EXPLANATORY MEMORANDUM TO

THE COMMUNITY INTEREST COMPANY (AMENDMENT) REGULATIONS 2014

2014 No. [XXXX]

1. This explanatory memorandum has been prepared by the Department for Business, Skills and Innovation and is laid before Parliament by Command of Her Majesty.

This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

This instrument amends the Community Interest Company Regulations 2005 (S.I. 2005/(the "2005 Regulations") to remove the share dividend cap. The "share dividend cap" was a limit introduced in the 2005 Regulations that prevented a community interest company from paying more than a certain percentage of the paid up value of the share as a dividend in any one year. This instrument also makes amendments to the 2005 Regulations consequential on this change.

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

None

4. Legislative Context

This statutory instrument amends the 2005 Regulations to achieve the purpose stated above. This is the third amending instrument made in relation to the 2005 Regulations since they came into force, the first being the Community Interest Company (Amendment) Regulations 2009 (S.I. 2009/1942) and the second the Community Interest Company (Amendment) Regulations 2012 (S.I. 2012/2335). Other instruments have made minor consequential amendments.

5. Territorial Extent and Application

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Minister for Employment Relations, Consumer and Postal Affairs has made the following statement regarding Human Rights:

In my view the provisions of the Community Interest Company (Amendment) Regulations 2014 are compatible with the Convention rights.

7. Policy background

7.1 The CIC provides a bespoke legal form for social enterprises that want to use the company form but with the assurance that the company's assets will be used for the benefit of the community. The model was introduced to give greater choice and flexibility to businesses with social objectives, which reinvest their surpluses in the business or the

community. The Companies (Audit, Investigations and Community Enterprise) Act 2004 (the "2004 Act") created CICs and contains the vires for this instrument, and established the Office of the Regulator of Community Interest Companies to oversee CICs and to ensure public confidence in the model ("the Regulator"). Over 9,300 CICs have been registered by the Regulator since 2005.

7.2 A key feature of the CIC is an "asset lock" that prevents CICs from using their assets other than in the community interest. One element of the asset lock is the share dividend cap. This prevents a CIC from paying a dividend per share of more than 20% of the paid up value of the share. This limit is considered to be a barrier to investment in CICs since it reduces the liquidity of shares and restricts unnecessarily the dividends payable. This instrument removes the share dividend cap.

7.3 Other elements of the asset lock will remain in order to ensure that CICs continue to use their assets appropriately. These include a cap on the performance related interest payable by a CIC and an aggregate dividend cap, set at 35% of profits per financial year. The Regulator sets these limits under powers granted by the 2004 Act.

7.4 The regulations are deregulatory and do not impose any additional burden on CICs. Legislation was necessary in order to remove the element of the asset lock that is being removed.

8. Consultation outcome

8.1 In conjunction with HM Treasury, the Regulator consulted publicly on the measures contained in this instrument from 6 June 2013 to 6 September 2013. The consultation was drawn to the attention of all CICs.

8.2 The responses were broadly supportive of changing the asset lock: 58% of respondents felt that having two caps on dividends is cumbersome, and 60% of respondents said that one or both caps should be removed, the majority favouring retaining the aggregate cap and removing the share dividend cap. 24% of respondents did not agree that there should be any change to the dividend caps and felt that a change would threaten the integrity of the asset lock. The remaining respondents did not have a view on this point.

8.3 The response to the consultation was published on 10 December 2013. The response set out the intention to remove the share dividend cap, but in order to address concerns over the asset lock, the response set out the intention to retain all other features of the asset lock. The only other change being made by the Regulator is to raise the performance related interest rate payable from 10% to 20%.

9. Guidance

9.1 Guidance as to the operation of dividend payments is available on the website of the CIC Regulator: http://www.bis.gov.uk/cicregulator and will be updated to reflect the changes that will be brought into force by this instrument.

10. Impact

10.1 The impact on business is not anticipated to be significant. Only around one quarter of CICs operate as companies limited by shares and those that do have found the existing

process complex and confusing. Investment has been limited owing to limited returns on the investment.

10.2 The impact on the public sector is as follows: the Office of the Regulator of Community Interest Companies will review its guidance in light of these amendment regulations.

10.3 A fast track Impact Assessment is being prepared for this instrument and it is anticipated that there will not be significant costs or burdens as a result of the measures.

11. Regulating small business

11.1 The legislation applies to small business.

11.2 To minimise the impact of the requirement on firms employing up to 20 people, a light touch regulatory framework is being maintained. The Regulations will not impose net costs on such businesses.

11.3 The majority of CICs are small companies.

12. Monitoring & review

The Office of the Regulator will monitor the impact of the amendments and will advise the Department if they are not working as intended. The Office is aiming to review these regulations in 2019.

13. Contact

Sara Burgess at the Office of the Regulator of Community Interest Companies Tel: 029 20346228 or email: sara.burgess@bis.gsi.gov.uk can answer any queries regarding the instrument.