBS Act, s 106(1)(a).

790 CCBS Act, s 106(1)(b).

791 CCBS Act, s 107(2)(b).

792 CCBS Act, s 107(4)(a).

793 For example, see: CCBS Act, ss 127 and 128.

794 CCBS Act, s 132.

795 Asset Lock Regulations, r 9.

796 Asset Lock Regulations, r 10.

797 Asset Lock Regulations, r 11.

court for an injunction.[798] Any decision of the registrar in these regards can be appealed.[799]

8.71 We suggested above that the registrar's powers under the Asset Lock Regulations be included within the CCBS Act as generally applicable to all community benefit societies regardless of whether they choose an asset lock. We also suggested that they should be applicable to co-operatives who choose an asset lock.

8.72 Further, the registrar has some of the same powers in respect of societies as are available against companies under Part 14 of the Companies Act 1985.[800] For example, the registrar can appoint inspectors where circumstances suggest that the society is defrauding creditors, is engaged in misconduct towards its members, or is withholding information from its members.[801] A warrant can be issued to enter and search premises.[802]

8.73 We do not see it as the role of the FCA to promote societies. Otherwise there would be a potential conflict of interest between, on the one hand, registering and regulating, and on the other hand, championing the form. Similarly, we do not think it the role of the FCA to ensure that a society maximally fulfils all the ideals of a co-operative, or that any given society succeeds financially despite itself.

8.74 Overall, we do not currently think that the registrar is lacking any necessary enforcement powers. We think that the registrar has effective powers to investigate and prosecute breaches of statutory duty.

8.75 There are two further suggestions to consider. First, some stakeholders have suggested that there be a power to intervene in the running of community benefit societies to protect the interest of the community, in a role akin to that played by the Attorney General in the context of charities.

8.76 We accept that, with community benefit societies, there is unlikely to be a private individual with standing to bring a claim for any default by the society. However, the Asset Lock Regulations empower the registrar to act to protect the community's interests. We think that these powers are sufficient without the need to create a new role akin to that of the Attorney General with charities.

8.77 Second, one stakeholder has suggested that it should be for the court, not the registrar, to appoint inspectors. They say, correctly, that disputes internal to the society (for example, between the society and a member), are not to be resolved by the registrar. If the society's rules seek to appoint the registrar to resolve the dispute, then section 137(3) of the CCBS Act provides that the dispute is instead to be

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798 Asset Lock Regulations, r 15.

799 Asset Lock Regulations, r 14.

800 The Co-operative and Community Benefit Societies and Credit Unions (Investigations) Regulations (SI 2014 No 574).

801 Companies Act 1985, s 432.

802 Companies Act 1985, s 448.

resolved by the court.[803] Accordingly, says the stakeholder, complaints raised by members, which currently might trigger the appointment of an inspector, should be made to the court, not to the registrar.

8.78 We think it potentially useful for the registrar of societies to be involved in any investigations of societies, rather than by-passing the registrar to go straight to court. We are not yet persuaded that the powers of intervention should be removed from the registrar and given only to the court.

8.79 As for complaints by members, if they do not wish to engage the assistance of the registrar, they can take their own private disputes to court (or through any dispute resolution process prescribed by the society's rules, such as arbitration).

ACCOUNTING PRACTICES

8.80 Some stakeholders have said that society accounts should follow the same practices as company accounts. This is because, they say, most people are accustomed to company accounts, and so understand them. Also, most software is tailored to company accounts.

8.81 On the other hand, some stakeholders have said that company practice does not always suit societies. For example, they say, how should share interest paid into withdrawable share accounts be treated?

8.82 In our view, this is not a matter for legislation – and the CCBS Act currently makes no such provision. Accounting practices and software should be developed by professional bodies in co-operation with the sector, rather than by legislators. Such practices are liable to evolve and should not be hampered by fixed legislation.

PUBLISHING ACCOUNTS

8.83 Some stakeholders have said that the registrar should publish the accounts of a society even where a society is being investigated. They say that, where no action ends up being taken against a society, the absence of accounts is itself a stigma when dealing with others. Some suggest that societies should be able to file their accounts online directly, rather than relying on the FCA to publish them. Some have said that the accounts and the annual report should be separate, so that if there is any question over one, then at least the other can be published.

8.84 We have been told that the FCA does not delay the publication of accounts if it investigates a society, but it will not publish accounts which do not meet the statutory requirements for accounts (for example, if they are incomplete or unsigned). In other words, only compliant accounts are accounts properly so called and capable of being published.

8.85 We agree that non-compliant accounts should not be published. More generally, we think that the mechanics of how and when society accounts are published is not suited to prescription by legislation which then fixes the practice in stone.

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[803] CCBS Act, s 137(3).

CHANGING AUDITORS

8.86 Should it be possible to change auditors without calling a special general meeting?

8.87 In comparison, a company can remove an auditor at any time by ordinary resolution at a meeting.[804] The resolution requires special notice.[805] This tends to mean giving 28 days' notice.[806]

8.88 Under the CCBS Act, automatic re-appointment of an auditor can be disapplied by a vote at a general meeting.[807] Replacement of an auditor also tends to require 28 days' notice.[808]

8.89 In our view, the rules for societies do not appear to be unreasonably restrictive. What is more, audits are there for the protection of the members (as well as the public), and so it should not be too easy to change auditors without the involvement of members. We are not currently persuaded of any need for legislative reform here.

SLEEPING MEMBERS

8.90 "Sleeping members" are those who technically remain members of a society, but who have not engaged with the society at all for an extended period of time. One stakeholder has suggested that minimum numbers for quorum should refer to active members, not sleeping members. Other stakeholders say that it would complicate matters to create different classes of members.

8.91 We think that it is open to societies to audit their membership periodically to remove from membership those who are no longer active.[809] There is nothing in the CCBS Act to preclude this. Indeed, some model rules provide for it.[810] Otherwise, we are not currently persuaded that there is any need for legislation to differentiate active members or define them. We think that the rules of a society could do so, if that was thought desirable.

DISPENSING WITH MEETINGS

8.92 One stakeholder has suggested that societies should have the power to dispense with annual general meetings. In comparison, a private company is no longer under any

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804 Companies Act 2006, s 510.

805 Companies Act 2006, s 511.

806 Companies Act 2006, sch 8 and s 312.

807 CCBS Act, s 93(2).

808 CCBS Act, s 94(2).

809 CCBS Handbook, pp 111 to 112; FCA Guide, para 6.1.15(3).

810 See, for example, the section on "untraced members" in the Co-operatives UK Co-operative Consortium Model Rules.

statutory duty to call an annual general meeting,[811] although its articles may still require one.[812]

8.93 Section 14 of the CCBS Act says that the rules of a society must make provision about "the method of holding meetings, [and] the scale and right of voting".[813] It seems to us that this potentially *requires* meetings to be held, although it does not prescribe any detail about frequency, or business to be discussed.

8.94 Neither the CCBS Act nor the FCA Guide says anything further about general meetings. The CCBS Handbook suggests that a society's rules should usually,[814] and perhaps must,[815] provide for at least one annual general meeting when the accounts can be presented.

8.95 We are mindful that the Second Co-operative Principle is democratic member control. Also, our proposed definition of a society includes one vote per member. All this requires an opportunity in which to exercise democratic control and to vote. In turn, that necessitates a meeting. This is consistent with our view that the CCBS Act requires meetings.

8.96 We can see how it might be necessary to postpone meetings, or hold them in one form rather than another. But we are not persuaded that societies should be able to dispense altogether with an annual general meeting of members. We do not currently propose any reform here.

MINUTES

8.97 Should societies be required to take minutes in every meeting of its officers?

8.98 This is not currently required under the CCBS Act. In comparison, in company law, minutes of all proceedings at meetings of directors must be recorded and kept for 10 years.[816]

8.99 We think that society rules can already require its officers to take minutes of their meetings – indeed, some model rules do so.[817] Otherwise, we are reluctant to impose additional administrative burdens on all societies, when some may be small and run informally. If society officers take decisions, those can already be scrutinised at the annual general meeting, where explanations can be given.

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811 Following the repeal of s 366 of the Companies Act 1985. See *Boyle and Bird's Company Law* (10th ed, 2019) para 13.9.

812 Companies Act 2006 (Commencement No 3, Consequential Amendments, Transitional Provisions and Savings) Order 2007 (SI 2007 No 2194), sch 3, para 32.

