

Converting a Charitable Trust to a Charitable Incorporated Organisation (CIO)

1. Introduction

Many charities are currently still structured as an unincorporated charitable trusts – that is a body of trustees who come together to hold funds on trust which are applied for charitable purposes as set out in the Declaration of Trust (also known as trust deed).

A body of trustees is just that – a body of individuals. So any legal agreements should technically be made in the names of the trustees, because ‘the charity’ is not a legal entity. If the charity has property it must be held in the name of holding trustees. If the charity enters into contracts – e.g. a contract of employment – then the individual trustees are the employer. If anything goes seriously wrong and the charity faces legal action, it is the trustees who will be sued as individuals – and if the case goes against them and the charity has insufficient funds they can be personally liable.

So although charitable trusts work well for smaller charities, particular those which simply give out grants, they lack two important features:

- **corporate status** – if the charity is a corporate body it can hold property in the name of the charity itself and enter into contracts on that basis – that is not possible as a charitable trust
- **limited liability** – if the charity is a body with limited liability it means that in most circumstances the trustees are protected from personal liability if the charity cannot meet its debts.

However, there can be further complications with the trust structure. It is not uncommon to find trust deeds which provide for a council or committee which makes all the operational decisions – so in practice the committee members may be the charity trustees even if they are not described as such (in law, the charity trustees are defined as “the persons having the general control and management of the administration of a charity”.) Conversely some trust deeds allow the charity trustees to nominate individual trustees to hold property (holding trustees) – in fact it is not unusual to find property held by holding trustees who have little contact with the charity trustees. In other cases, a corporate body, separate from the charity itself, is used as a trustee of property. So there is often considerable confusion between:

- the **charity trustees** – those who govern the charity and have final authority on all decisions regarding the work of the charity; and
- the **holding trustees** – who hold property in trust for the charity.

Not all unincorporated charities are trusts – some are membership bodies (charitable associations, governed by a constitution or rules). This article focuses on charitable trusts considering conversion to a CIO, though occasionally a charitable trust can have a wider membership structure beyond the trustees. So the issues for charities with a broader membership are mentioned from time to time.

2. What is a CIO?

A CIO is a corporate body with limited liability but it is registered solely with the Charity Commission. It is governed purely by the Charities Act 2011. It is *not* a company, and not therefore registered at Companies House. (This applies to a CIOs in England and Wales. CIOs in Scotland – known as SCIOs – are subject to the Charities & Trustee Investment Scotland Act 2005. They are formed by registration with the Office of the Scottish Charity Regulator, OSCR. CIOs will also be available in due course in Northern Ireland.)

It is much more straightforward for a charity which owns property to be a corporate body, because the body is a legal person in its own right and can hold the title to property without separate holding trustees. Also, limited liability is increasingly important if a charity gets into a dispute, as action could be taken against the charity itself, but not against individual members or trustees (unless they had acted improperly). Nowadays most charities other than the smallest are established as corporate bodies.

Until recently, the only straightforward means for a charity to have a corporate structure with limited liability was to establish a *charitable company* – i.e. to form a not-profit company limited by guarantee, and then seek registration of the company as a charity. This remains possible and is the main form used by large charities – but it means complying with company law *and* charity law. For example, any changes to trustees have to be advised to Companies House *and* to the Charity Commission, and the annual accounts have to comply with the requirements under the Companies Act 2006 *as well as* the Charities SORP (the standard for charity accounting).

A CIO overcomes this problem – it is a corporate body with limited liability and a registered charity. A CIO can only be formed if the Charity Commission is satisfied that it will be a charity in law.

A CIO is governed by a constitution – a bit more complex than your current trust declaration, but simpler than the articles of a charitable company. The Charity Commission produces model CIO constitutions for this purpose (but it still takes considerable work to take the model and create a suitable governing document for a specific charity).

A CIO is governed by charity trustees. Where a CIO is formed to take over from an existing charitable trust, it is usual for the existing charity trustees to become the charity trustees of the CIO (even if they are not generally called trustees at present). But in the CIO they will be charity trustees in the sense of taking decisions, rather than trustees personally holding property.

