

National Churches Trust



Charitable Incorporated Organisations-CIOs

Introduction

From January 2013 charities have been able to register as a Charitable Incorporated Organisation (CIOs). This new simplified structure will allow local trusts to take steps to protect their individual trustees from being personally liable for the activities of the charity by moving to this structure. Currently the majority of local trusts have a charity structure that is either an 'unincorporated trust' (governing document: trust deed) or 'unincorporated association' (governing document: constitution or rules). It is important that each trust understands the level of protection these structures offer their trustees and the issues that need to be considered when trustees undertake various activities in the trust's name. A CIO structure may not be the ideal solution for all local trusts and we would always recommend that you consult with your professional advisors before making a decision, however a CIO structure is likely to be attractive to those trusts that enter into contractual obligations, employ staff, own property or take on leases. A review of the alternative options available to you and the benefits of changing to a CIO will allow your trust to make a more informed decision about its future.

This document discusses CIOs and compares them to other existing structures, it considers their benefits, how to go about changing to a CIO status and other key issues that need to be considered. You will also find attached a draft constitution for your trust to use as a template for submission to the Charity Commission. There is a section on obtaining professional advice and an estimate of the costs involved in converting your status to that of a CIO and finally the contact details for the various advisors who contributed to this document.

What is a CIO and why change?

A Charitable Incorporated Organisation (CIO) offers charities and charity trustees a legal structure broadly equivalent to that associated with a limited company but without the need to register with Companies House.

If the current structure of a local trust is unincorporated the charity does not exist as a recognised legal entity in its own right, and therefore has to act through its trustees. This means that:

- the trustees are personally liable for the debts, contractual obligations and financial liabilities of the local trust. Whilst trustees are able to seek reimbursement from the assets of the local trust, if these are insufficient to meet the obligations the trustees are personally liable for any shortfall.
- the local trust cannot enter into contracts or control some investments in its own name, all contracts have to be entered into with the individual trustees and investments registered in the names of the individual trustees, therefore when you change trustees the contracts and investments need to be changed into the names of the new trustees.
- two or more trustees, a corporate custodian trustee or the charities' land holding service will have to 'hold' any land or investment on your charity's behalf as it cannot be registered in the name of the local trust itself.

Adopting a CIO as your corporate structure

A way of overcoming these issues is to establish the local trust charity as a corporate entity which will be recognized as a legal structure in its own right. Until the introduction of the CIO (governing document: constitution), charities wishing to exist as separate legal entities had to establish a company limited by guarantee (governing document: memorandum and articles of association).

Using a limited company structure or a CIO structure gives your charity the legal capacity to do many things in its own name, such as:

- employing paid staff
- entering into commercial contracts in its own name
- owning freehold or leasehold land or other property
- delivering charitable services under contractual agreements

Members of a company limited by guarantee have limited liability for its debts if it winds up. Members of a CIO may either have no liability or limited liability. This gives your individual trustees protection against being liable for the debts and other financial liabilities of the local trust.

In addition, the Directors of a company limited by guarantee, or the trustees of a CIO, are not personally liable for the debts, contractual obligations or financial liabilities of the charity. If a claim is made against the charity that exceeds the funds of the charity the trustees are not liable for the shortfall. (There are some limited circumstances where the trustees may still be personally liable under insolvency legislation or where they have exceeded their powers under the constitution.)

A CIO is very similar to a company limited by guarantee, but there are some differences. One of the main benefits of opting for a CIO structure when compared to a limited company is its simplicity. Charitable companies have to file accounts with two regulators, one with the Charity Commission and one with Companies House, which can be costly. There are also numerous regulations arising from both charity and company law which need to be followed. A CIO structure is regulated by the Charity Commission alone and all CIOs must register with the Charity Commission. Company law does not apply. CIOs must produce accounts under charity law; this allows those with income below £250k to produce simpler receipts and payments accounts.

Like companies (which must have both members and company directors) all CIOs must have members and charity trustees. Some CIOs may want the only members to be charity trustees; others may want a wider membership open to other people. The Charity Commission has produced two draft constitutions, the one included within this pack is based on the 'foundation' model for trusts whose only voting members will be the trustees. It is anticipated that this constitution will be the one most widely adopted by local trusts wishing to convert to a CIO status, however the second structure of 'association' should be considered as part of your decision making process.

