CO-OPERATIVES UK

Position paper

Co-operative and Community Benefit Societies (Environmentally Sustainable Investment) Bill

June 2020

Key points

- **Green Shares Bill contains three much-needed legislative changes that would further enhance the contribution co-operative and community benefit societies make to sustainable and inclusive economic development**
- **But the Green Shares Bill must also be amended in key ways to be of practical value. In current form, parts of the Bill would be impractical and counterproductive.**
- **We urge MPs and Government to support the passage of the Green Shares Bill to Committee Stage, where it can be amended as necessary**

1 Summary of position

1.1 The Co-operative and Community Benefit Societies (Environmentally Sustainable Investment) Bill (referred to hereafter as the 'Green Shares Bill') is a rare opportunity to give co-operative and community benefit societies (hereafter referred to as 'societies') a first class legal framework. The Green Shares Bill includes some positive changes to society law that would significantly enhance these corporate forms, as tools to build the more sustainable and inclusive economy we urgently need. **But the Green Shares Bill must be amended in key ways to be of practical value. In current form it would be impractical and counterproductive.**

1.2 We very much welcome the focus on societies in the Green Shares Bill. Primary legislation is badly needed to provide societies with legal tools found in the most effective co-operative law codes around the world. Opportunities for such primary legislation are very rare.[1]

1.3 The Green Shares Bill introduces a number of new *optional* legislative features that evidence suggests would add significant value, while also being requested by many societies.[2] These are:

- Repayable share capital – see Green Shares Bill **1** (3) **27B** [3]

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[1] Aside from the 2014 consolidation legislation (which could not be used to make material changes to the law) and a handful of Private Members' Bills of limited scope, the last significant government-initiated primary legislation that made substantial changes to society law was in 1954.

[2] We have recently consulted societies on their priorities for legislative action - see outcome here

[3] International research provides a useful insight into value of repayable shares – see here

- Non-distributable capital surplus – see Green Shares Bill **1** (4) **29A** [4]
- Restrictions to conversion of society into a company – see Green Shares Bill **1** (7) **11A**

1.4 However, we believe the way in which **1** (3) 27A of the Green Shares Bill restricts use of these valuable new features to only societies that are *"raising external capital to make environmentally sustainable investment"* would be impracticable and counterproductive.

1.5 As introduced, the Green Shares Bill would restrict rather than expand the scope for societies to take on mission-aligned investment for environmental and social purposes. And it would restrict rather than expand societies' ability to protect and enhance their environmental, social and economic impacts.

1.6 We therefore urge MPs and government to support the passage the Green Shares Bill to Committee Stage, where it can be amended to make it useful for societies.

1.7 Co-operatives UK and partners such as Mutuo have already built well-evidenced cases for the positive measures listed in 1.3. And experts in society law have already drafted provisions for these measures. This will greatly reduce the demands on the Committee and government.

2 Purpose and impact of co-operative and community benefit societies

2.1 The co-operative and community benefit society corporate forms exist to facilitate business with mutual and social purpose and democratic ownership and governance. These businesses are a cornerstone of the UK's social economy and have huge potential to deliver sustainable and inclusive economic development.

2.2 Many societies have clear purposes relating to environmental sustainability. This includes community energy schemes, e-car sharing co-operatives, low impact farming co-operatives and low impact community-led housing. And a significant number of these have raised, or are currently raising, equity investment from communities of place and/or interest.[5]

2.3 Beyond this, the majority of societies either have supplementary purposes or make commitments in the Rules relating to environmental sustainability. In practice these give rise to business models, directors' duties and clear accountabilities that aim to avoid and reduce environmental harms.

3 Green Shares

3.1 Green Shares Bill **1** (3) 27A establishes that societies could only use the new repayable share instrument (and by extension the features protecting capital surplus and purpose) if they are *"raising external capital to make environmentally sustainable investment".* Green

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[4] See our evidence paper for more on non-distributable capital surplus

[5] They currently do so using the most useful equity instrument currently available to societies: withdrawable share capital, usually using the 'Community Shares' financing model

Shares Bill **1** (3) 27A also provides a legal definition for 'environmentally sustainable investment'.

3.2 There is good evidence that a new repayable share instrument would add value for societies and is needed. Co-operatives UK supports such a change. But the way in which **1** (3) 27A of the Green Shares Bill restricts use of repayable shares to only societies that are *"raising external capital to make environmentally sustainable investment"* would be impracticable and counterproductive. We explain why below.

Environemtally sustainable investment

3.3 We fully support the intention to facilitate and encourage the allocation of capital to businesses that reduce environmental harms. But we do not believe it is practicable to attach such conditions to the use of a particular co-operative and community benefit society equity instrument.

3.4 In many cases repayable shares would be a useful tool for societies with strong environmental and social purposes to raise equity investment for general purposes, rather than for distinct environmental sustainability projects. We are concerned that this may not be permitted by **1** (3) 27A of the Green Shares Bill.

3.5 Furthermore societies may also find it useful to issue repayable shares to their existing members, rather than external investors, which it seems would not be permitted by **1** (3) 27A of the Green Shares Bill.

