

Options appraisal for LEP legal personalities

September 2018

	Company Limited by Guarantee	Community Interest Company (CIC) [can be combined with a company limited by guarantee or shares]
Legal Form	<p>Most guarantee companies are not-for-profit – as such, most companies need their articles of association to be drafted to reflect this. This model currently makes up the rest of LEP incorporation status.</p> <p>Registered at and regulated by Companies House. Governed, in the main, by the Companies Act 2006 (as amended).</p> <p>Must have at least one director who is a natural person. Directors are usually appointed by members, or with members' consent. Does not have any share capital or shareholders, but instead members who control it. A member needs to be a company or a natural person. In some companies, some or even all the directors may be appointed by one or more outside bodies, such as charities or local authorities who are backing the project. Need to consider whether/how proposed directors and members are conflicted in each case, to ensure public perception is of LEP independence. Companies Acts set out statutory requirements as to conflicts of interest</p> <p>Not prohibited from distributing its profits to members by the Companies Act or any other law (subject to satisfaction of certain conditions) but it is commonplace for restrictions to be put on profit distribution in the company's articles.</p> <p>Company itself is a separate entity and it is liable for its debts.</p>	<p>A CIC is a limited company with extra features to mark it out as a social enterprise. Limited numbers of LEPs have adopted this model.</p> <p>Regulatory body is the Office of the Regulator of Community Interest Companies, which is part of Companies House. CICs were established by the Companies (Audit, Investigations and Community Enterprise) Act 2004 and are subject to provisions laid down both in this Act, the Community Interest Company Regulations 2005 (as amended) as well as the Companies Acts.</p> <p>Company structure will depend on whether the company is limited by guarantee or by shares.</p> <p>Must have at least one director who is a natural person. Has shareholders or members who control it. As with companies limited by guarantee, CICs need to consider whether/how proposed directors and members are conflicted.</p> <p>A CIC must satisfy the "community interest test" throughout its existence – would a reasonable person consider its activities as being carried on for the benefit of the community.</p> <p>A CIC cannot be a charity granted charitable status by the Charity Commission.</p>

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	<p>Limited by guarantee (members provide a nominal guarantee in the eventuality a company is wound up).</p> <p>Subject to corporation tax and VAT.</p>	<p>Key distinguishing feature is the asset lock which seeks to ensure that assets are not transferred for less than full consideration and are used for the benefit of the community - 35% of CIC's distributable profits in any one year can be paid out in private dividends to shareholders (but more/all if to asset-locked bodies); rest is locked in to further CIC's mission. On dissolution, assets can only be transferred to another asset-locked body.</p> <p>Company itself is a separate entity and it is liable for its debts.</p> <p>Can be limited by shares or by guarantee.</p> <p>Subject to corporation tax and VAT.</p>
Costs	<p>Typical costs of registration using a reputable company registration agent are usually in the region of £50 to £150, depending on the level of service.</p> <p>It is subject to corporation tax to the extent that it has any income, profits or gains (in the same way as an ordinary trading company). However, if the company is registered as a charity with the Charity Commission then it may be able to benefit from certain tax exemptions.</p> <p>Will incur costs in transferring existing LEP assets to new company. Costs will vary depending on types of asset involved. There may also be tax implications depending on the type and value of assets transferred.</p>	<p>Typical costs of registration using a reputable company registration agent are usually in the region of £35 to £180, depending on the level of service.</p> <p>It is subject to corporation tax to the extent that it has any income, profits or gains (in the same way as an ordinary trading company).</p> <p>Will incur costs in transferring existing LEP assets to new company. Costs will vary depending on types of asset involved. There may also be tax implications depending on the type and value of assets transferred,</p>

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<p>Also costs relating to various ongoing filing requirements.</p> <p>Will incur back office and administration costs. Furthermore, LEPs who become independent from their accountable body will likely need to fund things such as: office space; general staffing; legal advice; HR resourcing; financial advice etc.</p> <p>VAT If the LEP's turnover is more than £85,000 in any prior 12 month period, or if it reasonably expects its turnover over the next 30 days alone to exceed this threshold, then it must register for VAT. This threshold tends to increase from 1 April each year. It is also possible to register voluntarily.</p> <p>If the LEP is VAT registered, then it must charge VAT at 20% on all of its standard rated supplies to customers. It must account to HMRC for the difference between this "output tax" VAT and the VAT it has suffered ("input tax") on a quarterly basis.</p> <p>It is also possible to account for VAT on a different or simplified basis. For instance:</p> <ol style="list-style-type: none"> 1. The 'cash accounting' scheme allows you to account for VAT once you have received payment for invoices, and similarly to recover VAT when you have paid it. However, the scheme is only available to businesses with a turnover above £1.35m. 	<p>Also costs relating to various ongoing filing requirements.</p> <p>Will incur back office and administration costs. Furthermore, LEPs who become independent from their accountable body will likely need to fund things such as: office space; general staffing; legal advice; HR resourcing; financial advice etc.</p> <p>VAT If the LEP's turnover is more than £85,000 in any prior 12 month period, or if it reasonably expects its turnover over the next 30 days alone to exceed this threshold, then it must register for VAT . This threshold tends to increase from 1 April each year. It is also possible to register voluntarily.</p> <p>If the LEP is VAT registered, then it must charge VAT at 20% on all of its standard rated supplies to customers. It must account to HMRC for the difference between this "output tax" VAT and the VAT it has suffered ("input tax") on a quarterly basis.</p> <p>It is also possible to account for VAT on a different or simplified basis. For instance:</p> <ol style="list-style-type: none"> 1. The 'cash accounting' scheme allows you to account for VAT once you have received payment for invoices, and similarly to recover VAT when you have paid it. However, the scheme is only available to businesses with a turnover above £1.35m.