Key issues to consider

The trustees need to consider if the objects of the CIO are the same as the existing charity or whether they need updating. For example has the geographical scope of the charity's work changed? If you are going to change the objects of the charity then you will need to consider the impact of this on the potential transfer. For example, if the objects of the new CIO are wider than the objects of the "old" charity then any funds transferred across to the new CIO will need to be held as a restricted fund for use in accordance with the "old" objects. If the objects of the new CIO are narrower than the "old" charity's objects then this will not be an issue. For example, say the objects of your old charity stated that its purpose was to award grants for the repair of church roofs, you may wish to broaden these objectives under the new charity to include not only church roofs but the entire fabric of a church building. In this case any funds that existed under the old charity would become restricted and could only be used for grants awarded towards the repair of church roofs (as per the old charity's objectives). You could also provide for the dissolution of the charity and state where the funds of the charity would go. Charity trustees will also need to review the assets and liabilities held by the charity to make sure that everything is transferred over to the new entity, for example property, bank accounts, investments, shares, external licenses, contracts, employees, etc. The old Charity will need to prepare a set of accounts reflecting the transfer of its assets, liabilities and activities to the new Charity. Ideally the transfer document needs to reflect a transfer as having taken place as close to midnight as possible on the last day of the relevant month (ideally at the year-end). Your accountants will be able to assist you with this process and with any tax implications of the transfer which should be minimal in most cases.

Depending upon the number of employees that are transferring, you will also need to consider the legal obligation to consult with the employees about the proposed transfer as they will be moving to a new employer. Failure to consult with employees can lead to claims for compensation. If you are considering changing any of the terms and conditions of your employees you will need to consult the employees.

You will also need to consider what to do with the remaining "shell" of the old charity. If you regularly receive legacies, then you may wish to keep the "shell" so that any legacies in the future can be claimed. If you decide to dissolve the old charity, then it will be necessary to enter the "incorporation" onto the Register of Mergers with the Charity Commission. This will mean that, in future, any payments meant for the old charity such as legacies will automatically be diverted to the CIO. However, you should note that if a legacy is left to the local trust "provided it shall still exist at the date of the deceased's death", then the gift would not be caught by the Register of Mergers and would fail. For this reason, charities that receive a lot of legacies often keep the shell charity in place. If you need to do this, then you should consider taking advice from a solicitor as to whether the CIO can become the corporate trustee of the "shell" charity.

How do we become a CIO?

CIO may not be the ideal solution for all local trusts. Charities/trusts wishing to work out whether CIO status will suit them should consult with their professional advisor. It is not yet possible for charitable companies limited by guarantee to apply for conversion to a CIO.

Set up a foundation CIO if you want your charity to be a corporate body. In order to do this you must follow the core steps below:

- have a constitution as your governing document – The Charity Commission have produced two model constitutions. The one attached is based on the foundation model for charities whose only voting members will be the charity trustees.
- register your CIO with the Commission for it to legally come into existence. Note the CIO will be given a new charity number and, for all intents and purposes, it will be a new charity. To do this you should complete the appropriate CIO constitution template as your new CIO's governing document. Once the trustees agree the constitution, register your new CIO by applying to the Charity Commission using their on-line application system. Once submitted a decision can usually be made in 40 working days, providing:
 - You can use the model wording for your objects from the Charity Commission website
 - You can show that all your activities are or will be consistent with your objectives
 - You can show that any private benefit is only incidental and is properly managed
 - You are able to use the Charity Commission model governing document
- You transfer your property and operations to the CIO (existing unincorporated charities only, you should check whether your charity can transfer its property in this way; you may need authorisation from the Commission). This is normally done by the "old" charity and the CIO entering into a transfer agreement that transfers over all of the assets and liabilities of the "old" charity to the CIO. If the trustees of both the "old" charity and the CIO are the same, you will need Charity Commission consent (by means of a "section 105 Order") to enter into the transfer agreement due to potential conflicts of interest. If your charity has any permanent endowment then special consideration will need to be given to how this is transferred across to the CIO and we would suggest you take specialist advice.