813 CCBS Act, s 14(4).

814 CCBS Handbook, p 126.

815 CCBS Handbook, p 128.

816 Companies Act 2006, s 248.

817 For example, Co-operatives UK: Multi-Stakeholder Model Rules, and Community Benefit Society Model Rules.

MODEL RULES

8.100 Should there be statutorily prescribed default model rules for societies?

8.101 There are three sets of model articles for companies under the Companies Act 2006.[818] There are no model rules under the CCBS Act. However, section 14 of the CCBS Act prescribes what topics must be addressed in the rules of a society. Also, the FCA has a list of "sponsoring bodies" who produce model rules which the FCA has already vetted as being consistent with the CCBS Act.[819] Applicant societies who use model rules pay a reduced fee for registration.[820]

8.102 Some sponsoring bodies offer multiple model rules, for example depending on whether the society is a worker co-operative or a housing association and so on. Co-operatives UK offer 18 sets of model rules.[821] By way of further comparison, the Charity Commission offers 7 sets of model constitutions,[822] and the Office of the Regulator of Community Interest Companies offers 8 sets.[823]

8.103 Some stakeholders have suggested that there be model rules annexed to the CCBS Act. They say that this could make registration quicker and cheaper (like setting up a company), even if there had to be multiple sets of model rules annexed to the Act.

8.104 In contrast, other stakeholders say that there would need to be too many sets of model rules to make it practical to annex them to the CCBS Act. After all, they say, which set of rules would best suit the would-be society? Some have suggested that there might need to be as many as 12 sets of model rules annexed to the CBBS Act.

8.105 Some stakeholders say that sponsoring bodies are useful in so far as they can advise societies on which set of rules to choose, and how to select the most suitable options within those rules. One stakeholder put it this way: if you cannot afford to pay a few hundred pounds to a sponsoring body, you probably should not be setting up a business.

8.106 In our view, there are too many possible options to make it appropriate to attach multiple sets of model rules as an annex to the CCBS Act. Model rules are in any case available. They are developed and updated by sponsoring bodies when needed – whereas any rules annexed to legislation would need legislative updating, which is burdensome. We think that the advice available from sponsoring bodies is also potentially an added value in the process which should not be discarded too readily. We do not propose any reform here.

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818 Companies Act 2006, ss 19 and 20; The Companies (Model Articles) Regulations 2008 (SI 2008 No 3229). There are also a large number of forerunner model articles which could still govern depending on when the company was incorporated: https://www.gov.uk/guidance/model-articles-of-association-for-limited-companies.

819 https://www.fca.org.uk/publication/forms/mutuals-model-rules-sponsors-list.pdf

820 FCA Guide, paras 3.3.2 to 3.3.5.

821 https://www.uk.coop/resources/model-governing-documents

822 https://www.gov.uk/government/publications/setting-up-a-charity-model-governing-documents

823 https://www.gov.uk/government/publications/community-interest-companies-constitutions

NOMINATION

8.107 Should the mechanism of nomination be abolished?

8.108 Under the CBBS Act, societies are required to have rules about the payment of nominees.[824] Nomination is where a member nominates who is entitled to their society shares (or other society property) upon their death.[825] Nomination is only available up to a limit of £5k.[826] A nomination is not variable by any will.[827] On proof of the member's death, the society must transfer the shares to the nominee.[828] Even if there has been no nomination, a society can distribute the property of a deceased member among such persons as appear to be entitled by law to receive it, even without letters of probate having been obtained.[829]

8.109 The language of section 37 of the CBBS Act seems to suggest that members have a statutory entitlement to nomination. In other words, society rules cannot preclude nomination.[830] The CCBS Act says explicitly that nomination is unaffected by the fact that a society's rules might designate their shares as untransferable.[831] We have heard that some society rules might purport to preclude nomination, but we question whether this is lawful.

8.110 Some stakeholders are content to abolish nomination. They say that most shares have a nominal value and are anyway not withdrawable so that nomination is of little significance. In contrast, some stakeholders say that it can be a cheap and useful alternative to probate. Some say that the limited value of society shares is a reason to provide a cheap alternative to the costs of probate, which might otherwise be disproportionate.

8.111 We are not yet aware of any problems with how nomination operates. Currently, we do not propose any reform.

SUBSIDIARIES

8.112 Should it suffice that a subsidiary society has only one member, namely the parent?

8.113 Under the CCBS Act, a society must have: three members; or two members which are registered societies.[832] There are also rules about preparing group accounts.[833]

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824 CCBS Act, s 14.

825 CCBS Act, s 37. Compare to "transmission" in company law: *Boyle and Bird's Company Law* (10th edn 2019) para 9.22.

826 CCBS Act, s 37(4).

827 CCBS Act, s 38(3).

828 CCBS Act, s 39.

829 CCBS Act, s 40.

830 A view shared by the CCBS Handbook, p 189.

831 CCBS Act, s 39(3).

832 CCBS Act, s 2(2)(b).

833 CCBS Act, ss 98 and 99. For the definitions of "subsidiary", see ss 100 and 101.

8.114 Some stakeholders suggest that a subsidiary society should only need to have one member. Some say that it ceases to be a subsidiary – it becomes a joint venture – if it has more than one member.

8.115 The CCBS Act says that a society can be a wholly owned subsidiary of another corporate body (X) if the society's members are: X; a wholly owned subsidiary of X; a nominee of X; or its wholly owned subsidiary.[834]

8.116 In Chapters 3 and 4, we have proposed definitions of co-operatives and community benefit societies as "societies". We do not think that it is possible to be a society of one.

8.117 As regards co-operatives in particular, in Chapter 3, we noted that the definition of a co-operative, advocated by the International Cooperative Alliance (ICA) and accepted by the FCA, was an "association" of members. We said that association and society meant the same thing. At any rate, we think that a co-operative needs at least one other person to co-operate with. We are not currently persuaded to propose that societies need only have one member.

VERIFICATION OF IDENTITY

8.118 Should there be legislative rules requiring the verification of members' identities?

8.119 One stakeholder has suggested this, in order to prevent individuals registering multiple times to secure multiple votes. Other stakeholders say that this is already forbidden by the law of fraud, or rarely occurs, or would be a major administrative burden for some societies.

8.120 In our view, each society can set its own processes for verifying the identity of anyone wishing to become a member. We do not think it appropriate to prescribe a process by statute, which is then fixed for everyone for the future. We do not make any proposals in this regard.

PEOPLE WITH SIGNIFICANT CONTROL

8.121 Should societies maintain a list of people with significant control?

8.122 Under the CCBS Act, a society must keep a list of members and officers.[835] In company law, a company must keep registers of members,[836] directors,[837] and secretaries,[838] and there are also duties to gather information about, and keep a

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834 CCBS Act, s 99(7).

835 CCBS Act, s 30.

836 Companies Act 2006, s 113.

837 Companies Act 2006, s 162.

838 Companies Act 2006, s 275.

register of, "people with significant control".[839] These requirements do not apply to public companies with voting shares admitted to trading on regulated markets.[840]

8.123 For a person to have significant control over a company:[841]

(1) They hold, directly or indirectly, more than 25% of shares[842] or voting rights[843] (or have a power of veto)[844] in the company; or

(2) They have the right to appoint or remove a majority of (the votes on)[845] the board of directors;[846] or

(3) They have the right to exercise, or actually exercise, significant influence or control over the company.[847]

8.124 Where A has a controlling shareholding in B who has a shareholding in C, then A has an indirect shareholding in C.[848] Also, if A has significant control over B who has significant control over C, then A also has significant control over C.[849]

8.125 The Secretary of State must issue guidance on what "significant control" means.[850] According to that guidance,[851] a person has significant control if the company generally adopts the activities which that person desires.[852] It includes a person whose recommendations are almost always followed by the board or by the majority of voting shareholders.[853]

8.126 If societies were to have rules about people with significant control, then we think that it would probably be appropriate to apply the rules in Part 21A of the Companies Act 2006 to societies (rather than create a separate regime from scratch).

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839 Companies Act 2006, Pt 21A.

840 Companies Act 2006, s 790B.

841 Companies Act 2006, sch 1A Pt 1.

842 Companies Act 2006, sch 1A para 2.

843 Companies Act 2006, sch 1A para 3.

844 Companies Act 2006, sch1A para 14(2)(b).

845 Companies Act 2006, sch 1A para 16.

846 Companies Act 2006, sch1A para 4.

847 Companies Act 2006, sch1A para 5.

848 Companies Act 2006, sch1A para 18.

849 Companies Act 2006, sch 1A para 6.

850 Companies Act 2006, sch 1A para 24.

851 https://www.gov.uk/government/publications/guidance-to-the-people-with-significant-control-requirements-for-companies-and-limited-liability-partnerships (PSC Guidance).

