

# CHAPTER 4

## Forming a CLT – Governance and legal structures

4.1 Why do CLTs need a legal form?

4.2 Legal forms and regulatory bodies

4.3 Factors to consider when choosing a legal form

4.4 Good governance

This is an abridged version of the CLT Legal Toolkit, available on the National CLT Network's website [www.communitylandtrusts.org.uk](http://www.communitylandtrusts.org.uk)

**‘Once you’ve been  
bitten by the bug of  
community-led activity  
and you show that  
things can be done, the  
sky’s the limit’**

David Brettell, Hands on Help for Communities

## 4.1 Why do CLTs need a legal form?

Once a Community Land Trust (CLT) has a clear set of objectives and has formed a steering group, it will need to be formalised into a legal entity. This is because CLTs are a legally defined concept but they are not a legal format in and of themselves. Any emerging CLT should choose a legal format that would enable it to meet the legal definition of a CLT as legislated in the Housing and Regeneration Act 2008, Part 2, Chapter 1, Clause 79:

A CLT is a corporate body which:

1 Is established for the express purpose of furthering the social, economic and environmental interests of a local community by acquiring and managing land and other assets in order –

1.1 To provide benefit to the local community

1.2 To ensure that the assets are not sold or developed except in a manner which the trust's members think benefits the local community

2 Is established under arrangements which are expressly designed to ensure that:

2.1 Any profits from its activities will be used to benefit the local community (otherwise than by being paid directly to members)

2.3 Individuals who live or work in the specified area have the opportunities to become members of the trust (whether or not others can also become members)

2.4 The members of a trust control it.

The chosen legal form will therefore need to have the following key features:

- It must be designed to benefit a designated community/the public/ section of the public, rather than members or private shareholders;

- It needs to protect the assets through a provision in the governing document, an **Asset Lock**. This will mean that if the CLT is wound up any assets will have to go to a similar organisation once creditors have been paid. However, it is important to note that this would be overridden by the mortgagee possession clause in cases of default. It is also subject to leasehold enfranchisement where this applies;
- It must dictate that any profit made by the CLT will only be used to further the objectives of the CLT – so profits/surpluses will need to be reinvested in the CLT rather than shared amongst members;
- It must provide opportunities for local people to become members and for the members to control the CLT.

The legal formats that are suitable for CLTs are therefore:

- **Community Benefit Society** (also known as an Industrial and Provident Society for the Benefit of the Community – this can be charitable or non-charitable. If it is non-charitable steps should be taken to ensure there is an asset lock. This can either be by way of including a custodian member of the constitution or the statutory asset lock);
- **A Community Interest Company Limited by Guarantee** (known as a CIC);
- **A Company Limited by Guarantee** (this can be charitable or non-charitable. If it is non-charitable steps should be taken to ensure there is an asset lock. This can be either by way of a custodian member of the constitution or by entrenching voting rights so that the asset lock cannot be voted out – essentially, this would require a unanimous decision to vote out the asset lock). There is more information on these legal forms in the next section.

## 4.2 Legal forms and regulatory bodies

Below is a summary of the suitable legal forms. This has been written as a guide and does not constitute legal advice. For more information, please visit the CLT Legal Toolkit on the National CLT Network website. The Toolkit includes

standard template constitutions for each of these legal forms. It is important to make a considered decision when choosing a legal form, as the cost of altering to a different legal form can be considerable, even if it is possible.

### Company Limited by Guarantee

A Company Limited by Guarantee is a simple structure, where members act as guarantors of the company rather than shareholders, up to an agreed level of support. This is normally a nominal amount, such as £1. A CLG is inexpensive to set up and can be easily converted into another legal entity. Some CLTs have chosen to set up a CLG to access funding and then converted to a more appropriate legal form at a later stage.

Many of the same features apply to a Company Limited by Guarantee and a CIC. However, because there is no requirement on a CLG to include an asset lock in its Articles, it should involve either a ‘custodian member’ of the constitution or entrenched voting rights to ensure that the asset lock cannot be voted out. The custodian member may be the local authority or a local church and has the power to veto any disposal of assets which might contravene the asset lock. In the case of entrenchment, the CLG would require the agreement of 100% of the membership to change or vote out the asset lock.

A company limited by guarantee can also take on the form of a registered charity with the Charity Commission. A registered charity by its very definition is a form of asset locked entity.

