



Special Update Feature

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Community Interest Companies - The Latest Chapter in the Social Enterprise Revolution?

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Introduction

This article explores Community Interest Companies (CICs) within the context of social enterprise, a key part of the third sector throughout the United Kingdom today.

Social enterprises form part of the third sector. The third sector is a term used to describe the not-for-profit sector which lies between the public sector and the traditional profit making private sector. This growing sector includes charities, foundations, voluntary and community groups and social enterprises as well as non-governmental organisations such as trade unions, religious bodies, housing associations, trade associations and other membership organisations such as research associations and professional societies and institutions.

The Government defines a social enterprise as 'a business with primarily social objectives whose surpluses are principally re-invested for that purpose in the business or in the community, rather than to maximise profit for shareholders and owners.'⁽¹⁾ Social enterprises exist to improve and tackle a number of social issues by using business solutions and, undoubtedly, have an important role to play in the UK economy.

Social enterprise takes on many different legal forms, one of which is the relatively new type of enterprise - the Community Interest Company. Other social enterprise legal forms include unincorporated associations; trusts; limited liability companies; some industrial and provident societies such as community benefit societies; charities; and charitable incorporated organisations.

This article is mainly concerned with the CIC and aims to provide a definition and broad understanding of this recent social enterprise legal form. It also explains why there is a need for this type of company within the sector, how it differs from other forms, and how the Government is keen to drive CICs forward. It will also provide a snapshot into what the future holds in terms of the need for more promotion of this new legal form.

The CIC explained

A CIC is defined in layman's terms as 'a limited company with special additional features created for the use of people who want to conduct a business or other activity for community benefit, and not purely for private advantage. This is achieved by a "community interest test" and "asset lock", which ensures that the CIC is established for community purposes and the assets and profits are dedicated to those purposes. Registration of a company as a CIC has to be approved by the Regulator who also has a continuing monitoring and enforcement role.'⁽²⁾

CICs are primarily motivated to deliver social or environmental outcomes and operate for a range of purposes, including tackling climate change, community transport schemes, childcare facilities, social housing, dealing with disabilities, Fair Trade - re-connecting consumers with local producers, regenerating disadvantaged areas, empowering local communities and delivering new, innovative services at a local level.

It has been possible to register as a CIC in England, Scotland and Wales since 1 July 2005 and 'the CIC legal form [has been]... specifically designed to provide a purpose-built legal framework and a "brand identity" for social enterprises that want to adopt the limited company form.'⁽³⁾ As well as paying the same fees to Companies House as other companies, there are additional fees to pay to the CIC Regulator. Companies House, on behalf of the Regulator, will collect these.⁽⁴⁾ The CIC status is not officially up and running in Northern Ireland, as legislation is still being passed. It is expected that it will be possible to register from April 2007 and the CIC Regulator website will be kept updated with any developments.

Back in September 2002, the Cabinet Office Strategy Office report entitled 'Private Action, Public Benefit'⁽⁵⁾ recognised the need for a reform of the law relating to the legal status and governance of charities and social enterprises. It was considered necessary that a new legal form be created to address a number of issues, including the ability of social enterprises to raise finance, the recognition and branding of the term 'social enterprise', and the need to prevent the assets of social enterprises not registered as charities from being sold for private gain - known as an 'asset lock'. The Department of Trade and Industry (DTI) then carried out a consultation on social enterprise in summer 2003. From this, recommendations were made and a CIC Bill was eventually announced, receiving Royal Assent on 28 October 2004.

talentSTAR became the first CIC in the UK on 11 August 2005. The company provides musical performers with a platform to showcase their talents via organised events. It also provides a genuine working environment and employment experiences in fields which may be less easy to break into for wide-ranging groups of musicians.⁽⁶⁾

As of January 2007, 643 companies have received the status and are operating as CICs. These companies are relatively easy to set up and have all the flexibility and certainty of a traditional company. Firstly, the company has to decide whether it is setting up as a private company limited by shares (CLS) or as a company limited by guarantee (CLG). In a CLS, shareholders each hold shares in the company. Their liability is limited to the amount unpaid on shares they hold. A public limited company (PLC) differs from a CLS in that its shares can be sold to the general public. In a CLG, each of the members gives a guarantee for a certain sum that will be put towards the company's finances if the company is wound up. A CLG cannot raise finance by issuing shares, nor pay dividends to its members.

