

CO-OPERATIVES AND COMMUNITY BENEFIT SOCIETIES ACT 2003

EXPLANATORY NOTES

INTRODUCTION

1. These explanatory notes relate to the Co-operatives and Community Benefit Societies Act 2003 which was introduced as a Private Member's Bill by Mr Mark Todd MP and sponsored in the House of Lords by Lord Carter, and received Royal Assent on 10th July 2003. They have been prepared by HM Treasury in order to assist the reader in understanding the Act. They do not form part of the Act and have not been endorsed by Parliament.
2. These notes need to be read in conjunction with the Act. They are not, and are not meant to be, a comprehensive description of the Act. So where a section or part of a section does not seem to require explanation or comment, none is given.

BACKGROUND AND SUMMARY

3. The purpose of the Act is to amend the law relating to societies registered under the Industrial and Provident Societies Act 1965 ("the 1965 Act"). There are two forms of such societies – 'bona fide co-operatives' and 'societies conducted for the benefit of the community' (community benefit societies) – which offer an alternative corporate structure to companies regulated under the Companies Acts. Bona fide co-operative societies are run by their members, for their members, whilst community benefit societies are enterprises which benefit the community and in relation to which there exist special reasons why they should not be registered as companies. Such societies can carry out a wide range of services, for example they can be retail societies, agricultural societies, housing associations or working men's clubs.
4. The aims of the Act are to:
 - enable the Treasury to bring forward, in secondary legislation, provisions under which community benefit societies could permanently prevent any use of or dealing with their assets except for the benefit of the community (*section 1*);
 - bring aspects of industrial and provident society law relating to societies' ability to enter into transactions into line with the corresponding legislation relating to companies, so as to provide protection for those dealing with societies and society committees from adverse consequences if a society or its committee were found to have acted outside the society's rules (*sections 2 & 3*);
 - bring aspects of industrial and provident society legislation into line with the position in company law in relation to how societies execute deeds and documents and enter into contracts (*sections 4 & 5*).
5. Currently it is not possible for investors in a community benefit society to be certain that its assets will always be used for the purpose of serving the community. For example, it is possible for a society to convert into a company and use its assets in whichever

way it wishes. The Strategy Unit Report Private Action, Public Benefit noted that this situation posed a “serious deterrent to funders” of these societies. The aim of **section 1** is to address this situation, by allowing for a regime under which members of a society could vote to prohibit irrevocably the distribution of assets other than for the benefit of the community, or the conversion of the society to a company or the transfer of its assets to another body, unless that company or body was also subject to a regime irrevocably restricting the use of and dealing with those assets (an asset “lock-in” regime).

6. Currently a society must limit itself to activities which are permitted by its rules. This creates a risk for those dealing with societies that transactions may be void if a society has acted outside its powers. Further, if the committee of a society has acted beyond its powers in entering a transaction, then the transaction will be void, even if it is within the powers of the society itself. These risks place a burden on a party to a contract with a society to verify that the society’s rules permit it to enter the proposed contract, and to check that the committee is acting within its powers. This in turn may increase the costs and time involved in entering contracts, or deter some from conducting business with a society because they perceive there is a risk of the contract being void.
7. The aim of **section 3** is to remove these costs or risks by applying to societies and their committees provisions mirroring certain provisions which currently exist in company law. The section will ensure that an act done by a society is not void simply because it is not permitted by the society’s rules, or because the society’s committee acted outside its powers in relation to the act. In addition, a party to a transaction with a society is relieved of the burden of having to enquire whether the transaction is permitted by the rules, or about any limitation on the powers of the committee to bind the society. But the provisions do not absolve the committee members from their duty to observe any limitation on their powers flowing from the rules, so they will remain liable to the society and the members to make good any loss resulting from acting outside those powers. The section includes special protections for societies which are charities, and **section 2** imposes on those societies obligations to ensure that their charitable status is clear in business documentation.
8. A person involved in setting up a society may wish to make contracts in the name of that society before it has been legally registered. At that stage the society does not exist as a legal entity and any obligations or rights in the contracts entered into at this stage may be unenforceable. **Section 4** addresses this situation, by allowing contracts to be enforceable against and by the person who has acted for or on behalf of the society.
9. Currently societies have to have a common seal, and have to use that seal when they enter into certain types of contracts or execute certain types of other documents. The need to have a common seal may impose a cost of having to have a seal made, and kept safe, and there may also be risks in having documents sent to where the seal is kept. **Section 5** removes these burdens by allowing societies to operate without a common seal, but also enables societies which do have a common seal to have further official seals for use overseas.