### Community Interest Company Limited by Guarantee (known as a CIC)

A CIC is a relatively new form of company, and is a mid-point between the flexibility of a Company Limited by Guarantee and the firm public benefit requirement of a charity. Its basic structure can be a Company Limited by Guarantee, a company limited by shares or a Public Liability Company; the ‘upgrade’ to a CIC structure guarantees that the company’s assets will be used for the benefit of the community. The most appropriate form for a CLT will be a CIC Company Limited by Guarantee, as this is non-profit distributing and the most democratic form. The CIC Regulator must be satisfied that the CLT will use its assets for the benefit of the community, through a community interest test and annual reports; the CIC must also include an asset lock in its Articles. This is cast in stone.

CICs are appropriate legal forms for attracting grants or loans but they cannot be charitable and cannot gain from any tax advantages. They are inexpensive to set up and are regulated by Companies House, which liaises with the CIC Regulator.

## Community Benefit Society (formerly known as an Industrial and Provident Society for the Benefit of the Community)

A Community Benefit Society (CBS) is set up for the benefit of the community. It can have a statutory form of asset lock and can be charitable. A CBS offers the unique ability to issue share capital, outside of the Financial Services and Markets Act regime.

Membership should be open to anyone, although some Societies plan restrictions on membership (e.g. those living and working in a community). All members have one equal vote, regardless of the number and type of shares they hold, and they vote for and are able to stand for the Committee of Management.

A CBSs' governing document is its Rules, which must be registered with the Financial Services Authority (FSA). One of the most cost effective ways to register a Community Benefit Society is by using Model Rules, which are available from the National CLT Network.

The CLT Legal Toolkit can be found at [www.communitylandtrusts.org.uk/resources/toolkits/Legal-Toolkit](http://www.communitylandtrusts.org.uk/resources/toolkits/Legal-Toolkit)



Residents moving in to Buckland Newton CLT, Dorset

## Characteristics of the different legal forms

	<b>Company limited by guarantee/Charity</b>	<b>Community Interest Company</b>	<b>Community Benefit Society</b>
Open membership	Yes	Yes	Yes
Member Democracy	Yes, one member one vote	Yes, one member one vote	Yes, one member one vote
Trading flexibility	Flexible (Limited where a charity)	Flexible	Flexible
Beneficiary representation on Board	Unrestricted (except where a charity)	Unrestricted	Unrestricted (except where a charity)
Payment to Board members	Possible	Possible	Possible
Raise share capital at affordable cost	No	No	Yes, using withdrawable shares
Legally enforceable asset lock	Yes	Yes	Yes
Reporting and regulation	Companies House and Charity Commission (if a charity) If also a Registered Provider the HCA's Statutory Sub-Committee will take on the role of lead regulator	Companies House and CIC Regulator. If also a Registered Provider the HCA's Statutory Sub-Committee will take on the role of lead regulator	Financial Services Authority. If also a Registered Provider the HCA's Statutory Sub-Committee will take on the role of lead regulator
Tax advantages	Rate relief Stamp duty exemption if a charity and/or Registered Provider Corporation tax exemption if a charity	None	None, unless an exempt charity, in which case tax advantages are the same as registered CLG Charity.
Tax relief for donation	Gift aid for registered charity	None	Gift aid if an exempt charity

## Cooperative Society

These are part of the Community Benefit Society family. The key difference is that Community Benefit Societies are set up to benefit the community whereas Cooperative Societies are set up to benefit their members.

Some CLTs have sought to include a cooperative element. It is possible to do so by setting up a two-tier structure where the CLT owns the land in perpetuity and leases it to the co-operative society on a 99 year lease. This approach is gathering interest among CLT groups.

## Limited liability

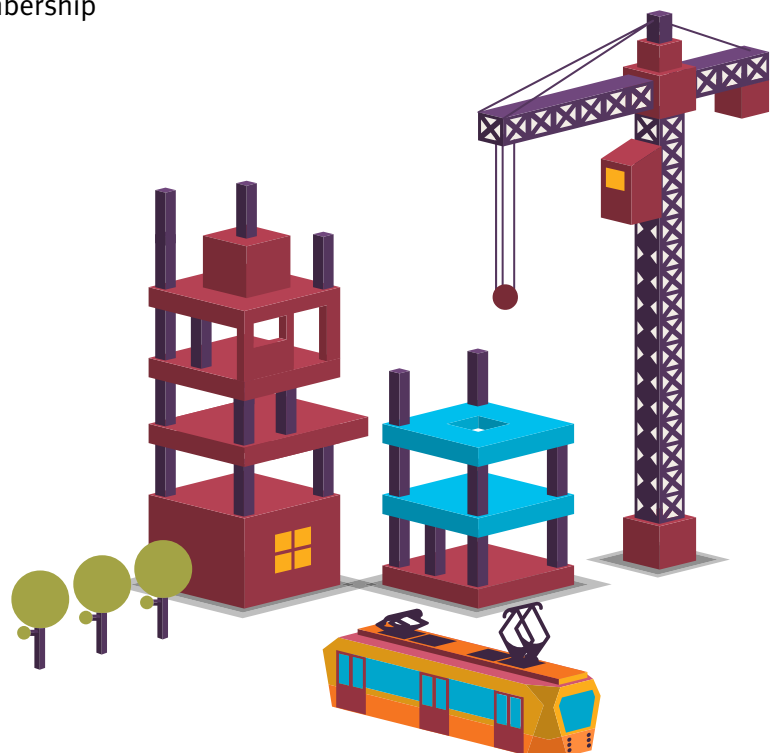
All these forms are limited liability, which means that in the event of the CLT not being able to repay its debts, the liability of the members is limited to either the amount they have paid for their shares (if a Community Benefit Society) or the amount they have guaranteed which is usually £1 (if a CIC Limited by Guarantee or a Company Limited by Guarantee). Board Members should take out indemnity insurance for their position as company directors/trustees. Directors and officers liability insurance is available through full membership of the National CLT Network.