In addition, a CIC has to include other special features to ensure it is working for the benefit of the community. These criteria include:

- The successful passing of a community interest test - an assurance that the primary objective of the company is to work in the interests of the local geographical community or community of interest;
- an asset lock, whereby the assets and profits of the CIC must be permanently retained within the company and used solely for the benefit of the community; and
- an additional annual report explaining how their activities have benefited the community and how they are involving their stakeholders as well as complying with CIC Regulator requirements (regularly, but lightly monitored).

Legal Requirements

* *Community Interest Test*

When registering as a CIC, either as a company limited by shares, or a company limited by guarantee, it is necessary to provide Companies House with a community interest statement

describing the social purpose of the company. The CIC Regulator will permit CIC status providing the statement passes the community interest test, demonstrating that the activities of the business will benefit the community or a part of it.

* *Asset Lock*

CICs must have an asset lock. The company is not able to transfer its profits or assets for less than their full market value. An asset lock also serves to protect any remaining assets for the community should the CIC become dissolved. In order to protect the asset lock, any shares that are paid to investors will be capped at a figure set by the CIC Regulator.

* *Annual Community Interest Company Report*

In addition to the usual submission of end of year accounts, a CIC is duty-bound to present an annual community interest company report for public record. The report must show how that the CIC has put community interest at the forefront of its activity, giving examples of particular groups of people it has helped within a specified community.

Most individuals or organisations able to form a company can gain CIC status. The restrictions that exist relate more to the activities or purpose of the CIC than to the people or type of organisation. CICs cannot be formed on political grounds, nor can they operate for the personal gain of an individual, or group of individuals.

CICs and charities

CICs do not have charitable status. CICs have more flexibility and less regulation than charities. Although many CICs will consider themselves to have charitable objectives, they are not charities. A charity can convert to a CIC but it will lose its charitable status and the associated tax advantages. However, it is permissible for a charity to own a CIC, in which case the CIC would have to pass assets to the charity.

(It should be noted that, at present, a Scottish charitable company may not convert to a CIC. Organisations are advised to contact the Scottish Charity Regulator for the most up-to-date information on this.⁽⁷⁾)

An organisation cannot, therefore, operate as both a CIC and a charity. It must opt for one or the other. So what are the differences between the two?

- * Whereas charities operate solely for charitable purposes, a CIC can be established for any lawful purpose, as long as activity chiefly benefits the community - either by locality or interest.
- * Charities have tax advantages that CICs are not eligible for. These tax advantages mean charities are much more tightly regulated and do not have the relative freedom of the CIC.
- * CICs can pay their board members; it is very rare for a charity to be permitted to pay board members.
- * The CIC legal form provides a brand identity for those social enterprises wishing to adopt the limited company form. The brand is becoming recognised in its own right within the social enterprise and larger third sector.

So the differences are clear. But which types of organisation would be best suited to opting for the CIC legal form?

For many types of organisation, charitable status is right for them and it would not benefit from converting to a CIC. For charities that have a specific public interest for a particular good cause/range of good causes, the flexibility of the CIC is not necessary. This is because the charitable objectives of many charities do not change from one financial year to the next. Consequently, the rigidity of the Charities Commission regulation is not a huge problem.

However, for some not-for-profit organisations it is vital for them to be able to quickly adapt to changing circumstances. These organisations are businesses, and are run like a traditional limited company where changes in the marketplace result in the need for immediate action. This is

significant for those working in areas of regeneration, where other developments taking place within a locality will have a knock-on effect on activity. Such organisations, therefore, need the flexibility and entrepreneurial nature of CIC status which has a light-touch relationship with Companies House and the CIC Regulator. The status has its own brand and is becoming widely recognised in its own right as a vital part of social enterprise.

The Government - how is it helping the brand to grow?

The Government has arguably helped to drive forward this new brand and place it firmly alongside other forms of social enterprise. Its flexibility and business-like approach, underpinned by a clear assurance of not-for-profit distribution for those working in the interests of the community, mean the CIC will grow into an important feature of social enterprise, the third sector and the UK economy overall.

As Chancellor Gordon Brown himself put it, 'social enterprise is the new British success story, forging a new frontier of enterprise - a quiet revolution involving 55,000 social enterprises in our country from the smallest community groups to larger businesses'.⁽⁸⁾

Enterprise Minister the Rt Hon Alun Michael MP comments how 'Across Government, we are seeking ways to create a more enterprising culture. Successful business activity includes social enterprises which are soundly based and that meet public needs. Community Interest Companies provide an innovative structure which is unique in the world and offers a creative solution to the challenges of regeneration and economic and social inclusion We want the marketplace for social investment to grow as people see social enterprises growing, and delivering at local, regional and national levels.'⁽⁹⁾