852 PSC Guidance, para 1.23.

853 PSC Guidance, para 3.3.

8.127 However, the origins of this company law were a concern that company structures could be used to conceal the "true" owners of a company, who could then use a private company for criminal purposes like money laundering or financing terrorism.[854]

8.128 We have not yet heard that stakeholders or the registrar have any real concerns about people using societies as a front for criminal activities. Further, society structure, such as one vote per member, reduces to some extent the potential for significant control over a society. Restrictions on withdrawing or transferring shares, and limits on rates of return, are perhaps a further barrier to using societies for criminal purposes.

8.129 We would be reluctant to propose an additional regulatory burden on societies or the registrar if there was little need. We are not yet persuaded that there is a need to apply to societies the rules in company law about people with significant control.

REWARDS FOR FOUNDERS

8.130 Should the CCBS Act acknowledge the legitimacy of rewarding society founders?

8.131 One stakeholder has suggested that such a reward might be, for example, an additional share of any surplus. Legislative acknowledgment might appear, they suggest, in section 14, or Part 3 (to create a category of founder member).

8.132 Other stakeholders think that this creates unnecessary extra complexity. Why not, they say, have founders simply pay themselves a salary for any work they do for the society? If cash flow is problematic to begin with, salary could be earned now but paid later. An alternative might be to allocate paid-up withdrawable shares.

8.133 Beyond that, we question the extent to which reward for founders is compatible with the ethos of a co-operative or a community benefit society, for the following reasons.

8.134 A community benefit society should carry on business for the sole benefit of the community. This does not mean that anyone associated with it should volunteer or work for free, but reward beyond a salary (or salary substitute like shares) risks becoming a payment for personal gain rather than for community benefit.

8.135 A co-operative succeeds through co-operation. It might be that one person provides an initial driving force, but co-operation necessarily requires the involvement of more people. The Co-operative Values of democracy and equality would suggest that all co-operators within a society are equals.[855] The success of a co-operative will depend on the vigour of co-operation, or subsequent waves of new membership. It is not obvious that the first members should benefit from that in a way which excludes later members who make important contributions.

8.136 Those who wish to profit, not from transacting with the business itself, but from the very creation of the business, have different corporate forms to choose from, like the company. There is nothing to preclude those other forms from being run on a co-operative basis. We do not propose any reform here.

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854 *Gore-Browne on Companies* (January 2024) ch 34 para [1].

855 On co-operative values, see Chapter 2.

LISTING CHARGES ON THE MUTUALS PUBLIC REGISTER

8.137 One stakeholder has suggested that it should be compulsory for societies to list all charges on their assets on the Mutuals Public Register. In this way, they say, credit reference agencies would know that the Mutuals Public Register presents a full picture.

8.138 Under Part 5 of the CCBS Act, in England and Wales, an application to the registrar can be made to register a fixed or floating charge on a society's assets.[856] The application can be made by the society or by the lender who has taken the charge as security for a loan.[857] If the application is accepted, the registrar is to keep a record on file, available for public inspection on payment of a fee.[858] This scheme does not apply to debentures under the Agricultural Credits Act 1928.[859] There is a parallel scheme for societies in Scotland.[860]

8.139 This provision was first introduced by the Industrial and Provident Societies Act 1967. This was done, according to the CCBS Handbook, because otherwise societies were unable to give floating charges.[861] At any rate, Part 5 does not make it compulsory to list all charges, and it does not require the registrar to record any charges on the Mutuals Public Register. In practice, however, the FCA does place a copy on the Mutuals Public Register.[862]

8.140 By way of comparison, in company law, a company was previously required to register any charges with the registrar.[863] However, this was repealed.[864] Under the new (current) regime, a charge can be registered by the company or any person interested in the charge,[865] and if not, then the charge is void against a creditor or liquidator or administrator.[866] Not all charges can be registered.[867]

8.141 We are not currently persuaded that it would be proportionate for legislation to impose duties on societies and the registrar to register society charges simply to make the Mutuals Public Register more usable by credit reference agencies.

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856 CCBS Act, s 59.

857 FCA Guide, para 8.7.3.

858 CCBS Act, s 59(4).

859 CCBS Act, s 59(6).

860 CCBS Act, ss 62 to 64.

861 CCBS Handbook, pp 39 and 195.

862 FCA Guide, para 8.7.7.

863 Companies Act 2006, s 860.

864 The Companies Act 2006 (Amendment of Part 25) Regulations 2013 (SI 2013 No 600).

865 Companies Act 2006, s 859A.

866 Companies Act 2006, s 859H.

867 See the discussion / criticism of company law in this regard in *Boyle and Bird's Company Law* (2022) paras 10.25 and 10.26.

LACK OF CAPACITY

8.142 Do the rules in the CCBS Act about a society's lack of capacity need reform to align with company law?

8.143 In company law, for example, the validity of an act done by a company shall not be called into question on the ground of lack of capacity by reason of anything in the company's constitution.[868] Additional rules apply to charities.[869]

8.144 Section 43 of the CCBS Act provides that the validity of an act done by a society may not be called into question on the ground of lack of capacity by reason of anything in the society's registered rules. Again, additional rules apply to charities.[870]

8.145 In our view, society law aligns with company law on this issue.[871] We do not currently see any need for reform.

VOTES ON SIGNIFICANT TRANSACTIONS

8.146 Should there be a statutory rule that requires a member vote for all "significant transactions"?

8.147 For example, while a community benefit society might have an asset lock, this does not prevent it from selling a significant asset (as long as the proceeds are still applied to benefit the community). In this way, a community benefit society might even be able to sell the asset which it was set up to own.

8.148 In comparison, a company may not enter into an arrangement to buy or sell a substantial non-cash asset *with a director* unless approved by a resolution of the members of the company.[872] "Substantial" is defined as: more than 10% of the company's asset value and more than £5k; or more than £100k.[873]

8.149 On the one hand, we can see the sense in protecting the central asset of a community benefit society by requiring any sale of that asset to be put to a vote. That said, such a requirement could be added to the rules of the community benefit society without necessitating a statutory provision.

8.150 On the other hand, requiring a vote for any significant transaction could prove challenging administratively, especially for large co-operatives. More of their transactions might exceed the threshold, and requiring a vote from a large membership could cause the society to become inefficient in its business dealings.

8.151 Further, company law does not require all substantial transactions to be put to a vote, but only those involving the self-dealing of a director. This is already addressed under

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868 Companies Act 2006, s 39.

869 Companies Act 2006, s 42.

870 CCBS Act, s 47.

871 A view shared by the CCBS Handbook, p 269.

872 Companies Act 2006, s 190.

873 Companies Act 2006, s 191.

the CCBS Act: a transaction between the society and a committee member is voidable, and the committee member must account for any gain.[874]

8.152 Overall, we are not currently persuaded to propose a statutory rule requiring all significant transactions be approved by a resolution of members.

REGULATING HOUSING SOCIETIES

8.153 Should all housing societies be required to register with the Regulator of Social Housing?

8.154 In England, societies can register with the Regulator of Social Housing.[875] Regulation is governed by the Housing and Regeneration Act 2008. Registration is optional, but many housing societies choose to register as a mark of quality assurance. In Wales, regulation is provided by Welsh Ministers' Housing Regulation Team,[876] under the Housing Act 1996. In Scotland, there is the Scottish Housing Regulator,[877] and the governing legislation is the Housing (Scotland) Act 2010. Reform to any of these statutes is outside the scope of this review.

874 CCBS Act, s 48.

875 https://www.gov.uk/government/organisations/regulator-of-social-housing

876 https://www.gov.wales/sites/default/files/publications/2022-01/regulatory-framework-for-housing-associations-registered-in-wales.pdf

877 https://www.scottishhousingregulator.gov.uk/

Chapter 9: Final questions

9.1 We conclude this consultation paper with the following final questions.

Consultation Question 81.

9.2 How would reform affect you? Please provide a general answer here. When answering other questions, please tell us, where possible, how that specific reform might affect you.

Consultation Question 82.

9.3 Are there any factors unique to Scotland which you think we should know about?

Consultation Question 83.

9.4 Are there any factors unique to the Channel Islands which you think we should know about?

Consultation Question 84.

9.5 Are there any other ways in which the CCBS Act might be improved to support the formation and development of new societies?

Consultation Question 85.

9.6 Does the CCBS Act raise barriers to growth and innovation, such that there are other reforms which are needed to support growth and innovation for societies?

Consultation Question 86.

9.7 Does the CCBS Act cause societies to incur unnecessary costs and burdens, such that there are other reforms which are needed to reduce those burdens and support the more efficient operation of societies?

Consultation Question 87.

9.8 Are there any other reforms to the CCBS Act needed to support an effective registrar?

Chapter 10: Consultation Questions

Consultation Question 1.

