EXPLANATORY MEMORANDUM TO

THE CO-OPERATIVE AND COMMUNITY BENEFIT SOCIETIES AND CREDIT UNIONS (INVESTIGATIONS) REGULATIONS 2014

2014 No. [XXXX]

1. This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of Her Majesty.

2. Purpose of the instrument

2.1 These Regulations repeal section 48 of the Industrial and Provident Societies Act 1965 ("1965 Act") which gave the Financial Conduct Authority ("FCA") power to require Industrial and Provident Societies and Credit Unions ("societies") to produce documents and provide information. By applying provisions of Part 14 of the Companies Act 1985 with modifications, the Regulations replace section 48 with more extensive powers for the FCA to obtain information from societies, including powers of entry to premises, and new powers for FCA to arrange investigations of societies.

3. Matters of special interest to the Joint Committee on Statutory Instruments

3.1 None.

4. Legislative Context

4.1 Section 4(1) and (2)(a) of the Co-operative and Community Benefit Societies and Credit Unions Act 2010 gives the Treasury power by regulations to apply Parts 14 and 15 of the Companies Act 1985 to societies, with modifications. These Regulations apply certain provisions of Part 14 with the modifications considered necessary for the legislation to apply to societies. Regulation 3 provides for the FCA to exercise its powers under the Regulations only to the extent necessary to maintain confidence in registered societies. The Regulations do not provide the FCA with the Part 14 power to impose restrictions on shares and debentures which is inappropriate for societies, and consequently Part 15 which contains further provision about restrictions on shares is not applied. Certain other provisions of Part 14 are not applied, including section 431(investigation of a company on its own application or that of its members) which is not applied because section 49 of the 1965 Act already permits a percentage of members of a society to appoint an inspector.

4.2 The new provisions supersede section 48 of the 1965 Act, which is repealed. The Regulations also contain amendments to other legislation consequential on the repeal of section 48.

4.3 These Regulations form part of a package of reforms of legislation applying to societies coming into force on 6th April 2014.

5. Territorial Extent and Application

5.1 This instrument applies to Great Britain.

6. European Convention on Human Rights

The Financial Secretary to the Treasury has made the following statement regarding Human Rights:

In my view the provisions of the Co-operative and Community Benefit Societies and Credit Unions (Investigations) Regulations 2014 are compatible with the Convention rights.

7. Policy background

- What is being done and why

7.1 This instrument is one measure for implementing the Government's commitment to promote mutual bodies and foster diversity in the UK economy. The objectives are to preserve and strengthen the unique features of societies registered under the 1965 Act, and to promote a diverse, healthy and successful mutuals sector which is able to offer a broad range of services to growing numbers of members.

7.2 The 1965 Act provides for the registration of societies. There are two types of registered societies, co-operative societies and community benefit societies. A co-operative society is a business owned and run by and for the benefit of its members. A community benefit society must satisfy the same co-operative principles as a co-operative society and must also be operated for the benefit of the community in which it works. All registered societies embody the democratic principles; in particular, members have equal voting rights regardless of the level of their financial commitment. This enables members, who may be employees, customers or residents, to be involved in the running of the business. In addition, credit unions are registered under the 1965 Act by virtue of the Credit Unions Act 1979.

7.3 Over 7,000 societies were registered in Great Britain in 2013. The number has grown as the sector has continued to provide a popular and successful structure for mutually run business. Societies cover a vast range of activities and industries including public service providers, football clubs, wind farms, web designers and agricultural suppliers. Some have hundreds of members and are large employers; others have just a handful of members. Societies are found in all parts of the UK (legislation governing registered societies is devolved in Northern Ireland).