And it does not stop there. The Government is keen to get young people straight out of school/college/university into social enterprise, including CICs. In November 2006, the Government announced its Social Enterprise Action Plan to raise awareness of what a social enterprise is and what can be achieved in terms of making a real difference to people's lives. The drive to make clear what a social enterprise is comes fresh from the finding that 'only one in four people know what a social enterprise is: a firm founded for a social purpose that reinvests its profit in the company or community.'⁽¹⁰⁾

Research has also shown that young people are attracted to the idea of working in a job where they are using a mix of business skills and social consideration/impact. The Plan includes promoting social enterprise in schools, providing curriculum materials and ensuring it is studied on GCSE and A-level business studies courses; encouraging graduates into social enterprise careers through providing support to the National Council for Graduate Entrepreneurship; researching new ways of providing social enterprise learning at tertiary level; and driving forward a social enterprise marketing campaign targeted at young people aged 14-30.

However, some commentators are more cynical about the Government fanfare regarding social enterprise; as Paula Howley (Projects Manager at Rise, which supports social entrepreneurship in the South West) puts it, 'to paraphrase all the policy/political people: There are lots of big problems but it's okay, there's a social enterprise. Hearing social enterprise being heralded as the 'one-treatment-cures-all' phenomenon is starting to make me feel rather queasy It's great to hear they have an interest and a belief in social enterprise. But do we have the infrastructure to deliver against these high expectations?'⁽¹¹⁾

There has been criticism that the Government is not backing up the theory with practice - facilitating real action at regional and local level. If CICs are to work, then the standard of business advice and support should equal that which is offered to the traditional limited company. Regional Development Agencies (RDAs) must drive suitable forms of support through their Business Links. This was brought into question at the official CIC launch, when only London Development Agency and Business Link Cumbria attended. Andrew Robinson, Head of Community Development Banking at Natwest & The Royal Bank of Scotland (RBS), speaking at the event, commented how 'the agencies

of government need to be doing the hard work, but where are the RDAs? These agencies are not here.⁽¹²⁾

Similarly, Paula Howley describes the way she sees the situation: 'I would say the most popular word used to describe business advice for social enterprise is patchy. Many infrastructure/advice agencies try to offer something to social enterprises. A recent Rise survey of providers in the South West found most were unclear about what a social enterprise is. You do have to wonder how they offer good support when they don't actually understand them.'⁽¹³⁾

Some are sceptical about the CIC brand *per se* as there seems to be a lack of understanding about what it actually is. There is much more the Government can do in terms of making more money available for the promotion of this legal form.

Eighteen months on - a success story?

It is fair to say that when CICs were introduced there was a great deal of ambiguity surrounding their status, not least in how successful they would be as a valid form of social enterprise, and what the status actually means. However, 18 months on, there is plenty to be positive about. With almost 650 CICs in operation to date, this legal form/status is proving to be a popular choice for many social enterprise organisations. This promising figure is, however, mirrored across the social enterprise sector as a whole, which is going through something of a boom period. The CIC status is one of a range of options within social enterprise, and all forms, from the trust to the community benefit society or charitable incorporated organisation, are seeing a rise in numbers.

Nevertheless, the relative and growing success of the CIC is being identified and quietly recognised throughout both Government and the social enterprise sector. 'The success of CICs and other social enterprises in placing social responsibility at the heart of their business poses a growing challenge to the private sector, to reinforce what is already done in the name of corporate social responsibility and ensure that ethical business activity is real and meaningful....The Government will continue to work to ensure that social enterprises are free from unnecessary regulation, have sufficient access to secure capital and, where they wish to be, are well-placed to help deliver public services.'⁽¹⁴⁾

On 10 July 2006, the results of the first CIC Annual Survey were announced at the Social Enterprise Coalition (SEC) Conference. The RBS/Natwest survey revealed that 43% of organisations chose to adopt the CIC legal form as it suitably bridged the gap between business and charity. A total of 19% stated they converted to receive less regulation, and 16% cited social purpose. Rowna Strathdee, of Bookdonors, is typical of many CICs: 'CICs are a godsend, they involve less regulation than a charity, and it is a model that recognises that we want to be a business.'⁽¹⁵⁾ Of CICs surveyed, 15% said becoming a CIC had made it easier to interact with other organisations such as local authorities, foundations, banks and government.⁽¹⁶⁾

A large part of this early success must be attributed to the CIC Regulator, John Hanlon, whose back-seat, trusting, yet encouraging approach makes life easier for the CIC. This light-touch regulation is in stark contrast to many other forms of Government regulation, not least that of the Charities Commission. As one solicitor puts it, 'John Hanlon and his team by all accounts are a committed office, endowed with a great deal of common sense and a can-do approach that is very refreshing.'⁽¹⁷⁾ Of those CICs surveyed, 89% said they found the application process "easy" or "very easy".⁽¹⁸⁾