10.1 We provisionally propose that there should be a new statutory definition of a co-operative. Do you agree in principle (subject to the formulation of a suitable definition)?

Paragraph 3.32

Consultation Question 2.

10.2 We provisionally propose a definition of a co-operative with the following ingredients.

A co-operative is:

(1) A society for carrying on any business;

(2) Mainly for the benefit of its members…

(3) …through transactions with its members;

(4) Membership is voluntary;

(5) Membership is open to all;

(6) One vote per member.

Do you agree with these elements? Are there any that you do not agree with?

10.3 In particular, do you think it accurate to describe the membership of any co-operative as "open to all", and if so why?

Paragraph 3.91

Consultation Question 3.

10.4 We provisionally propose that any new statutory definition of a co-operative should apply to all co-operatives and not only those registering after the introduction of the new definition. Do you agree?

Paragraph 3.99

Consultation Question 4.

10.5 We provisionally propose a transition period of 18 months for existing co-operatives to comply with any new definition. Do you agree?

Paragraph 3.100

Consultation Question 5.

10.6 We provisionally propose that there should be a new statutory definition of a community benefit society. Do you agree in principle (subject to the formulation of a suitable definition)?

Paragraph 4.25

Consultation Question 6.

10.7 We provisionally propose the following ingredients for a new statutory definition of a community benefit society.

A community benefit society is:

(1) A society for carrying on any business;

(2) For the sole benefit of the community;

(3) Membership is voluntary;

(4) Membership is open to all;

(5) One vote per member.

Do you agree with these elements? Are there any that you do not agree with?

10.8 In particular, do you think it accurate to describe the membership of any community benefit society as "open to all", and if so why?

Paragraph 4.46

Consultation Question 7.

10.9 We provisionally propose that any new statutory definition of a community benefit society should apply to all community benefit societies and not only those registering after the introduction of the new definition. Do you agree?

Paragraph 4.54

Consultation Question 8.

10.10 We provisionally propose a transition period of 18 months for existing community benefit societies to comply with any new definition. Do you agree?

Paragraph 4.55

Consultation Question 9.

10.11 We provisionally propose that charitable community benefit societies should cease to be exempt charities, so that they will be required to register with the Charity Commission. Do you agree?

Paragraph 4.81

Consultation Question 10.

10.12 Do you think that the lead regulator for charitable community benefit societies should be the Charity Commission or the FCA?

Paragraph 4.82

Consultation Question 11.

10.13 We provisionally propose that the CCBS Act should be amended to state explicitly as follows.

(1) Society shares can be withdrawable or non-withdrawable, and transferable or non-transferable.

(2) It is for societies by their rules to determine which of their shares are withdrawable or non-withdrawable, and transferable or non-transferable.

Do you agree?

Paragraph 5.39

Consultation Question 12.

10.14 We provisionally propose that the CCBS Act should provide a definition of a withdrawable share. Do you agree?

Paragraph 5.62

Consultation Question 13.

10.15 We provisionally propose the following ingredients of a definition of a withdrawable share.

(1) A withdrawable share can be cashed in, such that a society pays the value of the share, to the holder of the share, in return for the share being cancelled.

(2) A withdrawable share can be withdrawn at the option of the member or the society, depending on the society's rules.

Do you agree with each of these elements?

Paragraph 5.63

Consultation Question 14.

10.16 We provisionally propose that the CCBS Act should set out the minimum conditions for withdrawing shares. Do you agree?

Paragraph 5.85

Consultation Question 15.

10.17 We provisionally propose that the CCBS Act should provide that society rules can set extra conditions for withdrawing shares. Do you agree?

Paragraph 5.86

Consultation Question 16.

10.18 We provisionally propose that the minimum conditions for withdrawing shares should be as follows.

A society should pay for withdrawable shares only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year.

Do you agree?

10.19 In particular, we think that a society considering requests for withdrawal should be able to pay a proportion of the sought withdrawals, rather than all or nothing, if that is what it can afford. Do you agree?

Paragraph 5.87

Consultation Question 17.

10.20 We provisionally propose that the CCBS Act should provide a definition of a transferable share. Do you agree?

Paragraph 5.93

Consultation Question 18.

10.21 We provisionally propose that a transferable share be defined as one that can be passed from one person to another such that the transferee holds the share in place of the transferor. Do you agree?

Paragraph 5.94

Consultation Question 19.

10.22 We provisionally conclude that the form of transfer should be left to the sector to determine rather than prescribed in legislation. Do you agree?

If you do not agree, please detail what form you consider should be prescribed.

Paragraph 5.104

Consultation Question 20.

10.23 As for transferable shares, we provisionally propose that the CCBS Act should be amended to state as follows.

(1) The consent of officers of a society is needed to transfer shares.

(2) Officers can in their discretion refuse a transfer of shares.

(3) Their discretion must be exercised consistently with their duties as officers.

(4) The rules of a society can set further conditions on the transfer of shares.

(5) The rules of a society must provide for the form of any transfer of shares.

Do you agree with each proposition?

Paragraph 5.113

Consultation Question 21.

10.24 We provisionally propose that the CCBS Act should state as follows.

(1) A society can have different classes of membership with different rights.

(2) A society can issue different classes of shares with different rights.

(3) A society can issue shares to non-user investors.

Do you agree?

Paragraph 5.120

Consultation Question 22.

10.25 We provisionally propose, in the context of changes to class rights of shares or members, that the CCBS Act should provide as follows.

(1) Class rights should only be changed if the change is approved by at least 75% of affected shareholders or members.

(2) Society rules could set a higher threshold.

(3) If shares are changed from non-withdrawable to withdrawable, that should require a solvency statement by the officers of the society, confirmed by an auditor.

Do you agree with each element?

Paragraph 5.135

Consultation Question 23.

10.26 We think that there should be some protection for shareholders who still object to any change in their class rights. Which of the following protections do you think is suitable? You can select more than one, or indicate your preferred option.

(1) A complainant could petition the court to wind up a society on the basis that it would be just and equitable to do so.

(2) A complainant could petition the court on the basis that any change to class rights would be unfairly prejudicial.

(3) A society would have to buy out an objecting shareholder.

(4) Any change would not take effect against a shareholder who objects in writing.

If you think that there should be a different protection, please explain.

Paragraph 5.136

Consultation Question 24.

10.27 We provisionally propose that, when a society seeks to write down its shares, that should require a solvency statement by officers of the society, and a special resolution. Do you agree?

10.28 We provisionally propose that the special resolution should require the approval of at least 75% of voters at a general meeting. Do you agree?

Paragraph 5.141

Consultation Question 25.

10.29 We provisionally propose that there should be the following restrictions on interest rates paid by co-operatives on investments, deposits and loans.

(1) Any interest rate should be no more than is needed to obtain necessary funding.

(2) Any interest rate should be no more than a reasonable rate.

(3) Interest on investments and deposits should be paid only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year.

Do you agree?

10.30 In particular, we think that a co-operative considering interest payments should be able to pay a lesser rate, rather than all or nothing, if that is what it can afford. Do you agree?

Paragraph 5.206

Consultation Question 26.

10.31 We provisionally propose that there should be the following restrictions on rates of interest paid by community benefit societies on investments, deposits and loans.

(1) Any interest rate should be no more than is needed to obtain necessary funding.

(2) Any interest rate should be no more than a reasonable rate.

(3) Interest on investments and deposits should be paid only to the extent that the officers of the society think that the society can also pay its debts at that time and as they fall due over the following year.

Do you agree?

10.32 In particular, we think that a community benefit society considering interest payments should be able to pay a lesser rate, rather than all or nothing, if that is what it can afford. Do you agree?

Paragraph 5.214

Consultation Question 27.

10.33 Do you think that societies need a new type of share? If so, what would be its characteristics?

Paragraph 5.240

Consultation Question 28.

10.34 We provisionally propose that an officer be defined in section 149 of the CCBS Act as including a director. Do you agree?

Paragraph 6.8

Consultation Question 29.

10.35 We provisionally propose that officers of a society should be listed on the Mutuals Public Register. Do you agree?

Paragraph 6.15

Consultation Question 30.

10.36 We provisionally propose that a society should notify the registrar of any changes concerning its officers within 14 days. Do you agree?

Paragraph 6.16

Consultation Question 31.

10.37 We provisionally propose that a society's register of members and officers, available for inspection, should include their name and a contact address. Do you agree?

Paragraph 6.30

Consultation Question 32.

10.38 We provisionally propose that the contact address for members and officers might be an electronic address. Do you agree?

Paragraph 6.31

Consultation Question 33.

10.39 We provisionally propose that any contact address for members and officers which is a postal address need not be the residential address. Do you agree?

