Creating a subsidiary organisation

In-depth guide

CO-OPERATIVES UK

Subsidiaries

A co-operative could create a subsidiary for a variety of reasons. These include separating risk from the main organisation – or for strategic reasons it may be sensible to hive off activities into a subsidiary so that the main organisation can concentrate on delivering its own purposes.

What is a subsidiary?

Under section 1159 of the Companies Act 2006, a company is a subsidiary of another company (its 'parent company') if the parent company:

- Holds a majority of the voting rights in the subsidiary **and/or**
- Is a member of the subsidiary and has the right to appoint or remove a majority of its Board of Directors **and/or**
- Is a member of the subsidiary and controls alone, in agreement with other members, a majority of the voting rights **and/or**
- Is a parent company of an intermediate company and this intermediate company is the parent of the subsidiary

A company is a 'wholly-owned subsidiary' of another company if its only member is the parent company.

Why would a co-operative consider creating a subsidiary?

Where one or more subsidiaries are controlled by a parent company, a group structure is said to exist. A co-operative may be part of a group structure when:

- It plans to take on a new area of work, and although potentially lucrative, it doesn't meet the purposes of the co-operative. The members may decide to establish a subsidiary to undertake this new area of work
- It is carrying out numerous activities and is struggling to accommodate them all under the one business. Separating out different activities into separate subsidiaries may help the co-operative regain its focus
- It may want to start a new or unfamiliar project and the creation of a subsidiary reduces the risk of the failure of the co-operative if this new project fails

What are the advantages of creating a subsidiary?

- Enables the parent company to focus on its primary activities
- May avoid unwanted VAT registration by reducing the trading income of the parent company. VAT registration is compulsory when trading income reaches a certain level
- Enables risks to be managed. Separating activity out into other companies reduces the risk to the parent company
- Enables charitable organisations to separate its charitable activities from its non-charitable activities. For example, to carry out non-primary purpose trading or political campaigning

What are the disadvantages of creating a subsidiary

- Costs – these include fees for registration of another company or companies as well as ongoing administrative fees associated with preparing and filing group accounts with Companies House
- Tax benefits – if the parent company is a charity the subsidiary will not be able to enjoy the same tax benefits as the charity and it will not be able to use the charity's registration number
- If the parent company is a charity and one or more of the trustees of the charity wish to sit on the governing body of the subsidiary he/she will not be able to receive wages for work carried out for the subsidiary
- Loss of control – subsidiaries can become remote from the parent company and drift away from the original aims

Creating a subsidiary

It is relatively easy to set up a subsidiary company. It is necessary to incorporate a separate company with Companies House, but caution should be taken to ensure that the governing document is drafted to include those elements outlined in section 1159 of the Companies Act 2006 (see the 'What is a subsidiary?' section of this guide).

Co-operatives UK has a model governing document for a wholly owned company limited by guarantee and provides a registration service for prganisations seeking to create a subsidiary company. Email advice@uk.coop for more information or visit www.uk.coop.

Essential reading

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