The name of a CIO normally ends with “CIO” – so often the CIO is formed with a name which is the name of the old charity plus CIO on the end – e.g. “The XYZ Trust CIO”. It is possible to omit “CIO” from the legal name if the CIO status is disclosed on all documents (cheques, appeal letters, order forms, contracts etc) but our recommendation is that it is usually simplest to include “CIO” on the end of the legal name which saves these complications. Also, it is extremely confusing to enter into the formal agreements for transfer of assets if the legal name of the CIO is *exactly* the same as the charity it is replacing – having “CIO” as part of the name avoids this. Moreover, now CIOs are taking off, many charities are proud of their CIO status.

3. Why are CIOs only now available?

The Government accepted the case for CIOs in 2002. They became law in the Charities Act 2006, but regulations also had to be made, and this led to a long delay. The legal framework was subsequently consolidated in the Charities Act 2011 and the regulations finally took effect from 2 January 2013. However, they have quickly become popular, with more than 1000 CIOs now formed. Around 25% of all new charities being registered are CIOs.

(However, Scottish CIOs – SCIOs – have been available since April 2011, and around 40% of all new charity registrations in Scotland are now for SCIOs. So there is good experience of the concept.)

4. What would be the advantages for a charitable trust to become a CIO?

(a) In many cases the biggest advantage is that the charity would become a corporate body – a legal entity in its own right – rather than just a body of individual trustees.

This would mean that the properties and any other assets could be held officially in the name of “The XYZ Trust CIO” – there would be no need to change the title to properties when there are changes of individual trustees.

It would also mean that contracts with other parties would be directly held by the CIO rather than by the trustees as individuals – for example contracts of employment.

(b) Limited liability is very important for some charities, especially those providing services, where there can be a big risk of litigation if something goes wrong and trustees could be personally liable.

Our Experience:

At The Kubernesis Partnership LLP, we have significant experience in the formations of CIOs – both in England (the CIO structure) and Scotland (the SCIO) – and in helping existing charities and organisations to convert.

Recent clients which we have supported on this path include:

- a small international aid charity
- a charity providing specialist support to victims of domestic violence, with considerable public sector funding
- churches and other religious organisations, typically with buildings to transfer to a CIO
- two grant-making charities
- a specialist professional association.

We are also working currently with several others.

If anything went drastically wrong with the work of the charity and you faced a big legal action, or if you took out loans and circumstances changed and they could not be repaid, limited liability would be useful to protect trustees. Of course, many charities have considerable assets in the form of properties or investments, so limited liability would only offer additional protection if the charity faced debts in excess of these assets.

But if someone is going to sue the charity (even if the claim has no merit) it is much better if they sue a corporate body, rather than having court papers served on individual trustees.

(c) The process of converting to the CIO structure is a chance to look afresh at all kinds of issues in the governance of the charity – agreeing the CIO Constitution means creating a new governing document, rather than seeking to amend a trust deed which may be very out of date.

(d) On a practical level it is generally easier to deal with new trustee appointments in a CIO than a trust. The CIO is governed by a Constitution which would specify all the rules regarding AGMs, trustee elections etc.

(e) As a CIO, it is also easier to amend the governing document (the Constitution). There is no need for supplementary deeds. Amendments to the Constitution can be agreed by a 75% majority of members at an AGM – this corresponds closely to the existing arrangement in many charitable trust where the trust deed can be amended by a 75% majority.

Constitutional changes have to be registered with the Charity Commission before they take effect, but this is purely administrative. Any changes to the charitable objects require Charity Commission agreement (as in all charities) but administrative issues such as changing the number of trustees, quorums for meetings etc etc, can just be agreed by the members.

(f) For charities which have a wide membership structure, the CIO form allows a very clean arrangement with a two level of structure of members and trustees – as used by many associations. The members could be supporters, partner organisations, service users, etc. The members have a vote at the AGM when trustees are elected, and for changes to the constitution, but all day to day financial and operational decisions are taken by the charity trustees. (Members can be organisations or individuals.) However, where this distinction is not needed, a CIO can be formed whether the members and trustees are the same people.)