Paragraph 6.32

Consultation Question 34.

10.40 We provisionally propose that the residential address of an officer should be notified to the FCA. This would be confidential, but the FCA may use it to make contact with the officer. Do you agree?

Paragraph 6.33

Consultation Question 35.

10.41 We provisionally propose that duties owed by officers to their society should be addressed by the CCBS Act. Do you agree?

Paragraph 6.49

Consultation Question 36.

10.42 We provisionally propose that the CCBS Act should adopt the director duties set out in the Companies Act 2006. Do you agree?

Paragraph 6.50

Consultation Question 37.

10.43 We provisionally propose that the CCBS Act should follow company law and state that the consequences of a breach of duty by an officer would be those provided by common law or equity. Do you agree?

10.44 We do not propose the creation of any statutory derivative claim, such that a member can sue an officer in the name of the society. Do you agree?

Paragraph 6.59

Consultation Question 38.

10.45 We provisionally propose that there should be a right to appeal decisions by the registrar on whether a society meets the definition of a co-operative or community benefit society. Do you agree?

Paragraph 7.10

Consultation Question 39.

10.46 Do you think that an appeal against a decision by the registrar should be heard by the court (as is currently the case) or by a tribunal?

Paragraph 7.13

Consultation Question 40.

10.47 We provisionally propose that the power of the registrar to suspend a society's registration be repealed. Do you agree?

Paragraph 7.31

Consultation Question 41.

10.48 We provisionally propose that only after the notice period for cancellation has passed should the registrar be able to give directions to wind up the affairs of the society. Do you agree?

Paragraph 7.38

Consultation Question 42.

10.49 We provisionally propose that the notice period for cancellation be fixed at two months. Do you agree?

Paragraph 7.41

Consultation Question 43.

10.50 We provisionally propose that the CCBS Act should require the registrar to give a society reasonable warning before issuing any notice of proposed cancellation. Do you agree?

Paragraph 7.46

Consultation Question 44.

10.51 We provisionally propose that societies be given a statutory power to entrench their rules. Do you agree?

Paragraph 7.56

Consultation Question 45.

10.52 We provisionally propose that it should be for the rules of a society to decide the voting threshold needed to change an entrenched rule. Do you agree?

Paragraph 7.57

Consultation Question 46.

10.53 We provisionally propose that a society's rules should be capable of being entrenched on registration or later by special resolution. Do you agree?

Paragraph 7.62

Consultation Question 47.

10.54 We provisionally propose that the special resolution threshold which must be exceeded in order to entrench a rule should be the same as the threshold required for adopting an asset lock, that is:

(1) a first meeting where at least 75% of voters are in favour and at least 50% of members vote, followed by

(2) a second meeting where over half of voters are in favour (see section 113 of the CCBS Act).

Do you agree?

Paragraph 7.68

Consultation Question 48.

10.55 We provisionally propose that a society should be able to set voting thresholds in its own rules which are stricter than those in the CCBS Act in the following circumstances.

(1) Ratifying action by members of the committee which would otherwise be beyond the capacity of the society.

(2) Amalgamating societies or transferring engagements to another society.

(3) Converting to, amalgamating with, or transferring engagements to a company.

(4) Approving an instrument of dissolution.

(5) Disapplying the duty to appoint auditors.

Do you agree?

Paragraph 7.75

Consultation Question 49.

10.56 We provisionally propose that the restrictions on the use of the assets of a community benefit society, and the enforcement powers in that regard, as set out in the Asset Lock Regulations, be included in the CCBS Act as applicable to all community benefit societies. Do you agree?

Paragraph 7.89

Consultation Question 50.

10.57 We provisionally propose that the CCBS Act should expressly allow for asset-locked community benefit societies to pay interest on non-withdrawable shares. Do you agree?

Paragraph 7.96

Consultation Question 51.

10.58 We provisionally propose that it should be possible for a community benefit society with a statutory asset lock to become a charity. Do you agree?

Paragraph 7.101

Consultation Question 52.

10.59 We provisionally propose that the asset lock provisions of the Co-operatives, Mutuals and Friendly Societies Act 2023, as far as they apply to co-operatives, should be consolidated into the CCBS Act. Do you agree?

Paragraph 7.107

Consultation Question 53.

10.60 We provisionally propose that the Asset Lock Regulations which apply to community benefit societies should also apply to co-operatives which choose a statutory asset lock. Do you agree?

Paragraph 7.108

Consultation Question 54.

10.61 We provisionally propose that section 115 of the CCBS Act should be amended so that, when a company converts to a society, it must appoint either three members, or two members if both are registered societies. Do you agree?

Paragraph 7.114

Consultation Question 55.

10.62 We provisionally propose that the CCBS Act should provide expressly that partial transfers of engagements are possible, to companies or to other registered societies. Do you agree?

Paragraph 7.120

Consultation Question 56.

10.63 We provisionally propose that, where a society converts to, amalgamates with, or transfers its engagements to a company, any transfer of the society's property should vest without conveyance. Do you agree?

Paragraph 7.129

Consultation Question 57.

10.64 We provisionally propose that section 112 (conversion of a society to a company) be amended to remove reference to a society's registration being void. Do you agree?

Paragraph 7.138

Consultation Question 58.

10.65 Do you think that the registrar should advertise the cancellation of a society's registration or its dissolution in a local newspaper as well as in the Gazette?

Paragraph 7.143

Consultation Question 59.

10.66 We provisionally propose that the CCBS Act should enable HM Treasury by regulation to disapply duties under the CCBS Act temporarily for special reason (such as a pandemic). Do you agree?

Paragraph 7.148

Consultation Question 60.

10.67 Do you think that the CCBS Act should empower the registrar to require electronic-only filing of documents?

Paragraph 7.153

Consultation Question 61.

10.68 We provisionally propose repealing the need for signatures on a society's filed accounts. Do you agree?

Paragraph 7.156

Consultation Question 62.

10.69 Do you think that the registrar should have the power to impose a civil penalty in the form of a fine on a society which is late in filing their annual return (in line with equivalent penalties under company law)?

Paragraph 7.165

Consultation Question 63.

10.70 We provisionally propose as follows.

(1) The registrar should be able to direct a society to change its name after registration if the name has since become undesirable in the opinion of the registrar.

(2) There should be a right to appeal such a direction.

Do you agree?

Paragraph 7.174

Consultation Question 64.

10.71 We provisionally propose that the Mutuals Public Register be identified explicitly in the CCBS Act as the sole register which the registrar of societies is to maintain. Do you agree?

Paragraph 7.177

Consultation Question 65.

10.72 Do you think that the seal of the registrar of co-operative and community benefit societies be provided for under the CCBS Act?

Paragraph 7.181

Consultation Question 66.

10.73 We provisionally propose that the registrar should be able to use their available powers of intervention where the registrar believes that intervention is appropriate in the circumstances (rather than "only to the extent necessary to maintain confidence" in societies). Do you agree?

Paragraph 7.190

Consultation Question 67.

10.74 We provisionally propose that the CCBS Act should provide the following regime for society audits.

(1) Any person appointed to audit the accounts should be a qualified auditor.

(2) A society should be able to opt out of the duty to audit accounts when the society is below a certain size.

(a) There should be a single threshold (above which a society cannot opt out of the requirement to audit).

(b) That threshold should be both that turnover is not in excess of £10.2m and assets are not in excess of £5.1m.

(c) That threshold should be capable of revision by statutory instrument.

(3) The registrar should continue to be able to insist upon an audit.

Do you agree?

Paragraph 7.201

Consultation Question 68.

10.75 Do you think that co-operatives should be required by legislation to report on how their activities pursue their objectives?

10.76 Do you think that community benefit societies should be required by legislation to report on how their activities pursue their objectives?

Paragraph 7.207

Consultation Question 69.

10.77 Do you think that the CCBS Act should allow a society's financial year to end up to seven days earlier or later than the previous year (as with company law)?

Paragraph 7.213

Consultation Question 70.

10.78 We provisionally propose that section 81 of the CCBS Act be repealed (to remove the duty to display a balance sheet at a society's registered office). Do you agree?

Paragraph 7.216

Consultation Question 71.

10.79 We provisionally propose that, subject to its rules, a society should additionally be able to execute a document by one authorised signatory attested by a witness. Do you agree?

Paragraph 7.221

Consultation Question 72.

10.80 We provisionally propose that, subject to its rules, a society should be able to appoint, by deed, an attorney to execute documents on its behalf. Do you agree?

Paragraph 7.225

Consultation Question 73.

10.81 We provisionally propose that “cooperative”, “co-op” and “coop” should be included alongside “co-operative” on the list of sensitive (protected) business names. Do you agree?

