



Legal Structures for Community Activity

This is one of a series of factsheets for voluntary and community groups issued by West Norfolk Voluntary and Community Action, WNVCA.

It offers a quick overview of the different legal structures which are available (with some of their advantages and disadvantages), and some issues around trading, and personal liability.

We have made every effort to ensure accuracy, but cannot be held responsible for decisions you take based upon our guidance. You are advised to take expert legal advice as appropriate.

1. Why does any organisation need a structure?

- So that decisions get made, and effective action can be taken
- For accountability both internally and externally
- For democratic reasons
- To fulfil its mission, aims and objectives.

Many organisations in the Voluntary and Community Sector, particularly small ones, are known in law as “unincorporated association”, enabling their administration to remain as simple and practical as possible. This structure is implicit when a group of people have come together over a common belief or ideal.

In the eyes of the law, the officers of the organisation are deemed to hold personal responsibility for their actions. Signatures on cheques and documents could be shown in a court of law.

As an organisation takes on more or new responsibilities, choosing the appropriate structure becomes increasingly important. Protecting staff, board members, volunteers and service users is vitally important and by ensuring the right foundation is in place enables the wider community and potential supporters to understand and be reassured as to how the organisation operates.

2. Legal structure options.

Some of the possible structures are

	Main features
*Unincorporated association	<p>A group of people with a common goal Simple set of rules, or governing document. The Management Committee has overall charge. Individuals are held responsible or “liable” if anything goes wrong.</p>
*Company limited by guarantee	<p>A group of people with a common goal The rules and aims are set out in “memorandum and articles of association” – has to register with Companies House, and send reports, and notify changes. Directors of the company have overall charge. Company is an entity for legal purposes – this limits the personal liability of officers/trustees - individuals usually pledge £1, and that is the limit of their liability, unless they act fraudulently. Can obtain “charity” status by applying to the Charity Commission. Can develop trading opportunities</p>
Industrial and Provident Society	<p>Membership owned, inherently democratic “one member one vote” Two types of IPS, either “bona fide co-operative” or a “society for the benefit of the community”. Normally two tier structure with a management committee accountable to a wider membership Administration and Registration with the FSA (Financial Services Authority) Lack of understanding and recognition for this structure can bring issues with gaining support from potential funders and partners.</p>
Community Interest Company	<p>Trading activity benefiting the community. Must have defined “social” aims, and this is protected by a mechanism called an “asset lock”. Trading and making “profit” Surpluses (or “profit”) invested back into the organisation and/or new activities. Pays full taxes and rates, and cannot be “charitable”.</p>
*Trust	<p>Usually an “unincorporated body” set up from an endowment by an individual to support (grant-aid) a chosen cause or causes. Requires a Trust Deed as its governing document. Single tier structure with no members Any trust which is seeking charitable status must have at</p>

	least three trustee's to meet Charity Commission requirements.
Charitable Incorporated Organisation	<p>The launch of the charitable incorporated organisation - a new legal form for charities – is currently delayed. It is now not expected to become available until late this year or early 2011.</p> <p>The key feature to this proposed new structure is that it will remove the need for those organisations wishing to adopt incorporated charitable status having to register with Companies House and the Charity Commission. CC will become the sole regulator.</p>

There are other commonly used descriptions of organisational types. These are not to be confused with legal structures which are governed either by the Companies Act or by Case Law.

*Social Firm, or Social Enterprise	<p>Put simply it is a way of working This is not a defined structure – it is a generic term for organisations with characteristics of.</p> <ul style="list-style-type: none"> • Social ownership • Trading • Social objectives <p>Activity benefiting the community Trading and making “profit” Members, employees, or service-users come from the disadvantaged/beneficiary community Will adopt a structure as appropriate, e.g. company limited, co-operative, community interest company. May or may not be charitable.</p>
*Wholly owned subsidiary of a voluntary/ community organisation (Trading Arm)	<p>Undertakes trading activity under the ownership and control of the parent organisation – sometimes called a trading arm. Will have its own structure, e.g. company limited, co-operative, community interest company.</p>
Co-operative	<p>Activities are done for mutual benefit of the members (members can achieve something together which they couldn't do separately) Controlled by its members It is an Industrial & Provident Society – regulated by the Financial Services Authority, and can secure “charity” status from Inland Revenue.</p>

3. Charitable status

Those marked with * are able to take on “charity” status.

