

Policy Briefing

Siting the legislative and registration functions for co-operative and community benefit societies

October 2016

Summary of points:

- In form and function co-operative and community benefit societies are specifically intended to empower people in the economy, thus if the UK is to have a more Inclusive Economy and strong social sector these corporate forms will need to multiply and thrive
- The current siting of responsibility for co-operative and community benefit societies in government is illogical and dysfunctional (see **part 2**)
- Responsibility should move from HMT to BEIS (see **part 3**)
- There are good fiscal and organisational reasons for moving the registration function for co-operative and community benefit societies out of the FCA and into a new consolidated 'social economy registrar' (see **part 4**)
- There is broad support for such an overhaul (see **part 5**)

1 Background

- 1.1 More by historical happenstance than logical design, legislative responsibility for co-operative and community benefit societies sits within the Banking and Credit Team of HM Treasury (HMT) rather than within the Business Frameworks directorate of the Department for Business Energy and Industrial Strategy (BEIS). A related consequence of this arrangement is that the registrar function for these businesses is sited within the Financial Conduct Authority (FCA).
- 1.2 Co-operative and community benefit societies are incorporated under the Co-operative and Community Benefit Societies Act. There are almost 8,000 such societies, comprising a diverse range of businesses and entities including consumer-owned retailers, farmer-owned businesses, employee-owned business, community enterprises and housing associations, among many more.
- 1.3 Co-operative and community benefit societies currently form part of a broader family of mutual legal forms, comprising building societies, credit unions and friendly societies, known as 'mutual societies.' Crucially co-operative and community benefit societies are different from all the others in that they are not forms of legal incorporation used specifically to create defined financial

mutuals. Rather, co-operative and community benefit societies share a key characteristic of the company and community interest company legal forms, in that they can be used in almost every imaginable sector, but with the proviso that they must trade as co-operatives or for communal benefit.

2 The problem: fragmented policymaking

- 2.1 While in theory BEIS is responsible for creating an enabling corporate framework for UK businesses, in practice it has no part in legislating or policymaking for co-operative and community benefit societies (hereafter referred to as 'societies'). Instead this is the responsibility of HMT officials. While these officials are a great help when they can be, they serve a department dedicated to financial services and fiscal policy, so time and again even societies' most basic policy needs are crowded out.
- 2.2 Over decades it has proven very hard to get even routine maintenance of the legal framework done, let alone more strategic reforms. While in 2014 a commitment in the Coalition Agreement¹ resulted in welcome consolidation law and some useful secondary legislation, these changes were long overdue. For example, by 2014 archaic limits on individual holdings in share capital had become extremely restrictive and costly for many large farmers' co-operatives.² Piecemeal improvements at irregular intervals do not compare well with the regular good work government does to maintain and improve the company corporate framework.
- 2.3 The society corporate framework needs updating, is clunky, and in some places is outright dysfunctional. Key issues at present include:
- The need to review and update account reporting and audit requirements for small societies
 - The need to provide smoother less burdensome compliance processes for societies, especially in relation to the Mutuals Register and HMRC
 - The need to tidy up dysfunctional red tape in the asset lock regulations for community benefit societies
 - The need to fully adapt company insolvency provisions for use by societies, so that these can apply immediately without requiring government to intervene on a case-by-case basis
 - The need to provide straightforward and appropriate conversion routes between the society legal forms and other forms of incorporation

¹

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/78977/coalition_programme_for_government.pdf

² http://www.uk.coop/sites/default/files/uploads/attachments/capital_constraints_final_research1.pdf

- The need to provide an optional statutory asset lock for co-operative societies
- 2.4 Stakeholders tell us there other areas of society law that require review to ensure we continue to enable forms of co-operative and social innovation. These include the rules governing the distinction between co-operative and social purpose and the available forms of share capital. In light of a very costly and ongoing penalisation of mutual employers in the Pension Protection Fund,³ the statutory basis for the recording of charges may also need to be reviewed.
- 2.5 Furthermore this fragmentation of responsibility across government has meant that some key great initiatives brought forward by BEIS, to improve the business environment and to support entrepreneurship and enterprise, fail to benefit societies. Examples include the registrar of societies not having a Growth Duty or a specific Business Impact Target, and societies even being arbitrarily excluded from some schemes, as they were from the now concluded Growth Vouchers programme.⁴
- 2.6 This makes societies a less user-friendly legal option, with added burdens for smaller entities and less scope to adapt some of the best co-operative practices from around the world. We are particularly concerned by examples, brought to our attention by business development workers, of co-operative entrepreneurs making suboptimal choices in legal form because of shortcomings in the society corporate framework.

3 The solution: siting responsibility in BEIS

- 3.1 Government should move legislative and policymaking responsibility for co-operative and community benefit societies from Banking and Credit in HMT to Business Frameworks in BEIS. The BEIS policy brief confirms that responsibility for co-operative and community benefit societies would be better sited there. Its mission is to cement the UK's position as the best place in Europe to start and grow a business by supporting local growth and entrepreneurs. BEIS is responsible for maintaining and improving the business environment; ensuring legal and regulatory frameworks are balanced and enabling, while making sure markets function properly. The problem is that in practice much of this either excludes or otherwise marginalises societies.
- 3.2 If responsibility were to move to BEIS, societies will be served by officials with a specific business framework remit, rather than by officials in HMT responsible for financial services. While this would certainly not be a panacea allowing instant improvements to the society frameworks, seeking action

³ See here: <http://www.uk.coop/pension-protection-fund>

⁴ https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/349232/bis-14-1501-growth-vouchers-programme-terms-and-conditions-participants.pdf

through departmental and ministerial channels with these specific remits would constitute a considerably lesser challenge compared with the status quo.