Paragraph 7.238

Consultation Question 74.

10.82 We provisionally propose that the requirement to display a society’s registered name outside every place where it carries on business be repealed. Do you agree?

Paragraph 7.242

Consultation Question 75.

10.83 We provisionally propose that, subject to the rules of a society, the CCBS Act should expressly allow meetings to be virtual or hybrid. Do you agree?

Paragraph 7.248

Consultation Question 76.

10.84 We provisionally propose that, when a society notifies the FCA of an amendment to the society’s rules, the society need send only one copy of the amendment if this is sent by electronic means. Do you agree?

Paragraph 7.255

Consultation Question 77.

10.85 Do you think that the CCBS Act should explicitly provide that society rules may provide for an indivisible reserve?

Paragraph 7.258

Consultation Question 78.

10.86 Do you think that there is a need to reform the law relating to co-operative banks? If so, what reforms do you think are needed?

10.87 Do any of the proposed changes to the CCBS Act have particular consequences for co-operative banks that we need to consider?

Paragraph 7.264

Consultation Question 79.

10.88 Do you think that there is a need to reform the law relating to credit unions? If so, what reforms do you think are needed?

10.89 Do any of the proposed changes to the CCBS Act have particular consequences for credit unions that we need to consider?

Paragraph 7.268

Consultation Question 80.

10.90 As regards the topics set out in Chapter 8, we have provisionally concluded against reform. Do you think that any of those topics needs revisiting, and if so why?

Paragraph 8.2

Consultation Question 81.

10.91 How would reform affect you? Please provide a general answer here. When answering other questions, please tell us, where possible, how that specific reform might affect you.

Paragraph 9.2

Consultation Question 82.

10.92 Are there any factors unique to Scotland which you think we should know about?

Paragraph 9.3

Consultation Question 83.

10.93 Are there any factors unique to the Channel Islands which you think we should know about?

Paragraph 9.4

Consultation Question 84.

10.94 Are there any other ways in which the CCBS Act might be improved to support the formation and development of new societies?

Paragraph 9.5

Consultation Question 85.

10.95 Does the CCBS Act raise barriers to growth and innovation, such that there are other reforms which are needed to support growth and innovation for societies?

Paragraph 9.6

Consultation Question 86.

10.96 Does the CCBS Act cause societies to incur unnecessary costs and burdens, such that there are other reforms which are needed to reduce those burdens and support the more efficient operation of societies?

Paragraph 9.7

Consultation Question 87.

10.97 Are there any other reforms to the CCBS Act needed to support an effective registrar?

Paragraph 9.8

Appendix 1: Terms of reference

1.1 The Law Commission is to review the Co-operatives and Community Benefit Societies Act 2014.

1.2 The aim of the project is to identify changes to the legislative framework for co-operatives and community benefit societies which would modernise the law, proportionally reduce barriers/costs to operation for these societies, and support a more proportionate and effective regulatory environment – aligning as appropriate with relevant Acts which have updated in more recent years.

1.3 In particular, the Law Commission is to consider whether reform is warranted to ensure that:

(1) the governing law is fitting to the nature and needs of co-operatives and community benefit societies, identifying necessary updates to the legislation based on other modernisations; and

(2) the regulation is proportionate and effective.

1.4 The review is likely to include consideration of the following issues.

(1) Alignment with company and insolvency law.

(2) Alignment with data protection legislation.

(3) Alignment with auditing requirements.

(4) Alignment with charities law, as applicable, for charitable community benefit societies.

(5) The role and functionality of the registrar, including whether the mutuals register should contain a list of directors or managers.

(6) Consequences of, and manner of challenges to, suspension of registration and de-registration.

(7) Methods of raising capital.

(8) Dysfunctions in the existing community benefit society asset lock.

1.5 The Law Commission will not make recommendations as to the identity of the registrar or departmental ownership of the legislation.

1.6 If any reform to share capital is thought to be warranted, the Law Commission will set out options for reform.

Appendix 2: List of consultees

Prior to publishing this consultation paper, we have spoken or corresponded with the following:

Anthony Collins Solicitors LLP: Cliff Mills, David Alcock

Central England Co-operative: Simon Plunkett, Andrew Seddon

Charity Commission: Sania Akbar, Emma Khan, Holly Riley, James Wilkinson

Community Housing Cymru: Elly Lock

Confederation of Co-operative Housing: Blase Lambert

Co-operatives UK: James Wright, Tom Laing, Stephen Gill

Co-operatives & Mutuals Wales: David Smith, Bill Phillips, Peter Milford

Devonshires Solicitors LLP: Anna Bennett, Gemma Bell.

East of England Co-op: Jonathan Carey

Energy 4 All Ltd: Mike Smyth

Financial Conduct Authority: Ian Adderley, Gareth Reed, Morwenna Blewett

Football Supporters' Association: Nicola Cave

Housing Regulation Team, Welsh Government: Ian Walters

Ian Snaith

Mutuo: Peter Hunt

National Federation of Tenant Management Organisations: Nick Reynolds, Liz Michael

Newport City Homes: Joanna Fairley

Plunkett Foundation: Alison Macklin

Power to Change: Jessica Craig

Regulator of Social Housing: Mark Smith, Anna Moore, Anna Furlong

The Co-op Group: Dominic Kendal-Ward

The Midcounties Co-operative: Edward Parker

Trowers & Hamlins LLP: Ian Davis

union-coops:uk: Alex Bird

West Solent Solar Cooperative Limited: Cathy Cook

Workers.coop: John Atherton

Wrigleys Solicitors LLP: Malcolm Lynch, Peter Parker, Laurel Sleet, Morgan Gibson

We have also attended events hosted by the following:

All Party Parliamentary Group on Mutuals

Co-operatives & Mutuals Wales

Co-operatives UK

Social Enterprise Scotland

Appendix 3: Historic guidance

Copy seen by CR. 29/8/38. 8/8/3
CMB

Prevention of Fraud (Investments) Bill.

Herewith copy of the above "Sharepushing" Bill. Your attention is drawn to -

Clause 8 which restricts future registration under the Industrial and Provident Societies Acts to societies which satisfy the Registrar that they come within the categories authorised under Sub-clauses (1) and (6) and gives him power to cancel societies if at any time he discovers that they do not fulfil the new conditions of registration except where the societies were registered before 26th July 1938 and have not invited the public to invest since that date;

Clause 23(1) which defines securities, shares and debentures;

Clause 10(2)(a)(v) which exempts Industrial and Provident Societies and Building Societies from the restriction imposed by this clause on the distribution of circulars relating to investments.

The Bill is to be re-introduced in the Autumn Session and the Chief Registrar would be glad if in the meantime you would please examine the proposals thoroughly and submit any criticisms or suggestions which occur to you.

Certain questions inevitably arise on a reading of Clause 8 and the following comments are made tentatively in order to provide material for consideration.

Clause 8(1)(a).

What is a "bona fide co-operative society"? This phrase was used as a last resort because it had not been found possible to arrive at a satisfactory definition.

It is suggested that a bona fide co-operative society must satisfy the following conditions:-

(a) it cannot be a "money-making" society as defined in sub-clause 6;

(b) it must so conduct its business as to show that

/it exists

it exists primarily for the mutual benefit of its members, such benefit taking different forms according to the nature of the society but being always directly related to the use which the member makes of the facilities provided by the society and not to the amount of capital which he invests in or through the society (by contrast the non-co-operative society seeks to make profits for, and to apply them to the greatest advantage of, its shareholders as such);

(c) there must be no artificial restriction of membership i.e. no restriction with the object of enhancing the value of the "proprietary" rights or interests of the members. On the other hand restriction of membership would not necessarily offend the co-operative principle e.g. in the case of a club which must relate the number of members to the size of its premises, or in the case of a society which confines its activities to a particular area;

(d) no member other than a registered society shall have more than one vote;

(e) the return (in whatever form) on share capital must not exceed a moderate rate which might perhaps be taken, for practical purposes, as the maximum rate for the time being laid down by the Treasury in the case of a "Housing Association".

Clause 8(1)(b)

The intention is to let in societies which, although not co-operative societies, exist exclusively or mainly for a philanthropic or charitable purpose or for the promotion of social welfare e.g. slum-clearance societies and other housing societies, cultural or recreational societies, which do not aim at profit-making but seek to benefit members of the working classes who are usually not members of the society.