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	<p>2. The 'Flat Rate' scheme provides a simpler way to account for VAT and may be beneficial depending on specific circumstances. It allows businesses to account for VAT at a fixed rate and to keep the difference between the VAT which they charge to customers and the VAT which they pay HMRC.</p> <p>A LEP which is registered as a charity may not be required to charge VAT to its customers where it makes supplies which fall within any of the relevant exemptions or zero-ratings for charities.</p>	<p>2. The 'Flat Rate' scheme provides a simpler way to account for VAT and may be beneficial depending on specific circumstances. It allows businesses to account for VAT at a fixed rate and to keep the difference between the VAT which they charge to customers and the VAT which they pay HMRC.</p>
Flexibility	<p>Allows LEPs to develop own internal policies relating to management.</p> <p>Members of company will be able to modify the articles of association to suit individual and changing circumstances.</p> <p>Establishing LEP as a permanent legal personality means it can become self-sustaining beyond government funding to stimulate its own profit margin.</p> <p>If profits are not to be distributed (as provided by company's articles), they can instead be reinvested to help promote the objectives of the LEPs at their own choosing. This could potentially address the concerns about staffing costs if recycled into revenue expenditure.</p>	<p>Allows LEPs to develop own internal policies relating to management.</p> <p>Members of company will be able to modify the articles of association to suit individual and changing circumstances.</p> <p>Establishing LEP as a permanent legal personality means it can become self-sufficient beyond government to stimulate its own profit margin.</p> <p>As profits cannot be distributed beyond the 35% dividend cap (if the CIC is limited by shares), they can instead be reinvested to help promote the objectives of the LEPs at their own choosing. This could potentially address the concerns about staffing costs if recycled into revenue expenditure.</p>

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<p>More flexibility to implement innovative business measures to increase profit for the LEP.</p> <p>However, this freedom is subject to the Companies Act which lays down rules about things such as board meetings, member meetings, , accounts and audit – all of which will involve expenses and paperwork.</p> <p>The fact that a company limited by guarantee cannot have a share capital limits its fund-raising capacity, simply because it cannot issue shares to those who back it and join it. For this reason, some projects that are not essentially profit-motivated are set up as companies limited by shares. A guarantee company can borrow money and may issue debentures or debenture (loan) stock.</p>	<p>More flexibility to implement innovative business measures to increase profit for the LEP.</p> <p>However, a CIC is subject to dual regulations by both the CIC regulator and Companies House/Act.</p> <p>Most notably, CICs are not subject to the more onerous regulations and limitations which apply to charities. In particular, they can be trading enterprises benefiting from the advantages of limited liability and (if limited by shares) can issue shares and pay dividends. This provides relative freedom for the day-to-day running of the CIC, provided that the relevant caps and regulations are adhered to.</p> <p>CICs have the option to pay directors; however, the community interest test and the asset lock apply as much to the remuneration of directors as to any other area of a CICs business. Therefore directors' remuneration should never be more than is reasonable and remuneration arrangements should always be transparent. If the CIC is paying its directors more than they are really worth (to itself or the community that it serves) then it may well be breaching its asset lock. Such a breach may give rise to legal action.</p>

