Help Sheet:

A guide to the legal forms available to Charities

Charity + Caring

Not-for-profit organisations fall into two broad categories: charities and social enterprises. The key difference between these two categories is around who has overall control at decision making level and if those individuals are able to extract funds either by salary or distribution (dividend).

In general, charities are controlled by a volunteer Trustee Board with employed staff doing the day to day delivery and implementing the strategy of the Board. The Board making the decisions makes no personal financial gain. Charities tend to be at least part grant funded and a prerequisite of much of this funding is around charitable status and the inability of those charged with governance (i.e. the Board) to extract funds personally.

Social enterprises can be controlled by those who have invested in them and or those paid to work for them. This can be the individual(s) who own the business, all the staff together, the customers or a number of people who have bought "community shares" in the enterprise. Social enterprises generally operate via the selling goods and services, and by inviting people to invest in them, rather than by applying for grants and donations.

The remainder of this help sheet will focus on the options available for those looking to select a structure for their charity. Our help sheet "A guide to the legal forms available to Social Enterprises" examines the structures available to those entities.

Options available for the legal structure of a charity

Selecting the appropriate structure for your charity can be a daunting choice. It is important that the Trustees make the right decision for the organisation first time as any change of organisational structure at a later date is likely to be a complex process involving administrative burden and expense.

The most appropriate legal form for your charity will vary based on the intended scale, nature of the proposed activities and how it is to be governed, for example if you want it to have a wider membership.

Some charity legal structures are corporate bodies

If the structure constitutes a corporate body, the law considers your charity to be a person in the same way as an individual. This gives the charity legal capacity to do many things in its own name, rather than the trustees taking personal responsibility, such as

- employing staff
- delivering charitable activities under contractual agreements
- entering into commercial contracts
- owning property

Within corporate bodyies, generally trustees are not personally liable for what it does and they benefit from the protection afforded by limited liability.

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Broadly there are four different types of legal entity available:

- charitable company limited by guarantee
- charitable trust
- charitable unincorporated association
- charitable incorporated organisation.

Charitable Company Limited by Guarantee

This is probably the most common legal form seen in practice. A charitable company limited by guarantee is registered at Companies House and as a charity with the Charity Commission. Such a company does not usually have a share capital or shareholders, but members who act as guarantors. The guarantors give an undertaking to contribute a nominal amount (typically no more than £10) in the event of the winding up of the company. The members are often also the Trustees, although there may be members who are not Trustees. In these cases key decisions are taken to the membership at members' meetings and put to the vote. The administration and activities of the charitable company are governed by a set of Articles of Association which detail the objectives ("objects") of the charity. As a company limited by guarantee is a corporate body it can enter into legal contracts and hold property in its own name.

There is extra formality and expense with a limited company, as it will have to comply with both the Charities Act 2011 and the Companies Act 2006, laws which are not always clearly compatible. A charitable company is required to submit returns to both Companies House and Charity Commission and to produce financial statements which comply with both charity and company law. The Trustees also have additional duties placed on them as they would not only need to comply with trustees' duties under the Charities Act but also directors' duties under the Companies Act.

Charitable Trust

A charitable trust is simple and inexpensive to set up. It is governed by a Trust Deed, the contents of which can be more flexible than incorporated entities as there is no statutory framework that must be complied with. A charitable trust reports to the Charity Commission and is required to file an annual return and to produce financial statements which comply with charity law.

A charitable trust is not a separate corporate body so the trust cannot enter into legal agreements, which means the Trustees enter into agreements in their personal capacity which potentially creates a personal liability. As there is no Trustee limited liability protection afforded by this type of entity it is generally unsuitable for anything other than a simple organisation with non complex affairs.

Charitable Unincorporated Association

A charitable unincorporated associated is simple and inexpensive to set up. The charitable association is governed by a constitution not prescribed in law, however it does need to include features such as a prohibition on the distribution of funds to members, which is required to secure charitable status. A charitable incorporated association reports to the Charity Commission and is required to file an annual return and produce financial statements complying with charity law.

Like a charitable trust, this structure is not a corporate body and carries no limited liability protection for its Trustees. Again, from a Trustee perspective this makes it unsuitable for anything other than a simple organisation with non complex affairs.

Charitable Incorporated Organisation (CIO)

A CIO is the newest of the legal forms available for a charity and is specifically designed for use by charities. The other forms adapt existing types of legal forms which can mean compliance with multiple regulations which do not always sit well together. It is incorporated and regulated by the Charity Commission alone so there is only one legal framework to comply with. A CIO is governed by a constitution, the form of which is prescribed by the Charity Commission and is less flexible than a trust or unincorporated association.

The CIO can adopt either the Foundation Model Constitution or the Association Model Constitution, the former governed by voting members and the latter by Trustee members.

A CIO's members benefit from limited liability and it has its own legal personality allowing it to enter into legal agreements in its own right. A CIO reports to the Charity Commission and is required to file an annual return and produce financial statements which comply with charity law.

This structure is relatively new and remains untried, which could pose potential problems when the charity seeks finance from financial institutions who may be unfamiliar with this structure. One particular concern with CIO's is that the regulations make no provision for the Charity Commission to keep a register of charges e.g. a mortgage. The CIO model may therefore be unsuitable for charities with significant assets or those who may need to obtain debt finance.

12,500 CIO's have been registered since the introduction of the model in 2013 and it has certainly proved to be a popular option for Trustees looking to move away from one of the other structures to provide liability protection and/or avoid the complexity of multiple regulators.

Historically, changing charitable structure involves setting up a new charity, transferring the charity's assets and liabilities and closing the old charity. However draft legislation has been laid before parliament for approval and, if approved, will allow community interest companies (CIC's) seeking charitable status and charitable companies to quickly convert into CIOs from January. A move from unincorporated status to CIO would still however involve the asset transfer and closing down process.

Charity Commission guidance CC22a - Charity types: how to choose a structure provides Trustees with further details and points to consider when selecting and reviewing the structure of their charity.

Further information

If you would like further information, or for how our Charities team may be able to help you, please contact us at hello@garbutt-elliott.co.uk