What are the "working classes"? For certain purposes

/under the

under the Housing Act, 1936 the expression is defined as including mechanics, artisans etc. working for wages, persons not working for wages but working at some trade or handicraft without employing others, and persons whose average income does not exceed £3 a week. Another statutory definition, now repealed, makes the term cover all classes of persons who earn their livelihood by wages or salaries. It remains to be seen, however, whether any precise definition will be necessary in view of the intentions of paragraph (b) read as a whole and the fact that in any event the Registrar must be satisfied that there are special reasons for registry under the Industrial and Provident Societies Act. It seems hardly likely that the kind of societies contemplated in paragraph (b) would be carried on for the benefit of persons who would not come within a broad definition of the working classes; but if there were such societies they would have to bring themselves within the definition of bona fide co-operative societies or be excluded.

What are the "special reasons"? The general idea behind the whole Clause is that registration under the Companies Act must be regarded as the normal course and that registration under the Industrial and Provident Societies Acts is not a mere alternative form of registration but must be looked at and justified in the light of the origin and purpose of those Acts. They were of course a direct offshoot of the early Friendly Societies Acts and their object was to extend the scope of "provident" legislation beyond the purposes covered by the Friendly Societies Acts by facilitating the co-operation of members of the industrial classes in any industry, business or trade for their mutual benefit. The Acts thus became the charter of the Co-operative Movement and their main purpose is safeguarded by paragraph (a) of Clause 3(1), although a bona fide co-operative society is not confined to ~~the~~ members of ~~any~~ The working classes in terms to be as any more than is a friendly society.

The purpose mentioned in paragraph (b) is clearly in /line with

line with the objects behind the Friendly Societies Acts and the Industrial and Provident Societies Acts, but the societies in question are not co-operative in the ordinary sense. It is not sufficient, however, to rely on the purpose only because a society run for the purpose of (say) slum-clearance might be exploited by interested persons in which event the Registrar would not be satisfied that there were special reasons for registration under the Industrial and Provident Societies Acts.

The point of view to be adopted in considering registration under the Industrial and Provident Societies Acts is not that the refusal of registration is a hardship but that the granting of it is a privilege . It should be borne in mind not only that Industrial and Provident Societies enjoy various advantages under their own Acts, that they pay no capital duty and are not subject to the prospectus provisions and other requirements of the Companies Act, but that under this Bill they are expressly exempted from the restriction on circularising which is imposed by Clause 10 and that they will of course continue to be free to advertise except as provided in Clause 8(2) in regard to existing societies. This pre-supposes that no society will be registered unless it establishes a special claim to the privileges conferred and unless it can safely be allowed to invite the public to invest its money in or through the society.

General.

Existing societies or classes of societies should be tested to see whether the proposals go far enough or go too far or are otherwise open to criticism. It is presumed that many societies and promoting organisations would alter their rules and/or practice so as to comply with the new conditions of registration.

It is important to collect evidence, with dates, where existing societies render themselves liable to cancellation by issuing invitations to the public after 26th July last.

/Applicants

Applicants seeking to register societies which may be cancelled under the Bill should have their attention drawn to Clause 8, and it may be desirable to bear the clause in mind when considering amendments of rules and model rules for societies which it is not intended to exclude.

Our own model rules (P. 50) and certain forms of Annual Return will no doubt have to be re-considered in due course from the point of view of assisting the Registrar in the exercise of his discretion as to registration and cancellation respectively.

ZR

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INDUSTRIAL AND PROVIDENT SOCIETIES ACT 1965

Registration of Societies

Societies which may be registered

1. A society qualifies for registration under the Act if

(*a*) it is a society for carrying on an industry, business or trade and

(*b*) it satisfies the Registrar that either

(1) it is a bona fide co-operative society or

(2) in view of the fact that its business is being or is intended to be conducted for the benefit of the community there are special reasons why it should be registered under the Act rather than as a company under the Companies Act.

Bona fide co-operative societies

2. There is no statutory definition of a bona fide co-operative society but such a society will normally be expected to satisfy the following conditions:—

(*a*) *Conduct of business.* The business of the society will be conducted for the mutual benefit of its members in such a way that the benefit which members obtain will in the main stem from their participation in its business. Such participation may vary in accordance with the nature of the society. It may consist of purchasing from or selling to the society, of using the services or amenities provided by it or of supplying services to carry out its business.

(*b*) *Control.* Control of the society will under its rules be vested in the members equally and not in accordance with their financial interest in the society. In general therefore the principle of " one man one vote " must obtain.

(*c*) *Interest on share and loan capital.* Interest payable on share and loan capital will under its rules not exceed a rate necessary to obtain and retain the capital required to carry out the objects of the society. The appropriate rate may vary from time to time between societies of different classes and according to the term and security of loans.

Section 1(3) of the Act provides that a society which carries on business with the object of making profits mainly for the payment of interest, dividends or bonuses on money invested with or lent to the society or any other person is not a bona fide co-operative society.

(*d*) *Profits.* The profits of the society's business after payment of interest on share capital, if distributable amongst the members, will under its rules be distributable amongst them in relation to the extent to which they have traded with or taken part in the business of the society. Thus in a retail trading society or an agricultural marketing society profits will be distributable amongst members as a dividend or bonus on purchases from or sales to the society. In some societies (as for example social clubs) profits will not usually be distributable amongst members but are ploughed back to cheapen and improve the amenities available to members.

(*e*) *Restriction on membership.* There should be no artificial restriction of membership with the object of increasing the value of proprietary rights and interests. There may, of course, be grounds for restricting membership that do not offend the co-operative principle; for example, the membership of a club might be limited by the size of its premises and of a self-build housing society by the number of houses that could be erected on a particular site.

Societies for the benefit of the community

3. To qualify for registration otherwise than as a bona fide co-operative society a society must satisfy two principal conditions:—

(*a*) that its business will be conducted for the benefit of the community and

(*b*) that there are special reasons why it should be registered under the Act rather than as a company under the Companies Act.

4. A society claiming that it will be conducted for the benefit of the community must be able to show amongst other things that it will benefit persons other than its own members and that its business will be in the interests of the community. Typical societies which qualify for registration in this category are those which provide housing for various groups within the community, some (although not all) being charitable or

philanthropic in character. In considering whether a society in this category should be registered regard will also be had to whether it is non-profit making and is prohibited by its rules from distributing its assets among members and to the matters referred to at (*b*), (*c*) and (*e*) in paragraph 2 above.

Other conditions of registration

5. Every society seeking registration under the Act must also satisfy the following conditions:—

(i) unless the society consists of two or more registered societies it must have at least seven members;

(ii) the rules of the society must provide for all the matters required by Schedule 1 of the Act (these matters are set out in detail in the form of application for registration, form A, which may be obtained on application to the Registrar); and

(iii) the proposed name of the society must, in the opinion of the Registrar, not be undesirable. (The Registrar is prepared to indicate in advance of a formal application for registration whether a proposed name is, at that time, available).

6. The Registrar's certificate only certifies that a society is registered. It implies that the rules are in accordance with the Act but not that they are prudent, clear or well drafted. The responsibility in these matters rests on the society and its advisers. Great care should therefore be taken to have the rules settled in proper form.

Procedure for registration

7. Applications for registration must be in accordance with the requirements of the Act and of the Regulations made thereunder. These requirements are referred to in form A (see paragraph 5(ii) above).

8. Model rules prepared by certain "promoting bodies" will be accepted by the Registrar for registration. Applications using these model rules must be submitted through and endorsed by the secretary of the body concerned. A list of promoting bodies (F.280) is obtainable from the Registrar on demand.

9. If model rules of a promoting body are not to be adopted the proposed rules should be submitted to the Registrar in draft form for preliminary examination. Where the proposed rules are a copy of or are based upon rules of another society registered under the Act this should be stated.

10. The rules finally submitted for registration should be proof prints in book form, duly signed. The size is immaterial provided that it is not larger than A4 (210mm. × 297mm.) but there should be an adequate inner margin for purposes of filing.

11. The fee payable for an acknowledgment of registry of a society under the Act will depend upon whether application is made under paragraph 8 above or not. A note of the current fee (F. 823) is obtainable from the Registrar on demand.

REGISTRY OF FRIENDLY SOCIETIES,
17, NORTH AUDLEY STREET,
LONDON, W1Y 2AP.

89885 Dd.8237830 5m 12/80 StS.

Appendix 4: Historic legislation

The Friendly Societies Act 1846 recognised "investment societies".[878] The Act provided:[879]

> … a Society may be established … for any of the following Purposes… (4) For the frugal Investment of Savings of the Members for better enabling them to purchase Food … or other Necessaries, or the Tools or Implements of their Trade or Calling, or to provide for the Education of their children or Kindred… Provided always, that the Shares in any such Investment Society shall not be transferable, and that the Investment of each Member shall accumulate or be employed for the sole Benefit of the Member … and that the full Amount of the Balance due … shall be paid to him or her on withdrawing from the Society…

The (first) Industrial and Provident Societies Act 1852 provided:[880]

> The Interest of any Member in any such Society shall not be transferable, but the whole Amount of the Balance due to any Member shall be paid to him on Withdrawal from the same according to the Rules of the Society.