Charity Status has the advantages of:

- tax benefits
- fundraising benefits, potential wider appeal to funders.
- Image and credibility with the public.
- external support

The main disadvantages/problem areas are

- can't pay trustees, except under certain limited conditions
- can't change aims or rules without permission from Charity Commission
- trading is only allowed if in direct pursuit of the objects (i.e. the stated aims of the charity).
- loss of flexibility in terms of accountability to the Charity Commission
- additional administrative burden, annual reporting.

4. Trading

Charities can carry out trading activities

- where they contribute directly to their objects (i.e. the stated aims of the charity), known as primary or ancillary trading, or
- where they raise funds for the charity and do not involve significant risk.

Such activities will be exempt from corporation tax, so long as the profits go to the purposes of the charity.

If trading activities make a loss, the Trustees will need to answer whether they made a sensible decision to enter into trading.

Note: charities are able without restriction to sell or hire donated goods. This does not count as trading, and is zero-rated for corporation tax and VAT.

Examples of trading activity by charities are

- sale of goods manufactured by disabled people – by a disabled persons' charity
- sale of tickets for a theatre production by an arts or theatre charity
- sale of books, promotional pens, mugs and tea towels by a museum charity
- coffee/sandwich shop run by community centre.

Conducting a lottery counts as trading. However it is exempt from corporation tax, so long as it complies with section 3 (small lottery), or section 5 (society's lottery) of the Lotteries and Amusements Act 1976.

Any organisation, charitable or not, must register for VAT if its trading income exceeds £54,000 per year in any one quarter.

A charity must set up a trading subsidiary

- where the trading activity would involve significant risk to the assets of the charity itself.

It may also be beneficial to set up a trading subsidiary

- so that the administration is separate, or
- to reduce tax liabilities. However you should seek detailed advice on this.

Trustees should always put the interests of the parent charity first.

See Guidance info from the Charities Commission (CC35 Trustee's Trading and Tax)

5. Liability

Trustee liability - in a company limited, individuals only have limited personal liability if things go wrong – usually limited to £1.

Unincorporated Associations (most voluntary organisations) don't offer this protection. As a result Trustees (Management Committee members) can be personally liable to

- make good losses resulting from their actions
- be responsible in law for failings of the organisation.

The best ways to reduce risk/liability are to

- act openly, honestly and reasonably
- act within the governing document (constitution, or memorandum and articles of association)
- seek (financial and legal) information and advice before making decisions
- declare an interest where appropriate
- ask Charity Commission for advice when in doubt.

It is also possible to take out Trustee Indemnity insurance – see below.

Trustee indemnity insurance can help protect Trustees in situations where genuine mistakes were made in

- using funds outside the charity's objects or powers, or
- making poor investments.

It will not cover for

- losses where Trustees acted dishonestly, or in (reckless) disregard of their responsibilities
- liabilities to third parties e.g. breach of contract, redundancy payments, negligence

- penalties/fines for breach of statutory duty.

Some people argue that Trustee Indemnity Insurance is a waste of money, because

- it only covers aspects which most groups would be unlikely to have problems with, and
- any serious liability is not covered in any case.

Charity Commission advice is

- undertake proper risk assessments
- provide good internal procedures, to prevent the need for Trustee Indemnity
- if you do consider taking out Trustee Indemnity, check the policy carefully to be sure that the cover obtained is worth having.

This information has been produced by West Norfolk Voluntary and Community Action set up and owned by local groups to support, promote and develop local voluntary and community action.

We have taken all reasonable steps to make sure that this information is current and accurate. We cannot, however, guarantee its accuracy or completeness and therefore cannot accept liability for your acting, or failing to act, on the information given.

For resources, books, ideas and useful information please contact West Norfolk VCA or email info@westnorfolkvca.org.