COMMENTARY ON SECTIONS

Section 1: Community benefit societies: power to restrict use of assets

10. Subsection (1) enables the Treasury to make regulations to enable community benefit societies to ensure that some or all of their assets can only ever be used or dealt with for the benefit of the community. The regulations may define which community benefit societies have this option.
11. Subsection (2) enables the Treasury to prescribe in the regulations the purposes which are for the benefit of the community to which a community benefit society may “lock-in” its assets.

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12. Subsection (4) lists certain particular matters which the regulations may cover. For example it provides that the Treasury may make regulations about the procedure by which a society can adopt an asset “lock-in”; about how assets which have been “locked-in” must be dealt with in certain circumstances, such as insolvency, in which the asset “lock-in” may cease to apply; and to ensure that any person to whom “locked-in” assets are transferred can only use them for the same purposes for which the society could have used them.
13. Subsection (5) provides for the Treasury to include in the regulations other provisions for giving effect to an asset “lock-in” regime. For example, functions may be conferred on a person specified in the regulations to supervise compliance with the asset “lock-in” regime. It also permits the regulations to create criminal offences, though these may not be punishable by imprisonment for a term of more than seven years (see subsection (6)).
14. Subsection (8) requires any regulations under this section to be approved in draft by affirmative resolution in each House of Parliament before they are made.

Section 2: Status of charitable societies to appear on correspondence etc

15. **Section 2** inserts a new section 5A into the 1965 Act, requiring industrial and provident societies which are also charities to declare their charitable status on all correspondence and other official documents. Section 3 of the present Act relates to transactions performed outside the rules of the society. For those wishing to do business with societies it is important to know whether or not the society concerned is a charity. This could affect the validity of any transaction where there is the possibility that it might be outside the rules of the society. The new section 5A addresses this issue by requiring a society which is a charity, but whose name does not include either “charity” or “charitable”, to state that it is a charity, in correspondence and other specified documents. (Section 5A broadly corresponds to sections 68 and 96(1) of the Charities Act 1993 in relation to England and Wales, to section 112(1)(b) and (6) to (8) of the Companies Act 1989 in relation to Scotland and to section 349(3) and (4) of the Companies Act 1985).

Section 3: Capacity of society and power of committee to bind it

16. **Section 3** amends the 1965 Act in line with company law in order to make it easier for societies to enter into business transactions. It does this by inserting into the 1965 Act six new sections, numbered 7A to 7F.
17. Section 7A provides that the validity of an act performed by a society cannot be called into question on the basis that it is outside that society’s rules. The section allows for members to restrain their society from performing an act which is beyond the rules, and preserves the liability of committee members if they do not observe any limitations on their powers under the rules unless the members agree to relief from such liability in a special resolution. (Section 7A(1) to (5) corresponds to section 35(1) to (4) of the Companies Act 1985; section 7A(6) corresponds to section 378(1) and (2) of that Act; and section 7A(7) is analogous to section 380(1) and (4)(a) of that Act).
18. Section 7B provides that, in favour of a person dealing with a society in good faith, the power of the society’s committee to bind it is to be deemed not to be restricted by the society’s rules. (Section 7B corresponds to section 35A of the Companies Act 1985).
19. Section 7C removes the burden from a party to a transaction with a society of having to enquire whether that transaction is permitted by the society’s rules, or of having to enquire about any limitation on the powers of the committee to bind the society. (Section 7C corresponds to section 35B of the Companies Act 1985).
20. Section 7D disapplies sections 7A and 7B from societies which are charities, except in certain limited circumstances. Therefore, acts which are outside a charitable society’s rules will continue to be void except in the specific circumstances outlined in this

section. The aim is to ensure that the assets of societies which are charities are not used for a purpose for which they were not intended. (Section 7D corresponds to sections 65 and 96(1) of the Charities Act 1993 in relation to England and Wales, and to sections 112(1)(b) and (3) to (5) of the Companies Act 1989 in relation to Scotland).