## Regulatory bodies

During the life of a CLT and depending on the chosen legal form one or more of the following regulatory bodies will be key to the CLT:

- Financial Services Authority (FSA)  
[www.fsa.gov.uk/doing/small\\_firms/msr](http://www.fsa.gov.uk/doing/small_firms/msr)
- Companies House  
[www.companieshouse.gov.uk](http://www.companieshouse.gov.uk)
- CIC regulator  
[www.bis.gov.uk/cicregulator/website](http://www.bis.gov.uk/cicregulator/website)
- Charity Commission  
[www.charity-commission.gov.uk](http://www.charity-commission.gov.uk)
- Homes and Communities Agency  
[www.homesandcommunities.co.uk](http://www.homesandcommunities.co.uk)

For more information on each of these regulators, please visit the CLT Legal Toolkit on the National CLT Network website.



## 4.3 Factors to consider when choosing a legal form

In considering which is the most appropriate legal form for a CLT there are a number of factors that need to be thought through:

- **Ethos:** What sort of organisation does the CLT want to set up? Does the legal form help meet this ethos?
- **Funding:** Is the legal form appropriate for the financial arrangements required (for example, attracting grants, taking loans or raising share capital)? Does the legal form allow for the CLT to conduct its chosen training activities? (The pros and cons of registering as a charity are explored in the box below.)
- **Membership:** Is the legal form democratic and does it enable local and interested people to be involved? Does the CLT want the beneficiaries of the new homes or assets to be able to join and does the legal form allow for this?

- **Long-term use:** CLTs are organisations that are intended to have a very long life since the purpose of a CLT is to ensure that the homes or assets remain affordable for future generations. A group will need to consider the potential future uses of the CLT and whether the legal form will enable the CLT to pursue different kinds of projects as new uses emerge e.g. an energy generation scheme or community hall.
- **Process:** Is the legal form effective, efficient and economical?

A critical decision is whether or not to become a registered charity. Some of the advantages and disadvantages of charitable status are explored in the boxed text below.

### Registering as a charity: the pros and cons

Registering as a charity can provide significant advantages for a CLT. Charities are the ideal vehicle for attracting grants and donations and can attract loan finance. There are also significant tax benefits to being a charity. However, charities are heavily regulated and choosing to register will impose restrictions on the CLT's activity and legal form.

To register as a charity, a CLT must have an agreed purpose which matches one of the 13 charitable purposes defined by law. Depending on planned activities, suitable ones for CLTs may be 'prevention or relief of financial hardship'; 'advancement of citizenship or community development' or the 'advancement of environmental protection or improvement'. When applying for registration it is incumbent on the CLT to prove that it will be following and meeting those objectives in a public benefit test. This is strict because of the significant public trust and tax benefits experienced by charities.

Charities cannot pursue trading activities outside their primary charitable purpose. There are limited exceptions but a CLT should **always** seek professional advice if it wishes to pursue non-charitable activities. For example, developing market housing to cross-subsidise the development of social rental units can be problematic and not automatically permissible for a Charity. However, it is possible to set up a wholly or partly owned trading company as a subsidiary for a Charity that can gift its profits back to the Charity.

Only Companies Limited by Guarantee and Community Benefit Societies can become charities, and a CLT will need to consider this when choosing its legal form. However, a CLT can choose to register as a charity at any time. The decision to register is generally final, so a CLT cannot "abandon" its charitable status to pursue non-charitable purposes.



## 4.4 Good governance

Whether or not a CLT also becomes registered with the Homes and Communities Agency and/or the Charity Commission, the CLT will need to act in a transparent and accountable way to its community.