7.4 This proposal would give the FCA additional powers to investigate co-operatives, community benefit societies and credit unions where circumstances suggest their behaviour may be improper or unlawful. The additional powers proposed in this section are in line with the current powers in the Companies Act 1985, appropriately modified for societies. This proposal aims to create a level playing field with the requirements that companies face and increase confidence in the co-operative and community benefit society form. These powers include a requirement for the FCA to appoint an inspector if a court instructs them to do so and give the FCA power to appoint an inspector to investigate the affairs of a society. As with companies, the power would be available when it appears to the FCA that, for example, there may have been an intention to defraud creditors or the society has been conducted in a way which unfairly prejudices a group of members or for unlawful purposes. Other powers concern the expenses of the investigation and would be payable in the first instance by the FCA but recoverable from the society investigated. The measure also gives the FCA or an authorised investigator power to give directions to a society to produce documents and provide information and give the FCA or an authorised person power to apply to a magistrate for a warrant of entry to premises of a society on the grounds set out in section 448(2) of the Companies Act 1985.

- Consolidation

7.5 These Regulations apply provisions of Part 14 of the Companies Act 1985 to societies, so the possibility of consolidation does not arise.

8. Consultation outcome

8.1 The Government consulted publically on a package of measures (including this Order) proposed for the reform of societies' legislation; see *Industrial and Provident Societies: growth through co-operation* issued on 26 July 2013. The consultation period was eight weeks (until 20 September 2013). This was proportionate to the scale and subject matter of the consultation and took into account the capacity of interested parties to respond. The Treasury had regard to the specialised nature of the issues raised; the number of likely respondents; the prior involvement of some interested parties; and its on-going dialogue with industry representatives about the proposals and the timing of the consultation.

8.2 There were 42 responses to the consultation. These came from a variety of sources, including co-operative and credit union representatives, private individuals, trade bodies, legal advisors and consumer groups.

8.3 24 of the 42 consultation respondents commented on these proposals. All but two agreed with the proposals. The two respondents not supportive of the measure expressed concerns that additional powers for the FCA would create overlap with their principal regulators in relation to their activities as registered providers of social housing and registered social landlords. Three respondents asked that the grounds for the FCA to appoint an inspector be extended to any failure to operate the society in accordance with the registration requirements.

8.4 Despite the concerns raised about a possible regulatory power overlap for certain types of society the Government is not exempting any societies from this measure. The FCA's functions are analogous to those of Companies House and the Secretary of State under the Companies Act 1985. Grounds for the FCA to appoint an inspector for any failure to operate the society in accordance with the registration requirements have not been incorporated into the Order. The Government considers that the FCA's powers under section 447 of the Companies Act 1985 as applied, and related provisions, are most appropriate to deal with a society's suspected failure to comply with registration requirements.

8.5 A full Government consultation response has been published at: www.gov.uk/government/consultations/industrial-and-provident-societies-growth-through-co-operation

9. Guidance

9.1 The Treasury is not intending to issue any guidance in connection with these Regulations.

10. Impact

10.1 The impact on business, charities or voluntary bodies run as societies will be the costs of complying with an investigation, should one be deemed necessary by the FCA. Direct compliance costs for a society would be in providing copies of documentation and management time and we estimate that a maximum figure of £5,000 would be realistic. Based on past experience the FCA expects an average of 0-1 investigations per year and that each investigation may cost up to £100,000 which it will then charge back to the society. Therefore we estimate a maximum cost to business of £105,000 per year on average.

10.2 The impact on the public sector is negligible however the FCA may incur costs when they choose to use the additional powers. Costs are expected to be much less than when investigating large companies due to the smaller scale and simpler structure of societies generally. Investigation costs incurred will be charged back to the society.

10.3 The Regulatory Policy Committee has confirmed that this measure qualifies for its fast-track process; therefore no impact assessment has been prepared.

11. Regulating small business

11.1 Many societies are run as small businesses. The additional powers being given to the FCA were welcomed by consultation respondents and seen as an important further step towards creating a level playing field with the requirements that companies face and will increase confidence in the co-operative and community benefit society form. The measure will improve the legislation for the sector and have a low cost impact.

12. Monitoring & review

12.1 While no specific review is planned for this instrument, it will be reviewed with regard to future policy regarding Co-operative and Community Benefit Societies.

13. Contact

13.1 Candice Mullineux at the Treasury: 0207 270 1037 or email: Candice.Mullineux@hmtreasury.gsi.gov.uk can answer any queries regarding the instrument.