21. Sections 7E and 7F make provision for the circumstance in which a society enters a transaction with a member of its own committee, or a person connected with a committee member or a company with whom a committee member is associated, *and* the committee, in connection with the transaction, acts beyond its powers. Such a transaction is voidable by the society. (Sections 7E and 7F correspond to sections 322A and 735(1)(a) of the Companies Act 1985).

Section 4: Purported contracts, deeds and obligations

22. **Section 4** amends the 1965 Act to provide for contracts to be enforceable against and by a person who has acted for or on behalf of a society before it is registered. Subsection (1) deals with societies registered under the 1965 Act, by inserting a new section 29A corresponding to section 36C of the Companies Act 1985, inserted by section 130(4) of the Companies Act 1989. Subsection (2) applies the new section 29A to societies registered in Northern Ireland when operating in Great Britain.

Section 5: Execution of deeds and other documents

23. Subsection (1) of section 5 inserts six new sections into the 1965 Act, numbered 29B to 29G, dealing with aspects of how societies execute deeds and other documents and enter into contracts, in line with similar provisions in company law.
24. Section 29B removes the obligation for societies to have a common seal while ensuring that appropriate provision is made for the custody and use of any common seal which a society does decide to have. It corresponds to sections 36A(3), 36B(1) and 350 of the Companies Act 1985.
25. Section 29C corresponds to the remainder of section 36A of the Companies Act 1985, and sets out provisions on how documents can be executed by or on behalf of societies under the law of England and Wales, whether or not they have a common seal. It gives societies the choice to execute a document either through attaching their common seal or by getting it signed by the specified officers of the society, and subsections (4) and (5) create legal presumptions about when a document can be taken to have been validly executed and, in the case of a deed, delivered.
26. Section 29D provides for how documents can be executed by or on behalf of societies under the law of Scotland, whether or not they have a common seal. It corresponds to section 36B(2) and (3) of the Companies Act 1985, as substituted as regards Scotland by section 14 of the Requirements of Writing (Scotland) Act 1995.
27. Sections 29E, 29F and 29G aim to facilitate the ability of societies to enter into transactions overseas. They correspond to section 39 of the Companies Act 1985, as amended under section 130 of the Companies Act 1989, section 74 of the Law Reform (Miscellaneous Provisions) (Scotland) Act 1990 and section 14 of the Requirements of Writing (Scotland) Act 1995. The new sections enable societies to have official seals for use abroad, and make provision for the effect of the use of such seals and for authorising such use.
28. Subsections (2) to (7) of section 5 and the Schedule introduced by subsection (9) make various amendments to and repeals in the 1965 Act consequential upon the substantive provisions inserted by subsection (1). Subsection (8) makes a consequential amendment to the Land Registration Act 2002.

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Sections 6, 8 and 9: Interpretation, Channel Islands, Short Title and extent

29. These formal sections include provisions allowing the Act to be extended to the Channel Islands with appropriate modifications, and defining its territorial extent.

COMMENCEMENT

30. **Section 7** of the Act provides for it to be commenced by one or more Treasury orders, with any appropriate transitional provisions.

HANSARD REFERENCES

Stage	Date	Hansard reference
House of Commons		
Introduction	11 December 2002	Vol 396 Col 284
Second Reading	31 January 2003	Vol 398 Cols 1113-1146
Committee	18 March 2003	Hansard Standing Committee C
Report and Third Reading	4 April 2003	Vol 402 Cols 1167-1209
House of Lords		
Introduction	7 April 2003	Vol 647 Col 75
Delegated Powers and Regulatory Reform Committee report on Bill	7 May 2003	HL 102 (2002/03 Session, Eighteenth report)
Second reading	9 May 2003	Vol 647 Cols 1369-1385
Delegated Powers and Regulatory Reform Committee report on proposed amendments	11 June 2003	HL 122 (2002/03 Session, Twenty-first report)
Committee	13 June 2003	Vol 649 Cols 500-503
Report	27 June 2003	Vol 650 Col 535
Third reading	3 July 2003	Vol 650 Col 1002
Royal Assent – 10 July 2003		House of Lords Hansard Vol 651 Col 469 House of Commons Hansard Vol 408 Col 1429