5. What are the disadvantages?

(a) Some people feel CIOs are new and unproven and hence risky. Initially it may take a bit more work with external bodies (e.g. banks) to explain the status.

However, the concept has been around for 6 years – the delay has just been the final regulations. CIOs have now been operational for well over a year in England & Wales with few problems reported (and they have already been operating for around three years in Scotland, albeit under a different legal framework).

(b) The conversion to a CIO technically involves forming the CIO and then voting to wind up the existing charity and transfer all asset and liabilities to the CIO. So formally you are closing one charity and starting a new one.

This involves a number of practical issues, on which you will almost certainly want some guidance from advisers such as ourselves. These issues will create some extra work – for example properties and staff contracts would have to be transferred and any external agreements made by the current trustees would have to be reinstated with the CIO. Likewise, any existing pension funds and pension commitments would need to transfer – which may create complex issues that need to be considered at an early stage.

Your bankers may need to open new bank accounts for the CIO as it is a separate legal entity – but it is worth trying to persuade the bank to allow at least the main account used for incoming standing orders to transfer to the CIO.

Likewise insurance arrangements and any other external affiliations would need to be transferred.

You may also need to negotiate with funders to transfer future support to the CIO. If you are a grant-making charity, and have grant recipients to whom you have promised multi-year grants, they should be advised that future obligations are transferred to the CIO. But they are hardly going to complain if you are still committing to support them as agreed.

So overall there is some effort involved in the process – it's not trivial but hopefully it's not enormous either. We will provide more specific guidance if you seek our help to proceed. Moreover, all these issues – though significant – are "one off" – in the long run, operating as a CIO will lead to some simplifications compared to the current arrangements (for example, no need to amend details at the Land Registry when there are changes of trustees).

(c) A further possible disadvantage is that if anything goes wrong with the transfer process it would be very serious – e.g. if you managed to lose valuable property. But we would strongly recommend you to instruct

solicitors to handle any property transfers (we can help with this – in terms of recommending a solicitor experienced in this area – and we can handle much of the briefing and communications with the solicitors).

However, there is always an argument for minimising difficulties by doing nothing – but if the current trust structure is unsatisfactory, postponing the change just keeps the difficulties for the future, and means trustees continuing to accept personal liability.

(d) Converting to a CIO will obviously cost more than just making a one-off change to the trust deed. But in the longer term, the benefits of corporate status, the simplicity of future changes, and the benefits of not having to have separate holding trustees could outweigh the short term costs.

(e) Any process which involves registering a new charity could involve queries or even outright refusal by the Charity Commission. No organisation can be registered as a charity unless it is established for charitable purposes for public benefit. Public benefit does not mean that everyone has to benefit – many charities work in a specific field – e.g. young people, or a certain geographical area – or people with a certain medical condition. But it does mean thinking about your beneficiaries in relation to your charitable purpose.

6. Are there other ways a charitable trust could incorporate?

Yes, other approaches are possible.

(a) You could become a *charitable company* – i.e. a company limited by guarantee which is also registered as a charity. There are a few subtle cases where this could be better than a CIO – for example if you ever needed to raise loan finance by means of a floating charge across all the assets of the charity. But raising loans in this way is rare for most charities. If you need to borrow against freehold property this can be done as a CIO. The real benefits of the charitable company lie mainly in the greater familiarity of external parties – but as mentioned this would mean complying with charity law *and* company law.

But as a charitable company you would have all the complexities of complying with company law *and* charity law. The attraction of a CIO is that it is governed solely by charity law.

(b) There is a further option of applying to the Charity Commission for *incorporation of the existing body of trustees* under section 251 of the Charities Act 2011. This means the trustees become a corporate body, so property can be held in a name such as “The Incorporated Trustees of XYZ”. However, the charity remains governed by the existing trust deed.