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Reporting Requirements	<p>Must submit a memorandum on incorporation and articles of association, the latter being the main constitutional document of the entity. Must register accounts and a confirmation statement each year.</p> <p>Must maintain various company registers, including a register of those persons with significant influence and control. Duty to update Companies House of any changes to the contents of such registers.</p>	<p>Must comply with company regulations in general (see opposite note relating to companies limited by guarantee). Additionally, they must submit a Community Interest Statement and an annual Community Interest Report.</p> <p>The CIC needs to justify its status by declaring how it will be a benefit to the community through submission of form CIC36 which contains the initial Community Interest Statement with the initial application to form a CIC. An objects clause which identifies that the CIC will undertake activities for the benefit of the community should be included in the articles of association.</p> <p>In addition to the initial Community Interest Statement, every CIC must file an annual Community Interest Report alongside its accounts. This is filed at Companies House and copied to the CIC regulator, and as its name suggests, should assert what the CIC has done to benefit the community during the year. It also includes details concerning directors' remuneration, dividends declared, and capped performance-related interest paid on any loans.</p>
Accountability	<p>This model formalises the legal personality of LEPs, providing a transparent and accountable framework for reporting provided by general corporate regulations.</p> <p>Defined objectives in articles ensure that money is spent right.</p>	<p>This model formalises the legal personality of LEPs, providing a transparent and accountable framework for reporting provided by general corporate regulations.</p> <p>Defined objectives in articles ensure that money is spent right.</p>

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	<p>Asset lock (if put in articles) provides reassurance mechanism to public and investors.</p> <p>As directors can be appointed by LAs, this means that such directors could be directly accountable to a democratic body. As noted above, detailed consideration of conflicts of interest needs to be undertaken. The directors will have fiduciary duties to the company (i.e. LEP) ahead of the LA.</p> <p>However, such reporting requirements may set a precedent of fulfilling the bare minimum and as such limits any possible democratic accountability such as local scrutiny measures.</p>	<p>Asset lock provides reassurance mechanism to public and investors.</p> <p>Further accountability provided by requirement of Community Interest Statement and Reports. The key added feature is that CICs come under the regulation of the Office of the Regulator of Community Interest Companies. The Regulator's job is to make sure that each CIC is satisfying the community interest test and is not abusing the trust that the public expects to put in a CIC. By putting the company under the Regulator's scrutiny, the directors/shareholders of a CIC can clearly demonstrate that the company is genuinely undertaking activities for the benefit of the community and not for private profit.</p> <p>However, such reporting requirements may set a precedent of fulfilling the bare minimum and as such limits any possible democratic accountability such as local scrutiny measures.</p>
Advantages	<ul style="list-style-type: none"> ✓ Establishes LEP as an independent, self-sufficient body. ✓ Liability is limited to the amount set out in the company's articles - typically a nominal amount of £1 - protecting LEP members from personal liability. ✓ Common structure for non-profit organisations. ✓ Incentive for involvement is objectives rather than profit. ✓ Introduction of reporting requirements increases accountability and transparency. ✓ Asset lock (if included) means that LEPs can reassure the 	<ul style="list-style-type: none"> ✓ Establishes LEP as an independent, self-sustaining body. ✓ Limited liability either by guarantee or shares. ✓ Designed to provide an effective legal form for enterprises which aim to provide benefit to the community or trade with a "social interest" rather than make a profit – a lot of CICs tend to be spin outs from the public sector such as the City Health Care Partnership. ✓ Dividend cap on shares means that LEPs can reassure the public of genuine motives whilst still maintaining an effective

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	public of genuine motives whilst still maintaining an effective means of attracting financial support.	<p>means of attracting financial support.</p> <ul style="list-style-type: none"> ✓ Not subject to onerous regulations and limitations which apply to charities. ✓ Branding of CIC can be assuring to both public and investors. ✓ Flexibility to pay directors. ✓ Introduction of reporting requirements increases accountability and transparency.
Disadvantages	<ul style="list-style-type: none"> ✗ Introduces regulatory requirements – this may put off LEPs who are not using this model from changing as they may not want to have to comply with further regulations. ✗ Need to finance back office functions to manage finance, banking, procurement, HR communications and other operational activities. ✗ Lack of privacy for board directors and members, again potentially dissuading the LEP from changing models. ✗ Although filing with Companies House is straightforward, there are high penalties for delay/failure to file information. 	<ul style="list-style-type: none"> ✗ Introduces requirement to fulfil statutory reporting requirements and prepare annual accounts as well as submitting an initial Community Interest Statement and annual Community Interest Reports, a potential deterrent for LEPs who want to retain flexibility. ✗ Need to finance back office functions to manage finance, banking, procurement, HR communications and other operational activities. ✗ Lack of privacy for board directors and members, again potentially dissuading the LEP from changing models. ✗ Although filing with Companies House is straightforward, there are high penalties for delay/failure to file information. ✗ Does not receive the tax advantages extended to charities e.g. will not obtain business rate relief but may qualify for discretionary relief. ✗ The scope of the community interest test can be ambiguous.

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Conversion process	<p>Little difficulty in transforming all existing LEPs which are not limited companies into limited companies in terms of registration processes.</p>	<p>Already registered limited companies that are not CICs would need to pass and submit the relevant resolutions, articles, forms and fee and obtain approval from the CIC Regulator via form CIC37 if they decided to change to a CIC.</p> <p>Existing LEPs which are not limited companies would have to submit form IN01, form CIC36 and memorandum and articles of association plus a registration fee to become a CIC.</p>