

Community and social enterprise: The basics

1. Common characteristics of social enterprise organisations

- they are involved in trading
- they are potentially “viable” or “sustainable”
- they are owned by the community (or on behalf of it)
- they are answerable to the community
- they are run on the principle of one-person-one-vote (or occasionally a shareholding)
- they tend to adopt business management practices
- their prime purpose is community benefit (profit is secondary)

2. What do all the different terms mean?

Often not much. None has any legal standing, and they are used interchangeably. Politicians, bureaucrats and academics periodically adjust the language to suggest something new is happening – it usually isn't.

- **community enterprises**
 - often meaninglessly referring to any community-based organisation which does anything in an enterprising way, or,
 - more usefully, community-based organisations which generate income to enable them to meet their social objectives
- **community enterprise organisations** – could be any organisation which is helping the development of community enterprise or running enterprise projects
- **community businesses** – community enterprises which tend to run as stand-alone trading ventures, usually with more single-minded business objectives
- **social enterprises** – this term implies any trading ventures run for social benefit (not only those owned and run by the community organisations) and includes worker co-operatives, ILM organisations (see below)
- **social economy organisations** – same as social enterprises
- **community co-operatives** – same as community enterprises
- **development trusts – tend to display these common characteristics:**
 - multi-functional (economic, social and environmental objectives and activities)
 - work in partnership with the public and private sectors
 - involved trading activities
 - may also have a role in supporting and developing enterprise
- **intermediate labour market initiatives (ILMs)** – normally top-down organisations (ie without community ownership) which aim to provide jobs and training, particularly using government-funded programmes for unemployed people
- **worker co-operatives** – commercial organisations owned by the workforce, which may or may not have employment creation or social objectives.

3. Why should community organisations get involved in trading?

- to provide services not provided by the public sector
- to replace services withdrawn by public or private sector
- to deliver services devolved from public sector – eg community care
- to create jobs for local people
- to provide training at a *local* level which is designed to meet local needs
- to provide managed workspace – so other people can create jobs in the area
- to sustain or regenerate community buildings
- to generate income to support existing community projects
- to create “empowerment” for individuals and communities, by:
 - providing informal training and personal development for participants
 - providing varied volunteering opportunities for work experience
 - introducing people to commerce without personal risk
 - creating pride in community ownership
- to reduce dependency on grant funders – creating a sense of independence unique elsewhere in the voluntary sector
- to generate profits to be used for charity or community development work (rarely achieved!).

4. What trading opportunities are there?

Examples: Some of the most popular trading opportunities include:

- community cafes and catering – the most common of all
- childcare initiatives
- horticulture
- gardening and landscaping services
- recycling and environmental projects
- community transport
- sports facilities
- cinema, theatre, tourism and entertainment
- printing, design and publishing
- workspace management
- shops, post offices, and occasionally petrol stations and pubs, in rural areas
- providing training

Business: Community enterprise only works if organisations aim to make a profit. Just breaking even eventually mean failure.

Community and social enterprise 2: Getting constituted

1. An overview

Forthcoming changes: These notes are prepared for current circumstances. During 2003 the government announced that it was planning to introduce two new company structures which will increase the range of options for community organisations involved in trading. While they are not considered here, it is useful to be aware that change is on its way:

- The **Community Interest Company (CIC)** is proposed by the Department of Trade and Industry to help “social enterprise” organisations which can demonstrate they operate for public benefit (including community enterprise initiatives) to register new companies easily and cheaply and to *provide protection for their assets and profits* when they attract outside investments. This may not be of immediate interest to new projects getting started on a small scale, but the CIC may be useful later in helping them to grow.
- The **Charitable Incorporated Organisation (CIO)** has been proposed by the Home Office as part of a major review of charity law. This will be a special type of company with charitable status. In time these will supersede companies limited by guarantee which are separately registered as charities by the Charity Commission.

Preparation:

- there is no need to completely understand all the jargon connected with companies and constitutions from the start
- take a look at the pitfalls to be avoided (see “Getting It Wrong” below) and bear them in mind at each stage
- new organisations should immediately adopt a *simple* “community association” type of constitution to provide a framework for your group to work in while you make decisions about the future structure
- decide as clearly as you can *what your organisation will do* – you can’t choose a constitution in a vacuum.

Planning:

- if you are going to seek outside advice now is the time
- study the various options for different types of organisation - the alternative “legal structures” - and decide which seems to suit you best
- if your project involves an existing charity in any new trading activity, check whether that would be acceptable under charity law (from the Charity Commission in England and Wales) or the tax implications (from the Inland Revenue in Scotland), and establish what additional organisational structure/s might be needed for you to avoid endangering your charitable status
- if your organisation is *not already a charity*, now is the time to consider whether there is any value in setting one up.

