

## Conversion of charitable companies and CICs to CIOs: now available in E&W from 1 January 2018

### Summary

We are delighted to confirm that after a long process of campaigning (in which Kubernes clients have played a significant part) Parliament has now passed the key regulations which will allow charitable companies and community interest companies (CICs) in England & Wales (E&W) to convert **directly** to become **charitable incorporated organisations** (CIOs). *See below and next page for the practical implications.*

The regulations take effect from 1 January 2018, although the Charity Commission will be operating a phased process (see below) so they do not get overwhelmed with too many applications at the same time.

This is a long-awaited measure: the legislation to allow conversion of charitable companies to CIOs was enacted in the Charities Act 2006 (now consolidated into the Charities Act 2011). But although CIOs were in the 2006 Act, it was not until January 2013 that the first CIOs could be registered in England & Wales, and it will now be a further five years after that before the conversion of charitable companies can begin.

By contrast – under Scottish charity law – the equivalent provisions have been in force for much longer. It has been possible to register Scottish CIOs (SCIOs) since April 2011, and the direct conversion of Scottish charitable companies to SCIOs has been possible since January 2012.

Most of the regulations are subject to the ‘negative’ approval process – so the Minister (Tracy Crouch MP) just had to lay the regulations in Parliament and they become law automatically – but one aspect required ‘positive’ approval – i.e. a vote in both Houses of Parliament (Commons and Lords). Approval in the Lords was given on 7 November and in the Commons on 23 November. Unless something fundamental happens to interrupt Parliament (such as another General Election being called before Christmas 2017) we can therefore be confident that the regulations will take effect from 1 January 2018. This means that from 2 January (the first working day of the New Year) the Charity Commission and Companies House will *by law* be accepting conversion applications. All the proposed regulations have been published in draft by the DCMS (the Government department now responsible for charity law in E&W) together with the outcome of last year’s consultation and the proposed timescales at:

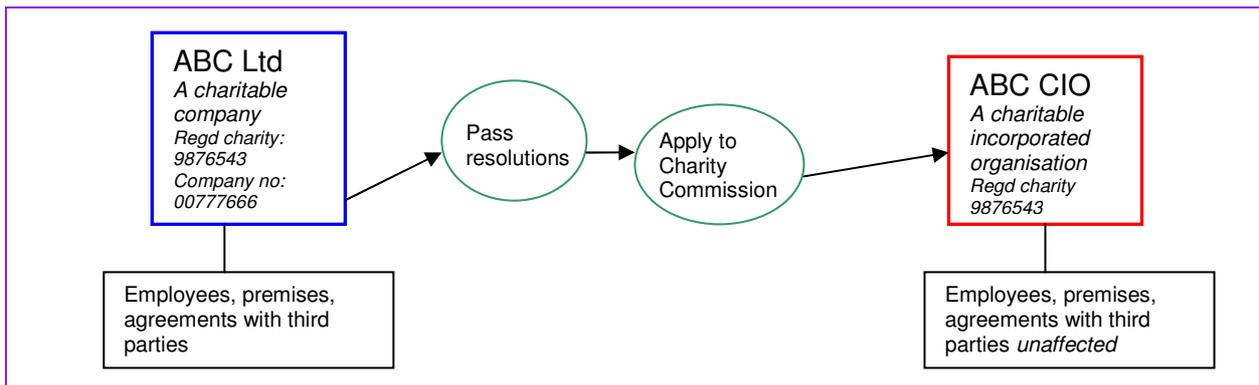
[www.gov.uk/government/consultations/converting-to-a-charitable-incorporated-organisation](http://www.gov.uk/government/consultations/converting-to-a-charitable-incorporated-organisation).

*At Kubernes, Gareth Morgan, has been specialising in the CIO framework for many years and we were active in the consultations that led to the latest regulations.*

*So we feel fully ready to work with charitable companies that would like to become CIOs in 2018!*

*Please get in touch as soon as possible if you may want to consider this (see last page for contact info). We will be offering reduced terms for the first few company/CIO conversions we handle.*

For more details on the process, see chapter 10 of Gareth’s book **Charitable Incorporated Organisations** – available to order from [www.kubernes.co.uk/publications](http://www.kubernes.co.uk/publications).



## Why would a company want to become a CIO?

Many charities are structured as *charitable companies* – they are formed by registering a company limited by guarantee at Companies House, and then an application is made to the Charity Commission (if the company is in E&W) to be registered as a charity. Similar arrangements allow a charitable company in Scotland or Northern Ireland to be registered with OSCR / CCNI as applicable. Sometimes people use terms such as ‘incorporated charity’ but many different kinds of charities are corporate bodies – including CIOs – so it is best to use the term *charitable company* (or ‘company charity’).

However, charitable companies have many disadvantages compared to CIOs, in particular:

- The charity trustees are also company directors and have obligations under charity law *and* company law.
- All changes of trustees/directors have to be notified to both Companies House *and* the charity regulator (Charity Commission / OSCR / CCNI).
- Accounts of companies have to be on a ‘true and fair’ basis, so even the smallest charitable companies have to follow the Charities SORP for their accounts, whereas a CIO under £250,000 income can produce receipts and payments accounts like other non-company charities.
- Members of a charitable company have to give a small guarantee (usually £1 or £5) towards wind-up costs, but this is not a requirement for CIOs.