Once CIO status has been obtained the follow up steps below should be completed:

- You need to make sure that all appropriate insurance arrangements are transferred to the CIO.
- You will need to register the CIO with HMRC for tax purposes.
- You will need to notify all third parties that you deal with that the operations of the "old" charity have been transferred across to the CIO. You need to be careful to consider whether transferring in this way will cause any existing arrangements to terminate and incur termination charges (for example if a photocopier lease has to be terminated and entered into again by the CIO).

- You will need to open new bank accounts in the name of the CIO, which will also mean transferring all standing orders and direct debits across to the new accounts as well as notifying any donors that they are now donating to a new charity.
- You will need to keep a register of its trustees (who are also the members).
- You will need to display the CIO's name at the CIO's principal office and include the name and charity number on all business correspondence.
- You will need to send accounts and an annual return to the Commission each year, regardless of its income.

Advantages of becoming a CIO

- The charity would become a legal entity in its own right, property and contracts could be registered in the name of the CIO; there would be no need to change the title to properties when there are changes of individual trustees and as contracts would be made in the name of the charity these could simply transfer to the control of the new trustees without being renegotiated.
- The CIO structure offers limited liability; this protects the individual trustees from being personally responsible for the debts of the trust, also any legal action taken against the trust would be in the name of the corporate body not the individual trustees.
- The structure is very similar, in practice, to the structure of a charitable trust (albeit with a separate corporate existence) so will seem familiar to trustees and not involve significant change.
- 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 since a new constitution would have to be created rather than amending the original trust deed which may be out of date.
- It is generally easier to deal with new trustee appointments under a CIO. The constitution will specify all the rules regarding AGMs, trustee election etc.
- As a CIO it is easier to amend the constitution; a 75% majority is needed at an AGM. Constitutional changes have to be registered with the Charity Commission, however administrative issues such as changing the number of trustees, quorums for meetings etc. can just be agreed by the members.
- A CIO with gross annual income of £250,000 or less can choose to prepare receipts and payments accounts, or accrual accounts.

Things to watch out for.

CIOs are a relatively new concept and may have to be explained to external bodies such as banks. Most banks have tended to see conversion to a CIO as simply a conversion, rather than creation of a new charity, so have not required new bank accounts to be opened.

- If you receive grant income from funders you will need to negotiate with them so that future funding is transferred directly to the CIO.
- Converting to a CIO status means that the existing charity is wound up. You will therefore have to seek guidance from your professional advisors. For example properties and staff contracts will have to be transferred and any external agreements made by the current trustees would have to be reinstated with the CIO. There will be some costs involved with converting your trust's status to a CIO. (see p7) The CIO will be an entirely new charity with a new charity number.
- Those trusts using the Gift Aid Small Donations Scheme (GASDS) will have to apply to HMRC for a certificate permitting the new charity to take on the Gift Aid History from the old charity. This will allow the CIO to claim under the GASDS straight away. The application for a certificate must be made in writing to HMRC before the earlier of 60 days before the new charity makes its first Gift Aid Exemption claim; or 90 days after the new charity began to carry on the activities of the old charity.
- The CIO structure may not be the ideal solution for all charities. Those with substantial assets or complex operations and relationships with other entities may be best advised to stick to existing incorporated structures for which the responsibilities and rights of members, directors and trustees have been tested in court.
- There is little in the way of precedent case law or guidance to answer any anomalies that may arise.

Professional Advice

It is important that your trust receives professional advice before making a decision to amend the corporate structure of your charity. This advice can be obtained from accountants and law firms who specialise in the charity sector. Trustees should also consider securing appropriate trustees indemnity insurance from a reputable insurance company.

The potential costs to use professional advisors to establish a CIO, register it with the Charity Commission and put in place the necessary documentation to enable the transfer to happen will vary from charity to charity depending upon your particular circumstances. As a general guide, the legal costs are likely to be in the region of £7,500 to £10,000 plus VAT, excluding advising on the transfer of employees and arrangements to transfer or register property which normally incur additional costs. If you are looking to change your objects as part of the incorporation process or have a permanent endowment, this will also involve further work.