- 3.3 Furthermore we believe that once BEIS has practical responsibility for the society legal form it will be easier for this to be maintained alongside the company legal form as matter of course, reducing future disparities. It will also become less likely that societies are unwittingly or unnecessarily excluded from agendas and schemes to support business.
- 3.4 We recognise that as the other mutual society legal forms are specifically financial in nature, HMT Banking and Credit would prefer to retain responsibility for these.

4 The registrar function

- 4.1 While the siting of the registrar function for societies is not our primary concern, we anticipate that moving the legislative function across Whitehall would most likely require a complementary move of this function out of the FCA. This could also be very beneficial.
- 4.2 The registrar function is carried out by the FCA Mutuals Team, which also acts as registrar for the other mutual societies (building societies etc.). It is important to recognise that while these other forms of society are financial in nature, and while the Mutuals Team sits within the Authorisations Division of the FCA, the Mutuals Team is not a financial services regulator. Indeed, particularly where the registration of co-operative and community benefit societies is concerned, the function is more akin to that of Companies House, with some more regulatory functions comparable with those of the Community Interest Companies Regulator and the Charity Commission, which prevent the legal forms being misused.
- 4.3 In practice the Mutuals Team has considerable discretionary powers in relation to societies. It performs its role diligently but because it is situated inside the FCA an institutional focus on entrepreneurship, cutting red tape and sector growth is sometimes lacking. We have concerns that while the FCA's mission, culture and structures may be suited to regulating a large and complex financial sector, they do not serve the best interests of societies as commercial entities with co-operative and communal objectives.
- 4.4 Whereas Companies House, the Community Interest Companies Regulator and the Charity Commission have clear institutional missions and frameworks centred on registering economic entities, and where necessary regulating their social or charitable nature, the siting of a comparable function within the FCA does not produce anything similar for societies. Unlike these other registrars, the Mutuals Team has no Business Impact Target or Growth Duty. We also find there are issues with institutional accountability and oversight for the

Mutuals Team within the wider FCA. Furthermore societies are not currently offered a clear process for challenge and redress. Given the degree of discretionary power the Mutuals Team has, and the fact that there are times when its regulatory policy and approach prove controversial, these issues are especially problematic.

- 4.5 We are also concerned that the current siting of the registrar function suffers from diseconomies of scale, which has costly consequences for many stakeholders. For instance the Mutuals Register is clunky and expensive to access. It costs £12 to access data on a society that would be free in relation to companies, community interest companies and charities. This is a significant additional cost to key stakeholders such as banks, credit reference agencies and those carrying out due diligence on societies. Furthermore, unlike companies, community interest companies and charities, societies have not been provided with an online portal that would allow them to easily update details on the Mutuals Register. This creates additional bureaucracy for both societies and the FCA, which puts extra strain on the limited capacity of the latter and results in increased regulatory costs, as well as delays which often make the Mutuals Register inaccurate.
- 4.6 Moving the registrar function for co-operative and community benefit societies to a consolidated 'social economy registrar', with hard links to Companies House and its 'Beta' service, under the oversight of BEIS, is an attractive proposition. It could provide important economies of scale resulting in more efficient processes, better service and lower regulatory costs. It could also support the development of a fit for purpose institutional remit and approach, aimed at helping people set up and run 'regulated legal forms'⁵ while properly guarding against their misuse.

5 Sector support

- 5.1 We believe there is strong support among societies and stakeholders for moving the legislative function from HMT to BEIS and for moving the registration function out of the FCA into a consolidated social economy registrar. This is certainly the view of many expert bodies which advise societies and seek to shape policy on their behalf.⁶
- 5.2 To ascertain support among our member businesses we have been running an online consultation. So far all 56 respondents have expressed support, representing a very diverse range of societies including large retailers like Midcounties Co-operative, public health mutuals like Unlimited Potential, large

⁵ Legal forms which, like companies, operate across the economy, but which are also regulated to ensure they operate in particular ways: co-operative and community benefit societies, community interest companies, charities.

⁶ For example, law firm Bates Wells & Braithwaite LLP: <http://www.bwbllp.com/file/fca-call-for-input-submission-of-bates-wells-and-braithwaite-london-lp-14-3-16-pdf>

public sector spin-outs like Leading Lives and employee-owned businesses like Unicorn Grocery.⁷

6 Concluding remarks

- 6.1 As set out in **part 2** the current siting of responsibility for co-operative and community benefit societies in HMT is not logical and does little to serve the interests of these important businesses. Maintaining corporate frameworks is part of the routine good work of government but the status quo makes this very difficult in relation to societies. As set out in **part 3** BEIS has a specific remit in this regard, thus it would be a more logical and effective arrangement if it were responsible for the society corporate framework.
- 6.2 In order to generate the full range of benefits to the society corporate framework, this overhaul would need to impact on regulatory processes as well as legislative processes. Thus, given the issues we have outlined in **part 4**, relating to economies of scale and institutional mission in particular, we think a complementary move of the registration function for societies out of the FCA would also be beneficial.
- 6.3 If government is truly going to create the best possible business environment, it needs to do this for all legal forms. What is more, in form and function co-operative and community benefit societies are specifically intended to empower people in the economy. Thus if the UK is to going to have a more 'Inclusive Economy' with a strong social sector, it will need these corporate forms to multiply and thrive. To this end, siting responsibility for societies in BEIS, and perhaps creating a new social economy registrar, would provide the basis for more effective and enabling policy in the future.

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⁷ We are happy to share details