Getting constituted:

- locate/choose a basic model constitution or constitutions for the structure you have decided on (the Charity Commission and some national bodies can provide standard models which can speed the registration)
- work through the constitution clause by clause to understand it fully
- adapt the model to meet your own needs by filling in the details on your objectives, operating area, classes of member, maximum and minimum numbers of members of the management committee or board, the size of quorums etc

- make sure your colleagues in the group are fully consulted on the proposed constitution and that they also understand its implications
- contact the charity Commission (England and Wales) if you intend to set up a new charity or reconstitute an existing one as a limited company - and follow their advice meticulously
- complete the registration forms for Companies House for any limited companies you are forming.

GETTING IT WRONG

Almost all the anguish associated with structures and constitutions is avoidable if you take a steady thoughtful approach to the process, and don't put it off until it is too late. Here are the main pitfalls to avoid.

The main dangers:

- **Panic and bad advice:** The two gravest threats to your organisation setting up the "right" structure and constitution at the right time are *bad advice* and *panic*. Each one of them makes you vulnerable to the other, and groups have great difficulty in avoiding either or both of these traps. See below.
- **Crystal balls:** Don't be rigid in the arrangements you adopt. You may kid yourself that you know how your organisation will develop and what type of constitutional structure it will need a year or two ahead. The odds are that you will be looking at the wrong version of the future.
- **Poor management:** Your constitutional structure will be no use to you (and could even harm your work and lead to legal problems) if you cannot administer it properly. So your first priority should be to ensure that your group is well organised and has the capacity to run its affairs effectively. If it can't, you should certainly not be thinking about forming a limited company or a charity.

Panic

- **How to panic:** This involves doing nothing (because everything seems so complicated or because you are busy on other things) until it's too late to do anything properly. Then, under pressure, you make a pig's ear of it.
- **When to panic?** This is the point when you *need* a constitutional structure and suddenly ...
 - a funder tells you that you could have been eligible for grant aid if only you had an appropriate constitutional structure for your project, or
 - you realise you may not have the best arrangement for dealing with imminent Corporation Tax or VAT liability, or
 - your members start looking for limited liability protection because your organisation has run into financial problems.

The wrong advice

Choosing the wrong "experts": Experts with a little knowledge of community enterprise are always the most dangerous. So be very cautious about listening to people who sound as if they might have useful knowledge in a *different* area of activity

- solicitors and accountants on the whole will probably understand companies limited by shares, and, perhaps, charitable companies, but very few have experience of community enterprise
- community development workers may be red hot with constitutions for community groups and have probably genned up on charity law, but that's not necessarily community enterprise
- local government officers may have worked on constitutions for community associations, and they may try to foist one of them on you: that model will probably be a disaster.

Paying for duff advice: Even worse than receiving poor advice is being charged for it. If you must part with money, make sure you know what you are getting. Check who else they have

worked for, and give one of their former clients a ring to find out whether their expertise was any use.

The wrong constitution:

Complexity. Subsidiary companies and complicated company and board membership arrangements can be desperately difficult for directors to understand – and you’ll never be able to explain them to the community. They are more likely to trip you up and cause disagreements later over interpretation. As a general rule, go for simple arrangements to start with, and embellish them later if you need to.

Rigidity: You may be tempted to tie your organisation down rigidly with a constitution which limits what it can do and specifies precisely the way it is allowed to do it. The problem with organisations which don’t change, of course, is they don’t go anywhere.

Subservience to democracy. If you want a genuinely co-operative structure you should explore the options extremely carefully because they are notoriously difficult to manage well. Find an organisation which has already taken this route, and talk to *everyone* – manager, workers and committee - to find out how it really works.

Teamwork by ordeal: If you insist that committee members write the constitution collectively you will get a bad set of rules and miserable trustees. You just need to ensure that they go through the final draft thoroughly.

The lapse of attention: Follow existing examples closely. If you adapt another constitution in radical ways (or if you are reckless enough to write your own) to meet what you think are your own needs, there is a real chance that you will overlook something fundamental and end up with a nightmare. It is not unknown, for example, for the clauses governing the quorum at meetings and the recruitment of new members to be accidentally worded in such a way that a group can never recruit enough people to hold a legal meeting.