The leading charity law firm Stone King LLP are prepared to offer local trusts a standardised package for completing the incorporation process. Their services are broken down into two parts.

a) Core Components:

- Finalising the Constitution (using the model)
- Applying to the Charity Commission to register the CIO
- Applying to the Charity Commission for a section 105 order to authorise the transfer of assets/liabilities
- Transfer Agreement between charitable trust and CIO
- Resolution of the charity trustees of the charitable trust
- Minutes for the first board meeting of the charity trustees of the CIO
- Preparing Trustees/Members statutory registers
- Template letter to third parties
- Note re use of CIO name and number
- Entry onto Register of Mergers at the Charity Commission

(b) Specialist areas:

- TUPE transfer of any employees (including pension issues)
- Transfer of property (including first registration of unregistered property)
- Transfer of permanent endowment / restricted funds
- Arrangements to leave a shell charity to catch legacies
- Setting up as an Association CIO with membership wider than just the trustees
- Registering with HMRC for tax purposes (normally done by the CIO's accountants)

In terms of the core components, their costs would normally be in the region of £5,000 plus VAT. However they are willing to offer this element to local trusts for a fixed price of £3,000 plus VAT, providing the attached draft constitution (drafted by Stone King LLP) is used with appropriate amendments for your particular charity. For the specialist areas, these would be charged at their usual hourly rates applying a 5% discount, and separate estimates can be provided for these elements on request. If you wish to use this package, please contact Tim Rutherford at Stone King LLP (contact details below) quoting "NCT Local Trusts CIO".

The Following Professional Advisors Contributed To This Document.

Charity Accountants

As one of the top 10 accountants in the not for profit sector, Buzzacott has had a number of enquiries about the benefits of CIO status and has discussed the merits and drawbacks with trustees, management and legal advisors. Amanda Francis, Managing Partner of Buzzacotts recently spoke at the annual CTF conference about this issue.

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Appendix 1

The Charity Commission's steps to converting to a CIO status

1. First Choose/Prepare a constitution which best matches your original charity, take professional advice if you think you need it.
2. Register your new CIO with the Charity Commission, using their online application form.
3. Once your CIO is registered, transfer your original charity's assets to it, ideally making sure you settle debts first. The two charities' purposes must be sufficiently similar and the original charity's governing document must allow you to give away all assets, if not you may need the commission's approval.
4. Once the asset transfer has completed, close your original charity in line with any rules set out in its governing document and notify the commission that it has been closed.

Appendix 2

The Charity Commission's Checklist for changing your charity structure

1. **Choose the right Structure**-Discuss the types of charity structure set out in the Charity Commission's 'charity types: how to choose a structure (cc22a) and choose the right structure for your charity'.
2. **Agree your charity's purposes**-Discuss your charity's purposes (the objects clause in its governing document) and update them if necessary in line with the Charity Commission's guidance 'How to write charitable purposes.'
3. **Decide how any asset will transfer**-Check that your governing document allows you to transfer your existing charity's assets -these rules are likely to be in its dissolution clause. If it doesn't, you may need the commission or another body to approve the transfer.
4. **Make sure your charity is up to date with admin and filing**-Make sure your most recent annual return and accounts have been submitted to the commission.
5. **Decide if you need to take advice**-Take professional advice if you need to plan your restructure.
6. **Apply to the Commission using its online application form**-The commission can't accept incomplete applications because it needs to be satisfied that your new organisation is a charity and eligible to register. You will also need to confirm that your trustees understand their role and responsibilities.
7. **Say that the new charity is replacing an existing one**-Make sure you complete the relevant section in the application form, you'll be asked for the original charity's number.
8. **Explain any changes to your charity's purposes**-Tell the commission about the changes to your objects and your reasons for making them-there is a section in the form.
9. **Give details of any assets that will transfer and how**-Explain which assets will transfer, the powers you have to do this and any approvals you've had to get. This is particularly important for a permanent endowment-an asset with conditions on how it can be used.
10. **Upload all necessary documents as PDF files**-You need to provide your new charity's agreed governing document, a signed copy of your trustee declaration, proof of income and other supporting documents.

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