There are many further issues. Particularly for small/medium charities and these create major complications in trying to run the charity effectively, and it can be hard to persuade people to become trustees if they have all these issues to consider.

CIOs offer many of the benefits which were previously only possible as a charitable company, in particular corporate status (so the CIO is a legal entity which can hold its own property and enter into contracts in its own name) and a CIO offers limited liability to members/trustees provided they act properly.

Because of these advantages, the vast majority of new charities are now being formed as CIOs. Around 60% of new charity registrations with the Charity Commission are now CIOs and with OSCR in Scotland as SCIOs. Well over 15,000 CIOs & SCIOs have been registered in the last few years.

### ***So, many trustees and staff of charitable companies are asking: could we convert to become a CIO and no longer have all the complications of company status?***

The answer is generally: **yes**. Furthermore, from January 2018 it is possible for a charitable company to convert *directly* to become a CIO (in E&W) or a SCIO (in Scotland). See below for more details.

Note: There are a few cases where a charitable company may be more appropriate than a CIO – mainly where the charity needs complicated loan finance (but there is no problem for a CIO with most loans whether informal loans, or mortgages secured on a building). But we believe that CIOs are much better and simpler in the majority of cases. Please get in touch to discuss these issues further.

## What is meant by *direct conversion*?

The direct conversion process – available from January 2018 in E&W – means that a charitable company can simply *become a CIO* – subject to passing some straightforward resolutions and Charity Commission approval.

Nothing transfers from one entity to another: it’s just like repainting a house in a new colour – it is still the same house! The corporate body simply changes from being a company governed by company law *and* charity law to being a CIO – the same corporate body but now with a simpler legal framework only under charity law.

So there is no need to transfer any employees or funding or premises – it is the same entity – just subject to a new legal framework. So there is no need to wait for the end of a financial year: in fact it would be best to *avoid* year end for a change of this kind.

Assuming the company is already a registered charity, there is no change to the charity registration number – but you would give up your company number). (If, however the company is not yet registered as a charity – for example because its income is under £5,000 – a new charity registration is involved in the conversion process because all CIOs regardless of size are registered charities.)

You may need a change of name – typically to add “CIO” on the end of the name in place of “Ltd”. But if the company had permission to omit “Ltd” from its name you could convert without changing the name – though bear in mind that a CIO must make its status clear on all literature if the letters “CIO” (or “SEC” in Wales) are not included in its name.

If your organisation started the year as a charitable company and finished the year as a CIO, you would prepare CIO accounts at year end for a normal 12 month period: the trustees’ report would simply explain the constitutional change that took place during the year. (But if you had not yet filed accounts for the previous year, they would, of course, need to be accounts for a charitable company.)

Naturally such a conversion needs careful discussion with trustees before going ahead (and with members in a charitable company with a wider membership). And of course, if you have any conditions from funders or lenders that you must get their approval for any constitutional changes, you must check they are happy – but

unless your CIO constitution will have weaker governance arrangements it is hard to see on what basis a funder might object. (For a lender it may be a bit more complex, but except in the case of a company with a 'floating charge' which is rare with charities, a lender should not normally have concerns.)

### Why is the direct conversion so much better than before?

Until the new regulations take effect in E&W in January 2018, if a charitable company wanted to become a CIO, it was necessary to form a CIO as a completely new entity, pass resolutions in the company to transfer everything to the CIO, and then arrange to dissolve the company – essentially the same steps needed as transferring an unincorporated charity into a CIO. This meant negotiating with funders to transfer funding and transferring employees. If the charity held premises, solicitors had to be engaged to transfer the property. Complications can arise with existing agreements with suppliers (e.g. equipment leases), with landlords with pension funds and much more. So *until now* it has generally been better for an *existing* charitable company to stick with company status, even though new charities are being formed as CIOs.

### My charity is a company – can we convert to become a CIO in January 2018?

In order to avoid the Charity Commission being overloaded with applications, a phased timescale has been agreed as follows.

The earliest date you can apply to convert is based on the *total income* of the charitable company in its most recent accounts/annual return. But we are delighted that *priority is being given to the smallest* charitable companies – which are hit the hardest by the complications of being companies rather than CIOs.

- From 1 Jan 2018: Applications accepted from charitable companies below £12,500 income
- From 1 Mar 2018: Applications accepted from charitable companies below £25,000 income
- From 1 May 2018: Applications accepted from charitable companies below £100,000 income
- From 1 June 2018: Applications accepted from charitable companies below £250,000 income
- From 1 July 2018: Applications accepted from charitable companies below £500,000 income
- From 1 Aug 2018: Applications accepted from charitable companies of any size.

However, there are a number of steps to be taken before an application to convert can actually be submitted to the Charity Commission –

(1) The trustees/directors need to agree in principle to proceed with a conversion and unless they have a lot of expertise will need to seek professional advice on the detailed steps that follow.