The Industrial and Provident Societies Act 1862 stated that the "matters to be provided for in the Rules" of a society included:[881]

> (4) Determination whether the Shares shall be transferable, and in case it be determined that the Shares shall be transferable, Provision for the Form of Transfer and Registration of Shares and for the Consent of the Committee of Management and Confirmation by the General Meeting of the Society; and in case Shares shall not be transferable, Provision for paying to Members Balance due to them on withdrawing from the Society.

The Industrial and Provident Societies Act 1876 provided that the rules of a society were to include:[882]

> (7) Determination whether the shares or any number thereof shall be transferable; and if it be determined that the shares or any number thereof shall be transferable, provision for the form of transfer and registration of the shares, and for the consent of the committee thereto; and if it be determined that the shares or any of them shall be withdrawable, provision for paying the members the balance due thereon on withdrawing from the society.

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878 9 & 10 Vic c 27.

879 Friendly Societies Act 1846, s 1.

880 15 & 16 Vic c 31, s 3.

881 25 & 26 Vic c 87, s 4 and sch.

882 39 & 40 Vic c 45, s 9(1) and sch 2.

This was reworded slightly by the Industrial and Provident Societies Act 1893:[883]

> (7) Determination whether the shares or any of them shall be transferable; and provision for the form of transfer and registration of the shares, and for the consent of the committee thereto; determination whether the shares or any of them shall be withdrawable, and provision for the mode of withdrawal and for payment of the balance due thereon on withdrawing from the society.

[883] 56 & 57 Vic c 39, s 10(1) and sch 2.

Appendix 5: Director duties in the Companies Act 2006

Section 170 Scope and nature of general duties

(1) The general duties specified in sections 171 to 177 are owed by a director of a company to the company.

(2) A person who ceases to be a director continues to be subject—

(a) to the duty in section 175 (duty to avoid conflicts of interest) as regards the exploitation of any property, information or opportunity of which he became aware at a time when he was a director, and

(b) to the duty in section 176 (duty not to accept benefits from third parties) as regards things done or omitted by him before he ceased to be a director.

To that extent those duties apply to a former director as to a director, subject to any necessary adaptations.

(3) The general duties are based on certain common law rules and equitable principles as they apply in relation to directors and have effect in place of those rules and principles as regards the duties owed to a company by a director.

(4) The general duties shall be interpreted and applied in the same way as common law rules or equitable principles, and regard shall be had to the corresponding common law rules and equitable principles in interpreting and applying the general duties.

(5) The general duties apply to a shadow director of a company where and to the extent that they are capable of so applying.

The general duties

Section 171 Duty to act within powers

A director of a company must—

(a) act in accordance with the company's constitution, and

(b) only exercise powers for the purposes for which they are conferred.

Section 172 Duty to promote the success of the company

(1) A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—

(a) the likely consequences of any decision in the long term,

(b) the interests of the company's employees,

(c) the need to foster the company's business relationships with suppliers, customers and others,

(d) the impact of the company's operations on the community and the environment,

(e) the desirability of the company maintaining a reputation for high standards of business conduct, and

(f) the need to act fairly as between members of the company.

(2) Where or to the extent that the purposes of the company consist of or include purposes other than the benefit of its members, subsection (1) has effect as if the reference to promoting the success of the company for the benefit of its members were to achieving those purposes.

(3) The duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company.

Section 173 Duty to exercise independent judgment

(1) A director of a company must exercise independent judgment.

(2) This duty is not infringed by his acting—

(a) in accordance with an agreement duly entered into by the company that restricts the future exercise of discretion by its directors, or

(b) in a way authorised by the company's constitution.

Section 174 Duty to exercise reasonable care, skill and diligence

(1) A director of a company must exercise reasonable care, skill and diligence.

(2) This means the care, skill and diligence that would be exercised by a reasonably diligent person with—

(a) the general knowledge, skill and experience that may reasonably be expected of a person carrying out the functions carried out by the director in relation to the company, and

(b) the general knowledge, skill and experience that the director has.

Section 175 Duty to avoid conflicts of interest

(1) A director of a company must avoid a situation in which he has, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company.

(2) This applies in particular to the exploitation of any property, information or opportunity (and it is immaterial whether the company could take advantage of the property, information or opportunity).

(3) This duty does not apply to a conflict of interest arising in relation to a transaction or arrangement with the company.

(4) This duty is not infringed—

(a) if the situation cannot reasonably be regarded as likely to give rise to a conflict of interest; or

(b) if the matter has been authorised by the directors.

(5) Authorisation may be given by the directors—

(a) where the company is a private company and nothing in the company's constitution invalidates such authorisation, by the matter being proposed to and authorised by the directors; or

(b) where the company is a public company and its constitution includes provision enabling the directors to authorise the matter, by the matter being proposed to and authorised by them in accordance with the constitution.

(6) The authorisation is effective only if—

(a) any requirement as to the quorum at the meeting at which the matter is considered is met without counting the director in question or any other interested director, and

(b) the matter was agreed to without their voting or would have been agreed to if their votes had not been counted.

(7) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

Section 176 Duty not to accept benefits from third parties

(1) A director of a company must not accept a benefit from a third party conferred by reason of—

(a) his being a director, or

(b) his doing (or not doing) anything as director.

(2) A “third party” means a person other than the company, an associated body corporate or a person acting on behalf of the company or an associated body corporate.

(3) Benefits received by a director from a person by whom his services (as a director or otherwise) are provided to the company are not regarded as conferred by a third party.

(4) This duty is not infringed if the acceptance of the benefit cannot reasonably be regarded as likely to give rise to a conflict of interest.

(5) Any reference in this section to a conflict of interest includes a conflict of interest and duty and a conflict of duties.

Section 177 Duty to declare interest in proposed transaction or arrangement

(1) If a director of a company is in any way, directly or indirectly, interested in a proposed transaction or arrangement with the company, he must declare the nature and extent of that interest to the other directors.

(2) The declaration may (but need not) be made—

(a) at a meeting of the directors, or

(b) by notice to the directors in accordance with—

(i) section 184 (notice in writing), or

(ii) section 185 (general notice).

(3) If a declaration of interest under this section proves to be, or becomes, inaccurate or incomplete, a further declaration must be made.

(4) Any declaration required by this section must be made before the company enters into the transaction or arrangement.

(5) This section does not require a declaration of an interest of which the director is not aware or where the director is not aware of the transaction or arrangement in question.

For this purpose a director is treated as being aware of matters of which he ought reasonably to be aware.

(6) A director need not declare an interest—

(a) if it cannot reasonably be regarded as likely to give rise to a conflict of interest;

(b) if, or to the extent that, the other directors are already aware of it (and for this purpose the other directors are treated as aware of anything of which they ought reasonably to be aware); or

(c) if, or to the extent that, it concerns terms of his service contract that have been or are to be considered—

(i) by a meeting of the directors, or

(ii) by a committee of the directors appointed for the purpose under the company's constitution.

Section 178 Civil consequences of breach of general duties

(1) The consequences of breach (or threatened breach) of sections 171 to 177 are the same as would apply if the corresponding common law rule or equitable principle applied.

(2) The duties in those sections (with the exception of section 174 (duty to exercise reasonable care, skill and diligence)) are, accordingly, enforceable in the same way as any other fiduciary duty owed to a company by its directors.

Section 179 Cases within more than one of the general duties

Except as otherwise provided, more than one of the general duties may apply in any given case.

Section 180 Consent, approval or authorisation by members

(1) In a case where—

(a) section 175 (duty to avoid conflicts of interest) is complied with by authorisation by the directors, or

(b) section 177 (duty to declare interest in proposed transaction or arrangement) is complied with,

the transaction or arrangement is not liable to be set aside by virtue of any common law rule or equitable principle requiring the consent or approval of the members of the company.

This is without prejudice to any enactment, or provision of the company's constitution, requiring such consent or approval.

…

(4) The general duties—

(a) have effect subject to any rule of law enabling the company to give authority, specifically or generally, for anything to be done (or omitted) by the directors, or any of them, that would otherwise be a breach of duty, and

(b) where the company's articles contain provisions for dealing with conflicts of interest, are not infringed by anything done (or omitted) by the directors, or any of them, in accordance with those provisions.

(5) Otherwise, the general duties have effect (except as otherwise provided or the context otherwise requires) notwithstanding any enactment or rule of law.