On 9 October 2006, John Hanlon himself praised the uptake, ' In just fourteen months we have seen CICs set up as cinemas, radio stations, special schools, ferries, railways, day-care centres and recycling units. In fact, the list is endless but they all have one thing in common. They are providing real and tangible benefits to communities throughout the UK. And I am particularly pleased to see that an increasing number of CICs are helping the vulnerable and disadvantaged not only in the UK but also abroad.'⁽¹⁹⁾ During this speech, Hanlon announced the 500th CIC - Territory Mapping, based in Portsmouth. This CIC is engaged in providing training and coaching to social

enterprises, voluntary organisations and charities, aiming to help them improve overall performance through developing suitable strategic business plans.

The uptake of CICs since August 2005 has been impressive. The Social Enterprise Coalition is confident this will grow and we should hopefully see a nation where in excess of 400,000 CICs are in successful operation. However, for this to happen much needs to be done in terms of promoting the brand to ensure that funders are keen to support the CIC, as the situation at present is variable.

What does the future hold? - Finding suitable funders

As many funders have been unaware of what the true definition of the CIC is, they have been understandably unwilling to fund this type of company. However, this is more to do with a lack of understanding as opposed to being unwilling to fund the activity. Sue Campbell, of Equal Ability CIC in West Yorkshire, explains how 'we recently applied for Lottery money, but we got knocked back because they didn't understand what a CIC was ... But we explained it to them and have now got through to outline stage.' This example demonstrates the crucial need for the Government and the social enterprise sector to communicate the meaning of the CIC so it is a widely used everyday term, easily understood, equalling that of other terms within the third sector.

It is early days, but there is plenty to build upon. The CIC Regulator is doing much to ensure that any confusion surrounding CICs is eradicated by contacting any organisation he becomes aware of that needs to be clued up on the status. The Big Lottery Fund has now agreed that it will consider funding CICs. Previously, the governing documents (memorandum and articles of association) CICs were able to provide, did not meet the funder's criteria. However, the Big Lottery Fund's changing attitude to funding, whereby it is chiefly concerned with outcomes of funding and purpose of project, means the CIC is now eligible to apply. This means a number of Lottery programmes may be a source for the CIC to tap into.

Similarly, the Regulator has now contacted all Business Links to ensure they are aware of the role and purpose of the CIC so they are in a position to give advice accordingly. High Street banks are also being contacted so they are clear on the legal status of the CIC.

To conclude

The CIC is steadily establishing itself as an important part of the social enterprise and wider third sector throughout the UK. Its status as a limited company working for community benefit is allowing for hundreds of worthwhile projects to take place and is providing back-up to key public services. From town-centre management, community transport and recycling schemes through to childcare facilities, social housing and social welfare schemes, CICs are very broad-ranging in what they do and who they help. The community interest test, asset lock and end-of-year community statements help to ensure that profits are going back into developing the company or to a segment of the community, validating the CIC as a worthy form of social enterprise. The gap between private business and charity working for the public good has been bridged by this growing legal form.

In spite of this credible success, more needs to be done to promote the CIC and to build capacity to ensure numbers continue to rise. The social enterprise sector, alongside the Government, needs to clearly define what a CIC is through nationwide promotion. It is essential that infrastructure is in place whereby organisations from the public, private and the voluntary sector know what CICs do, in order to inform, advise, promote, fund, or work with potential or existing CICs.

If such a drive to push CICs forward becomes a reality, then Social Enterprise Coalition Chief Executive Jonathan Bland's vision for a future where 400,000 CICs are in operation throughout the UK may also become a reality.

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If you found this article useful, you may also wish to read the following Special Update Features:

Credit Unions - A Community Approach to Combating Financial Exclusion (August 2005)

Social Enterprises Explained (February 2003)

The full list of Special Update Features may be accessed on GRANTfinder through the User Library link (via My Resources on the Internet version of GRANTfinder).

Useful links

CIC Regulator: <http://www.cicregulator.gov.uk/>

Business Link: <http://www.businesslink.gov.uk/>

Social Enterprise Coalition: <http://www.socialenterprise.org.uk/>

Social Enterprise Magazine: <http://www.socialenterprisemag.co.uk/>

Companies House: <http://www.companieshouse.gov.uk/>

Charity Commission: <http://www.charity-commission.gov.uk/>

Office of the Scottish Charity Regulator: <http://www.oscr.org.uk/>

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