

## OVERVIEW

### 1. What is a community interest company?

A community interest company (CIC) is a limited liability company with the specific aim of providing benefit to a community. This legal form can be adopted by a range of social enterprises and 'not-for-profit' projects serving communities throughout the UK, which combine the pursuit of a social purpose with commercial activities.

Social enterprises can comprise of partnerships between local authorities, businesses and other stakeholders working for the community's benefit – for example, in operating day care centers, out of hours GP care, waste recycling, local transport or the provision of low-cost work units for start-up businesses.

A CIC is incorporated under the Companies Act 1985 by the Registrar of Companies and has to conform to company and insolvency law in the same way as other UK companies. The level of governance, the members rights and duties and the statutory filing requirements, all adhere to UK and European company law and guidelines, including rules on insolvency, accountancy, and governance, in the same way as any other UK company. Listed CICs have to comply with the Combined Code on Corporate Governance, or any other codes (such as those issued by institutional investors).

### 2. What are the key features of this legal form?

The "community interest company" brand is distinctive in describing a company working for the benefit of the community. The CIC also has the advantage of the "company" legal form, which is familiar and well understood by the business community and it is flexible enough to adapt to most organisational structures, membership or governance from a single member company to a co-operative.

CICs can be companies limited by guarantee or limited by shares. A CIC limited by guarantee is a 'not for profit' company.

CICs will be able to take advantage of the risk-taking features of a company and can access the debt market for loans and bonds. If limited by shares it may be able to expand through the selling of shares. Also there is no limit to the level of profit a CIC is allowed to make as this profit will be used to benefit the community it was set up to serve.

If a CIC limited by shares aims to make profit that profit can (under certain checks and balances) be distributed to its members (who may or may not form part of the requisite community).

The CIC is quick, easy and inexpensive to set up. This is because unlike a non-charitable company, the CIC has statutory clauses, which include an asset lock. These clauses provide legal protection against demutualisation and 'windfall profits' being paid out to its members and directors, without all the necessary checks and balances of mutuality or charitable status.

There is greater transparency of operation as a CIC has to deliver an annual community interest company report about its activities for the public record, which includes details of assets transferred for less than market value; dividends paid; and directors' remuneration.

Stakeholder involvement is integrated into its governance through its annual community interest report.

The CIC has greater flexibility compared to a charity in terms of its activities. It does not have trustees and its directors can receive reasonable remuneration. There are no tax advantages so regulation is light touch, a balance of minimal regulation whilst maintaining confidence in the "CIC" brand.

A community interest company has continuity of purpose once it is incorporated it will continue in existence until it is either dissolved, or converted to a charity. If it is dissolved the residual assets will be preserved for the community rather than distributed to members. So a CIC may find Community Finance Institutions a valuable source of funds.

### 3. Additional requirements for a community interest company

In addition to the requirements on ordinary companies a CIC has to:

- Satisfy and continue to satisfy a community interest test.
- Adopt certain statutory clauses in its constitution (this includes a clause to lock in the assets to providing benefit to the community), and
- Deliver an annual community interest company report with its annual accounts

### 4. How do you form a community interest company?

The formation and registration is similar to that of any limited company. New organisations can register by filing the Form 10, Form 12 and memorandum and articles of association together with a form CIC36 signed by all their directors, explaining their community credentials to the Registrar of Companies for England and Wales, or the Registrar for Scotland with a fee of £35. Existing companies can convert to a CIC by passing resolutions which make changes to their name and to their memorandum and articles of association and by delivering to the Registrar of Companies copies of these documents, together with a fee for £25, and a form CIC37 (which is similar to a CIC36, but asks for confirmation that the company is not a charity, or that permission has been obtained from the Charity Commission to convert). The Registrar will conduct the normal checks for registration and pass the papers to the Regulator of Community Interest Companies, to determine whether the company satisfies the community interest test. It should be noted that a CIC cannot be politically motivated; set up to serve an unduly restrictive group; or be a charity; and its activities must be lawful.

All these forms, model memoranda and articles of association together with an explanation of the procedure and worked examples can be found on our website [www.cicregulator.gov.uk](http://www.cicregulator.gov.uk), using the 'FORMS' tab.