This is a bit simpler because it avoids the formal wind-up of one charity and transfer to a CIO. But whilst this offers corporate status, incorporation under section 251 does *not* offer limited liability: the trustees remain personally liable for decisions. Also, because the existing trust deed remains the governing document, it does not address any deficiencies in that: any changes have to be made by deeds of amendment, as at present.

7. Possible timescale for conversion to a CIO

If your trustees decide to proceed with becoming a CIO, it is best if the final transfer can take place at the end of an accounting year, to avoid non-standard financial years.

However, the process needs to be started a long time before year end – preferably quite early in the financial year – in order to allow for proper discussion at each stage. The table below shows a possible timescale for a charity with a 31 March year end.

A POSSIBLE TIMESCALE FOR CONVERTING A CHARITABLE TRUST TO A CIO

June 2014	Trustees agree in principle to convert to a CIO at next year end (i.e. conversion to take place on 31 March 2015).
June–July 2014	Consult supporters, funders, staff and others about the principle of the conversion. Consider any changes to current governing document (objects, numbers of trustees, voting, etc.) to be included in the CIO’s constitution. If the existing charity has members – rare for a charitable trust – fix date for a special members’ meeting in October to approve wind-up of existing charity (this could be combined with a normal AGM in charities where an AGM is held).
Aug–Sept 2014	Drafting of the CIO Constitution (allow for several drafts until everyone is happy). Detailed planning for the conversion process – allocate responsibilities and take professional advice at this stage on any issues which may not be straightforward (do not bury problems until later).
October 2014	New CIO constitution agreed by the applicants (the people to be the initial members – often the same as the trustees).

	Formal resolution passed to wind up the existing charity and transfer to a CIO 'as at 31 March 2015 or such other date as the trustees may decide'.
November 2014	Application to register the CIO is submitted to the Charity Commission.
December 2014	Responding to Charity Commission queries
January 2015	CIO is formed and registered on (say) 12 January. First meeting of the CIO trustees follows. Finalise transfer agreement between the old charity and the CIO (or pre-merger vesting declaration).
Feb–Mar 2015	Formally notify all parties that the transfer is proceeding. Open new bank accounts for the CIO if needed. Make sure all contracts are re-established with the CIO.
31 March 2015	Transfer date – all assets and liabilities of the old charity transferred to the CIO. Last accounts for the old charity will finish on this date.
1 April 2015	Work of the charity now undertaken through the CIO. All letters, brochures, website, emails, etc should now show the details of the CIO (not the old charity).
July 2015	Trustees of the old charity hold a final meeting to approve the last set of accounts (year ending 31 March 2015) and file with the Charity Commission.
31 March 2016	First year end for the CIO. First CIO accounts prepared for the period 12 January 2015 – 31 March 2016. (Note that the first accounts must start from the date of incorporation even though in this example the work of the CIO only began from 1 April 2015.)

Further information

Gareth Morgan is the author of the book *Charitable Incorporated Organisations* published in June 2013 by the specialist charity publishers Directory of Social Change. Copies can be ordered from The Kubernews Partnership LLP for £22.40 including postage – see www.kubernews.co.uk/publications. It includes sufficient detail to be usable by professional advisers with full references to all the regulations but is written in language understandable to anyone familiar with the charity sector. It provides detailed comparison of the CIO with other structures in the charity/social enterprise field and extensive discussion of the process of converting existing charities. It covers CIOs in England and Wales, Scotland (SCIOs) and Northern Ireland CIOs (when implemented).



There is some broad guidance about CIOs on the Charity Commission website [www.charitycommission.gov.uk/frequently-asked-questions/faqs-about-charitable-incorporated-organisations-\(cios\)/](http://www.charitycommission.gov.uk/frequently-asked-questions/faqs-about-charitable-incorporated-organisations-(cios)/) including model Constitutions. For SCIOs see the OSCR website www.oscr.org.uk/about-scottish-charities/scio/

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- If you are not currently in KCAS it is possible to register online (see www.kubernews.co.uk/advice-service) and then queries can be raised immediately subject to the terms of the scheme. For other enquires, please e-mail info@kubernews.co.uk.

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