### Governing documents

The governing document(s) of a CLT are its 'rule book'. This sets out:

- The CLT's Objects (i.e. purpose);
  - The powers the CLT has to fulfil its Objects;
  - Membership of the CLT, including members rights and how they may join, retire, resign and may be removed;
  - A restriction on members being able to access the CLT's assets (part of the 'asset lock');
  - How general meetings of the CLT are to be convened and held, including voting rights of members;
  - The composition of membership of the board, how Board members are to be appointed, retirement provisions and powers to remove a Board member;
  - The powers granted to the Board, how it is to conduct its business, voting rights and powers to delegate to sub-committees and others;
  - A rule preventing Board members profiting by their position (this deals with conflicts of interest);
  - Provisions dealing with paid officers of the CLT (e.g. chief executive, finance director etc), if applicable;
  - Provisions dealing with the need to produce annual reports/accounts etc. and the appointment of an auditor;
  - What happens to the CLT's assets if it were ever to be wound up;
- How the CLT may execute documents as deeds;
  - How to make changes to the constitution; and (if relevant)
  - Powers for the Board to make bye-laws regulating how the CLT is to be run.

### Governing policies

In order to ensure that the CLT upholds good governance the CLT will need to have the following policies:

- **Identifying and dealing with conflicts of interest:** This will establish procedures for identifying those activities and interests of members which may carry a risk of bias in the conduct of their CLT duties. It will define when members must abstain from decisions in which they have an interest and how to treat decisions which have been taken in which a conflict of interest has become apparent.
- **Register of directors' interests:** This will record those activities and interests (especially financial) of CLT directors which may carry a risk of bias in the conduct of their CLT duties.
- **Code of conduct:** This outlines the rules and proper practices of the CLT, including the standards and principles which guide decision making and procedures of the CLT. For example, the behaviour and probity of directors, engagement with the community and appropriate use of resources. A template Code of Conduct for CLTs is available from the National CLT Network.
- **Trustee role description:** This will define the legal obligations of CLT trustees, including their required competencies, responsibility for decisions and accountability to members.
- **Financial authority policy:** This defines the procedures for taking and delegating financial decisions, and making transactions.

- **Reserves policy:** This sets out the CLT's policy on generating and handling financial reserves, including what proportion of turnover must be set aside and how it is to be safeguarded, and the circumstances under which such reserves can be used by the CLT.
- **Allocations policy:** This defines the CLT's approach to allocating housing units to prospective residents. It will set out allocations criteria such as economic and local residency requirements as well as any s106 obligations with the local authority.
- **Disposal models and disposal/occupancy cascade:** This defines the manner in which the CLT will release its assets, such as through sale or lease of housing, and the manner in which it will retain an interest in the property for long-term sustainability. The disposal/occupancy cascade can form part of the allocations policy. This gives the ability to provide that the first and subsequent lettings will be on similar terms.
- **Policy relating to repossession of property:** This sets out how the CLT will manage breaches of tenancy conditions at various stages from initial interviews and letters to the tenant up to service of legal notices to start court proceedings for possession. The CLT should be firm but fair to balance its interests in a reasonable and proportionate way with that of the tenant and neighbouring tenants.
- **Data protection policy:** This determines the CLT's practices for handling and retaining confidential details of residents and other persons in accordance with legal data protection requirements. This will also establish procedures for handling a breach of confidentiality.
- **Exit strategy:** In the event that the CLT is to be wound up or its assets transferred to another CLT or similar entity, where should it go to? The constitution can set this out in either specific or general terms.

Please visit the National CLT Network website for relevant template documents.

## Responsibilities of Directors

The most important responsibilities of CLT Directors are those set out in the Companies Act 2006. These are there to ensure Directors act with probity and diligence, and are:

- 1 To act within their powers as Directors, as authorised by the CLT's Memorandum and Articles\*
- 2 To avoid conflicts of interest
- 3 To declare interests
- 4 Not to accept any benefit from a third party which is offered because of their position as a Director
- 5 To exercise reasonable care and diligence, and skill commensurate with their own knowledge and experience
- 6 To exercise independent judgement
- 7 To promote the success of the CLT, having regard to its long-term success, its employees, suppliers and customers, community, environment, members and to high standards of business conduct. This is the most important of the Directors' responsibilities, and includes a duty to actively promote the success of the CLT, not merely to abstain from harming the CLT.

\*The Companies Act 2006 does not govern Community Benefit Societies but the above list reflects the usual requirements of a Society's Rules (its constitution) and good practice governance.

In addition, the Directors will have some procedural responsibilities according to the legal form the CLT has chosen, such as filing their Annual Return and Accounts, and completing an annual Community Interest Review (in the case of CICs).