### 5. The community interest test (Forms CIC36 & CIC37)

A CIC has to make a community interest statement for the public record describing what it will do, who it will help and how. If it makes a profit, or surplus, what the company will do with it. This information is provided on a form CIC36 or CIC37 and is placed on the public record after incorporation.

Based on this statement the Regulator decides whether an organisation is eligible to become a community interest company. This statement sets on the record in a transparent manner the purpose, the activities and desired outcomes for the CIC going forward, which are overseen by regulation throughout the life of the company.

## 6. The statutory clauses (memorandum and articles of association or constitution)

A community interest company's articles contain certain statutory clauses:

- To lock in the assets to benefiting the community it was set up to serve.
- To prevent the CIC falling under the control of individuals, or organisations, who are not members.

These clauses, including the “asset lock”, are overseen by regulation and cannot be removed from its constitution. It is this that sets it apart from other companies and prevents demutualisation and windfall profits being paid out to its members and directors.

## 7. The statutory “asset lock”

A community interest company's assets can only be distributed for less than the market value to another asset locked body, such as, a CIC or charity or to benefit the community it was set up to serve.

Once a CIC is incorporated it will continue in existence unless it converts to a charity or is dissolved. If the company is dissolved, any assets remaining after distribution will be transferred to another asset locked body, such as, a CIC or charity to be used for a similar community purpose.

A CIC limited by shares, which adopts the appropriate clauses in their articles, and subject to company law requirements, may pay a dividend on shares if agreed by a resolution of its members.

Dividends payable to certain types of shareholders (non-asset locked bodies e.g. not a charity or CIC) will be subject to a dividend cap. The cap is, at present, a maximum dividend per share of 5% above the Bank of England base rate and a maximum aggregated dividend of 35% of the distributable profits. Unused dividend capacity can be carried forward for 5 years. There is also a cap on performance-related interest of 4% above the Bank of England base rate.

For example:

If a community interest company had 3 shareholders each holding a share with a paid up value of £1 and the Bank of England base rate was 6%. The maximum dividend per share would be  $£0.11p \times 3 = £0.33p$  aggregated dividend.

If the CIC had distributable profits for the year of £300 the maximum aggregated dividend would be  $£300 \times 35\% = £105$ . As the £0.33p is well within the maximum aggregated dividend of £105 (and the members had agreed to the distribution) the CIC could pay an aggregated dividend of £0.33p. For more detailed examples see Annex G of the guidance on our website

[www.cicregulator.gov.uk](http://www.cicregulator.gov.uk)

The asset lock will not affect the ability of community interest companies to use their assets in the normal course of business. For instance, they will be able to use their assets as collateral for finance, and if they do so, the assets will be available to creditors in the event of default.

## 8. Director's and member's responsibilities

As with any other company, general company law imposes, on directors, a range of duties and other responsibilities. In addition to these general responsibilities CIC directors (and, for collective decisions the members) are also responsible for ensuring that the company is run in

such a way that it will continue to satisfy the community interest test, which is overseen by regulation.

#### 9. Annual community interest company report and accounts

Whatever membership, structure, or governance is adopted, it is up to the directors and members to ensure it is complied with and is in the best interest of the CIC and its community. This is overseen by regulation.

To this end a CIC must deliver to the Registrar of Companies with its annual accounts a community interest company report, both documents are placed on the public record. The CIC report provides transparency of operation and describes:

- How the company's activities have benefited the community
- What steps were taken to consult stakeholders and what was the outcome
- What payments were made to directors
- What assets were transferred other than for full consideration
- What dividends were paid
- What performance-related interest was paid on loans or debentures

The involvement of stakeholders is overseen by regulation and is integrated into the corporate governance of the CIC through the annual report.

#### 10. Director's remuneration

Community interest companies have the option to pay their directors remuneration. This too is overseen by regulation. The community interest test and the asset lock apply as much to the remuneration of directors as to any other area of a CIC's business.

Directors' remuneration should never be more than is reasonable and remuneration arrangements should always be transparent. General company law rules apply and there needs to be legal authority (approval by the members, or provided for in the company's memorandum or articles of association). The primary discipline on CIC directors' remuneration arrangements is transparency and stakeholder influence or approval.