

Devolution Guidance – 07

Understanding CICs

(Community Interest Companies)



Context/ Overview

A Community Interest Company (CIC) is a type of company introduced by the UK Government in 2005 under the Companies (Audit, Investigations and Community Enterprise) Act 2004, designed for Social Enterprises that want to use their profits and assets for the public good.

Setting up a Community Interest Company...

This guidance covers some of the key areas involved in CICs, including:

- Reasons for and benefits of setting up CICs
- Costs involved
- Legal paperwork required
- What an asset lock is
- Who regulates CICs
- Examples of some CICs in Cornwall

What is a Community Interest Company (CIC) and how is it connected with Social Enterprise?

CICs were developed to address the lack of a legal vehicle for non-charitable social enterprises across the UK. Available since 2005, there are now over 3,100. CICs vary in size from tiny community-based organisations to multimillion pound enterprises. Their areas of operation include physical well-being, radio and television, the arts, education, and health and social work.

Fundamentally CICs are normal companies. They can be established either as companies limited by guarantee (CLG), which around three-quarters are, or companies limited by shares (CLS). However, they have some unique and important additional features to safeguard their social mission.

What are these additional features?

A CIC has to carry out activities which fulfil a community purpose. This is defined when an application is made to set the CIC up. There are a huge variety of purposes which meet the so-called "community interest test". These range from promoting the healthcare of residents of a particular community to promoting climate change awareness programmes or reducing greenhouse gas emissions.

A CIC also has a "lock" on its assets. This prevents profits from being distributed to its members or shareholders other than in certain limited circumstances. It also means that all assets must be used for the community purpose or, if they are sold, open market value must be obtained for them and the proceeds used

for the community purpose. In addition, if the CIC is wound up, its assets must be transferred to another, similarly asset-locked body.

Can CICs be charities as well?

No. Charities can trade to pursue their public benefit purposes and many do so very successfully. However, being a charity is not the best route for many social entrepreneurs because of the basic rule of charity law that charities must in most circumstances have volunteer boards. A major advantage of CICs is that their directors can be paid a salary, which means that the founders of the CIC can retain strategic control of the enterprise by sitting on the board as paid directors.

At the same time, the asset lock and community purpose requirements ensure that the social mission is protected, and CICs are less heavily regulated than charities. This means that other organisations, including local authorities and other public bodies, may be more willing to contract with a CIC than a commercial company. As the social purpose is protected, CICs are also increasingly successful in attracting the kind of grant-funding traditionally restricted to charities, though the more traditional grant-givers may still be more inclined to support charities than CICs.

On the other hand, CICs do not currently benefit from any of the tax advantages that charities do.

How are CICs financed?

Both individuals and companies can invest in a CIC, subject to certain rules that regulate this. A CIC can be financed by loans or bonds, though there are limits on the amount of interest that can be paid if the CIC agrees to pay interest at a rate linked to the CIC's financial performance. A CIC that is a CLS can issue shares, but if the CIC buys back those shares only the capital paid for the shares can be repaid pound for pound, with no uplift. In other words, all capital gains on buy back will belong to the CIC and not to shareholders or members. However, there is no restriction on the price at which shares in a CIC can be sold to somebody else.

Where the CIC is a CLS, the payment of dividends is permitted within defined statutory limits, currently 5% above the Bank of England base rate. There will also be a ceiling of the amount of a CIC's profit that can be distributed by way of dividends, currently 35%. These limits are currently being reviewed by the CIC regulator.

This all sounds a bit restrictive; surely a normal company would offer more flexibility?

It really all depends on your aspirations. If you intend to build up value in the company over time with a view to the shareholders or members extracting that value later, a normal company will be more appropriate. But the whole point of a CIC, and the major difference from a normal company, is that its assets are locked into the business to ensure that they are applied for its social purpose, subject to the limited profits which may be distributed. The price of the flexibility offered by a normal company is the lack of protection for the social mission,

while the raison d'être of a CIC is to strike a balance between the need to protect the social purpose while allowing reasonable remuneration for directors and a limited return for investors.

What are the protections for the directors and members/shareholders?

As with normal companies the CIC benefits from "limited liability". This means that the CIC will be liable for the actions of its directors and directors will not incur personal liability, except in certain exceptional circumstances (such as where the director has acted fraudulently, or continued to trade when the CIC has become insolvent).

Shareholders will only be liable up to the amount of their contribution (where a CLS), and members only up to a nominal amount (usually £1) in the event it winds up (where the CIC is limited by guarantees).

Who regulates CICs?

Are the reporting requirements the same as for normal companies?

CICs are regulated by the CIC regulator with what is intended as a "light-touch". This compares with the relatively "heavy" regulation of charities by the Charity Commission. However, the CIC regulator will respond to complaints from stakeholders and has considerable powers to act to protect the community interest.

As with all companies, CICs are required to file annual accounts and an annual return (now called a Confirmation Statement) with Companies House. In addition, a CIC has to file a community interest report annually, which will explain how the CIC pursued the community interest and involved its stakeholders and will, if applicable, give details of payments to directors and any dividends paid.

What do I need to do to set up a CIC?

First of all you need to make an application to Companies House for a small fee, currently £35.

The application will include form CIC36 which sets out the CIC's social purpose and the activities it will carry out to achieve it, its proposed governing document (the articles of association) and some administrative forms for each director.

Provided there are no issues raised by the CIC regulator or Companies House, the CIC should be registered around two to three weeks from the application date. Unfortunately, it is still not possible to register a CIC electronically, which can speed up the registration process for normal companies.

Further information

Further information about CICs and Social Enterprises is available online:

- **Regulator of Community Interest Companies**
www.gov.uk/government/organisations/office-of-the-regulator-of-

community-interest-companies

- **The CIC Association**
www.cicassociation.org.uk/
- **A Guide to Social Enterprises**
www.socialenterprise.org.uk/
- **Social Enterprise Magazine**
www.pioneerspost.com/

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