(2) A new CIO Constitution must be prepared which will *replace* the company's Articles as the governing document of the charity – this may take several drafts before it is presented to members.

(3) A general meeting of members of the company must be called to pass special resolutions (a) to convert to a CIO (if agreed by the Charity Commission) and (b) to adopt the new CIO Constitution in place of the Articles.

(4) The resolutions and new Constitution are sent to the Charity Commission which liaises with Companies House. If all is OK, the charity ceases to be a company and continues as a CIO.

So if you are looking to convert your charitable company to a CIO at any time in the first half of 2018, we would recommend *starting the process right away* in order to be ready to submit the application in the first slot above depending on your income. Please get in touch for further advice.

But if you are involved in a small charitable company (under £12,500 income), and you are very focused with trustees/members ready to make speedy decisions, it would just about be possible to complete the steps above in time to be one of the very first conversions in early January 2018!

Note that the conversion process is *not* the time to make other big governance changes. In order to use the direct conversion process, the charitable objects must be substantially the same before and after conversion, and the members of the company must become the members of the CIO.

However, in the normal case of a company limited by guarantee, the members' guarantee can be *removed* as part of the conversion if (as usual) the guarantee in the company's articles is no more than £10 per member.

### What if we are a Scottish charitable company: registered with OSCR?

The good news is that Scottish charitable companies can *already* convert directly to become SCIOs, following largely the same process as above. This has been possible since 2012 – so England & Wales are finally catching up!

However, we feel the Scottish process for direct conversions has not received much publicity and many of those working with Scottish charities rarely mention this. *We feel there are many small and medium-sized Scottish charitable companies which could greatly simplify their affairs by converting to SCIOs.*

*Since 2016, Kubernews has been operating from our dual bases in Yorkshire and in Scotland, but we have long had a detailed involvement in the Scottish charity framework and the rules on SCIOs.*

*So we are well placed to support Scottish charitable companies that wish to become SCIOs.*

As in England and Wales, the process can take place at any time in the year, and the SCIO will keep the same charity number as before.

Moreover in Scotland (unlike in E&W) it is also possible for a charitable community benefit society (CBS) (formerly known as an Industrial & Provident Society) to convert directly to a SCIO.

### What about charitable companies in Northern Ireland?

Although CIOs are on the statute book in Northern Ireland under the Charities Act (Northern Ireland) 2008 they have not yet been implemented. So CIOs cannot yet be registered in NI and therefore an NI charitable company cannot, as yet, convert to an NI CIO.

However there is a lot of interest in CIOs in Northern Ireland, and we hope the registration of CIOs by the Charity Commission for Northern Ireland will become possible within the next year or two. The conversion of NI charitable companies can then follow.

### What about community interest companies (CICs)? Can a CIC become a CIO?

The answer to this question is: yes. Once the various sizes of charitable companies have had a chance to apply to convert, it will also be possible for a CIC to convert to become a CIO. Direct conversions of CICs to CIOs in E&W are due to start from 1 September 2018. The provisions for CIC conversions are included in the regulations now approved by Parliament.

However, direct conversion of CICs to CIOs will only be possible in England & Wales (there is no provision for a Scottish CIC to convert directly to a SCIO).

Community interest companies (CICs) are a special form of company intended primarily for non-charitable social enterprises. CICs are formed by registration at Companies House and with the CIC Regulator – they are *not* charities so can never be registered with the Charity Commission. A CIC only has to meet a 'community interest' test which is much broader than the public benefit requirements in charity law, and a CIC can have paid directors and can distribute up to 35% of its profits to shareholders. (We have supported a number of Kuberthesis clients in forming CICs – often as a non-charitable trading subsidiary of a charity.)

Most CICs are deliberately set up to be outside the framework of charity law and most would not want to become charities, as charitable status would limit what they can do.

But some organisations have been persuaded to set up as CICs where, on reflection, they would be able to achieve their vision much more effectively as charities. This is particularly the case with CICs set up with unpaid boards and with no intention to distribute profits. As a CIC, it is hard to access charitable grants, and there are no charity tax concessions. Many local authorities are reluctant to offer business rates relief to CICs. But, if a CIC converts to become a CIO – which would mean meeting all the requirements of charitable status, including adopting charitable objects and meeting the public benefit requirement, and (in most cases) being governed by voluntary trustees – it could then have all the benefits of charitable status.

And from autumn 2018 this will be possible – a CIC will be able to convert *directly* to a CIO, so it would then become a registered charity. But it would retain its existing corporate identity so there would be no need to transfer staff, premises or contracts.

Nevertheless, for a CIC to convert to a CIO involves preparing a CIO Constitution to replace the CIC's Articles, and then the full charity registration process, so it needs a lot of careful planning. Moreover, a CIC to CIO conversion will *only* be possible at times of year when the CIC has no outstanding accounts to file.

This Bulletin is prepared primarily for charities and professional advisers who belong to the [Kuberthesis Charity Advice Service](#) – but may be used by others on an "as is" basis.

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

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