The wrong side of the law

Most people are concerned about the legal issues of their trading and company status because it is an area which they have so little knowledge of. In fact, the risks are relatively small, and groups which run their operations responsibly and with reasonable care have little to worry about. The main points to be aware of are:

- **personal liability:** forming a company limited by guarantee reduces but does not eliminate the risks of personal liability for debts (see “Getting it right” below)
- **recklessness:** if you don’t monitor and control your registered company properly, you could lose that personal liability protection
- **illegal trading by charities:** there is a small risk that you could lose your charitable status; but that is less immediately important than the unexpected tax bill you could get
- **Companies House penalties:** financial penalties for missing reporting deadlines set by Companies House can be painful
- **infringing the Companies Acts and operating unconstitutionally:** members and directors have the right to expect that you will run your company within the law, and within your memorandum and articles and infringements could land you in court; reprisals taken by former friends and colleagues can be surprisingly vicious if you fall out

GETTING IT RIGHT

First steps

Get a basic constitution: If your organisation is new and planning for your enterprise project will take a few months, get a basic constitution (for an unincorporated association) as a temporary measure. This gives you the assurance that you are operating legitimately through the planning phase.

Find a model: When you are ready to design the permanent constitution from a similar organisation to your own, and ask someone familiar with it to explain what it means.

A few commonly basic questions: Before you get stuck in, here are some instant answers to the most common questions about constitutions and company registration. They’re obviously not comprehensive, but they may help to give you a better sense of where you are going.

Should we form a limited company?	It is wise to do so in all but the smallest enterprises. If you have permanent staff and a turnover of more than a few thousand you would be foolish not to.
When should we form it?	There is no ideal time. Don't register before you're sure you are going to trade, but definitely do so before you acquire significant assets.
How should we choose a suitable constitution and company structure?	Get advice from someone who <i>really</i> knows, and think about how their experience affects you (the people with the most experience are often other community businesses).
Can we use a simple model constitution designed for community businesses?	Yes, but There are plenty of good models, but you will have to use common sense to choose the optional variations which best suit your organisation.
We are a registered charity. What do we do if we want to trade?	If trading income turns out to be more than a quarter of your total income (or £50,000 for organisations with a turnover above £200,000) you should form a <i>subsidiary</i> or <i>parallel trading company</i> . The charity should also be a limited company if it is not one already.
Our business has charitable aims. Should we form a charity?	Not unless there are obvious financial advantages to doing so. The advantages of charitable status in a community enterprise context are often exaggerated. But check the tax situation with an accountant.
What can our trading company do?	It can do pretty well anything you like provided it's within the law – the business is in your own hands
Are there any real advantages to registering as a limited company?	It may be a hassle and expense. But without registration you'll be in a lot more trouble if things go wrong. Even if the board members are prepared to take a risk with personal liability, is it really fair to risk assets which you hold in trust for the community?

Stay calm! Community groups are often highly nervous about the legal responsibilities involved in company registration. That's fair enough (though frequently inconsistent with the reckless abandon with which many groups approach the more important consequences of employing people). To help you keep things in perspective, here are a few basic tips designed to allay the most common fears:

- bear in mind that members of your management committee have legal responsibilities, and personal liability for any losses, as a result of their *current* involvement (forming a company does create additional responsibilities, but also reduces the risks)
- difficult language in constitutions can easily be explained by an advisor
- in practice there are relatively few possible structures to choose from
- there is nothing remotely inconsistent in a charity forming a company – huge numbers of charities of all sizes are companies limited by guarantee
- poorly managed groups shouldn't attempt to run either charities or businesses, so stop now if this applies to you
- forming a new company is straightforward, but it does demand attention to detail to avoid irritating delays – the best advice comes in a pack from Companies House (tel 0870 3333 636; web site www.companieshouse.gov.uk)
- advice on constitutions is available from agencies which specialise in the particular type of organisation you are interested in (community businesses, co-operatives, community associations, community care projects etc)
- the best information often comes from groups which have already done what you are planning, so it's good to get networking
- there is no *right* solution for your organisation and the law does not recognise "community businesses" – in the end you have to depend on good judgement and make changes later if you get it wrong first time.

The options

These notes cannot hope to cover the wide range of possible community enterprise structures in any detail. The following account indicates the options and provides signposts to those which you might need to pursue in more detail.

Types of organisation: There is actually very little choice, as the table below shows:

<i>structure</i>	<i>uses</i>	<i>disadvantages</i>
unincorporated association or partnership	this is automatically the status of your group unless you choose an alternative structure, but you <i>must</i> formalise it with a proper constitution if you do not choose another option – it's easy.	members are personally liable for organisation's debts
private company limited by guarantee	- gives members some protection against personal liability - great flexibility – this is the legal structure for most of stand-alone community-owned trading companies (and charities and conventional community groups which register as limited companies)	- cost of annual accounts, - the “limited liability” protection does not cover incompetent and neglectful directors
private company limited by shares	suitable in certain circumstances for: - subsidiary trading companies, - trading companies where members of the community are able to take a real financial stake in the enterprise	- cost of annual accounts, - very difficult to adapt to a democratic “one-person-one-vote” arrangement for community ownership
friendly societies	similar to the company limited by guarantee, designed for co-operative organisations	less flexible than companies limited by guarantee and not usually recommended.