3.6 Furthermore, to be effective, such conditionality would presumably require a robust new certification process, which would not be cost effective given the relatively small number of societies that might issue such shares in the beginning.

3.7 Rather than increasing the amount capital allocated to environmentally sustainable investments, the conditionality of the Green Shares Bill would probably reduce scope for such investment.

3.8 If the intention is for more societies to be raising more capital for environmentally beneficial activities, then legislation should provide capital raising options that are practically useful for many societies in many contexts, rather than a small number in limited circumstances. We believe efforts to increase the allocation of capital to environmentally sustainable businesses, should focus on increasing the reach and impact of 'Environmental, Social, and Governance (ESG)' investing instead.

Repayable share capital

3.9 However, we do believe the Co-operative and Community Benefit Societies Act should be amended to give societies the option of issuing shares that repayable at the option of the society, rather than withdrawable at the option of the shareholder, along the lines set out in **1** (3) 27B. But for the reasons set out in 3.3 to 3.9 above, in would be counterproductive to limit use the new equity instrument in the ways set out in **1** (3) 27A of the Green Shares Bill.

3.10 A repayable share instrument would enhance the ability of societies to raise equity investment in more significant amounts, from both members and, crucially, from external investors including institutions. Repayable shares would provide investors with a straightforward, non-market exit, which would be compatible with co-operative and

community purposes, while also providing complete certainty in capital planning for the society.

3.11 A new repayable share instrument is also needed in addition to the existing withdrawable share capital instrument, because the latter has a £100,000 maximum shareholding limit per investor[6], which is problematic for some larger societies.

3.12 Clarity in legislation would also remove the risk that a repayment of share capital by the society (rather than a withdrawal by a shareholder) could be challenged under Trevor vs Whitworth case law.

4 Non-distributable capital surplus

4.1 We also believe the Co-operative and Community Benefit Societies Act should be amended to include an *optional provision* for 'non-distributable capital surplus', along the lines of **1** (4) **29A** of the Green Shares Bill. This option would be especially useful to co-operative societies, which currently lack any kind of 'statutory asset lock'. Such legislation would provide a legal guarantee that capital surplus in a co-operative society will be committed to co-operative purpose. This would help encourage more of the endeavour, participation, support and investment needed for these businesses succeed. It would enable founders to apply the proven combination of a clear purpose, mission-aligned investment and a statutory 'asset lock', in a business that focuses on mutual benefit and shares profits as a reward for participation. This in turn should end a distortion in behaviour that leads some founders to make suboptimal choices of legal form. Such legislation would also boost the long-term resilience of societies.[7]

4.2 However, these benefits will not come about if use of non-distributable capital surplus is restricted to only societies that that are *"raising external capital to make environmentally sustainable investment".* Most societies that might want to use such a provision are not in a position to issue repayable shares to external investors. And where they are, the issues set out in 3.3 and 3.9 will also apply.

5 Restrictions to conversion of society into a company

5.1 We believe there is value giving co-operative societies the *option* of adopting a provision which legally prevents future conversion into a company, along the lines of Green Shares Bill **1** (7) **11A**. Such legislation would provide a legal guarantee that the mutual and social purposes of co-operative societies are protected. This would help encourage more of the endeavour, participation, support and investment needed for these businesses succeed. Such legislation would also boost the long-term resilience of co-operative societies.

5.2 However, these benefits will not come about if use of the 'conversion restriction' is only available to societies that are *"raising external capital to make environmentally sustainable*

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[6] http://www.legislation.gov.uk/ukpga/2014/14/part/2/crossheading/maximum-shareholding

[7] See our evidence paper for more on non-distributable capital surplus

investment". Most societies that might want to use such a provision are not in a position to issue repayable shares to external investors. And where they are, the issues set out in 3.3 and 3.9 will also apply.

6 Our preferred way forward: amending the Bill

6.1 Given that opportunities to make primary legislation for societies are very rare, we urge MPs and Government to support the passage of the Green Shares Bill to Committee Stage, in order that it be amended, so that it can be made useful for societies.

6.2 We urge that in Committee the Green Shares Bill be amended so as to:

- Retain provisions for repayable shares, non-distributable capital surplus and prevention of conversion to a company, while removing provisions that restrict the use of these tools to only societies issuing repayable shares to external investors for environmentally sustainable investment
- Replace the 'environmentally sustainable investment' restrictions of **1** (3) 27A with a requirement to issue repayable shares using the more practicable 'Environmental, Social, and Governance (ESG)' framework

6.3 If amended as above, the Green Shares Bill would significantly enhance the society corporate forms as tools to build the more sustainable and inclusive economy we urgently need.

6.4 Co-operatives UK and partners such as Mutuo have already built well-evidenced cases for the positive measures listed in 1.3. And experts in society law have already drafted legislative provisions for these measures. This will greatly reduce the time demands on the Committee and government.

Contact

James Wright, Policy Officer

e: james.wright@uk.coop

t: 0161 214 1775

About Co-operatives UK

Co-operatives UK is the national association of co-operative businesses. We have over 800 co-operatives in direct membership, including leading consumer co-operatives, worker owned businesses, community businesses and farmers' co-operatives.