HM Treasury

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response to consultation

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Contents

1 Introduction

1.1 This document is the Government's response to the consultation on a package of measures to improve Industrial and Provident Society (IPS) legislation, *Industrial and Provident Societies: growth through co-operation*. The consultation was issued on 26 July 2013, was open for eight weeks, and closed on 20 September 2013.

1.2 Chapter 1 of this document outlines the background to the consultation and the wider context. Chapter 2 outlines each of the measures being considered in the consultation, a summary of responses received and how the Government is proceeding. Chapter 3 provides a summary of the Government's decisions and next steps. Chapter 4 gives a full list of respondents.

1.3 IPSs form a major part of the mutuals landscape, with a diverse mix of over 7,600 independent IPSs in the UK. The Industrial and Provident Societies Act 1965 (IPSA) allows for the registration of two types of societies. The first of these are co-operative societies, which are businesses owned and run by and for their members. The second of these are community benefit societies, which operate for the benefit of the community in which they work (e.g. housing associations). The IPS form embodies the democratic principle, with each member having an equal voting right regardless of their level of financial commitment. IPSs cover a vast range of businesses and industries; including public services, football clubs, credit unions, wind farms and agriculture. They also come in a range of different sizes from the UK's largest mutual, with an annual turnover of more than £14 billion, to community based societies with a handful of members. Moreover, IPSs have good geographic reach with an IPS located in every postcode area across the UK. The co-operative movement is still growing with membership in the UK at over 15 million in 2013 and a combined turnover of over £37 billion.

1.4 The Financial Conduct Authority (FCA) is responsible for IPS registration – a function similar to that performed by the Registrar of Companies for companies registered under the Companies Act 2006. In order for an institution to be registered as an IPS, it must satisfy the FCA that either (a) it is a bona fide co-operative or (b) its business will be conducted for the benefit of the community.

1.5 While co-operative enterprises may, in principle, take any legal form, the IPS is a legal form designed specifically for them. HM Treasury has responsibility for IPS policy and for the governing legislation. The primary piece of legislation is IPSA 1965, supplemented by several further pieces of legislation, all of which the forthcoming Consolidation Bill will cement into one place.

Background to the consultation

1.6 The Government's approach to mutuals is enshrined in its founding document, the Coalition Agreement, where it set out its commitment to foster diversity and promote mutuals. The Government's vision for the IPS sector is of a diverse, healthy and successful sector which is able to continue to offer a broad range of services to an ever-growing number of members. The Government also believes that it is vital that the unique features of the traditional IPS form are preserved, and that the sector stays focused upon serving its members in line with its core, member-focused principles. The measures proposed in the consultation aimed to help the sector achieve these key objectives and ensure the IPS sector has a legislative environment that will allow it to thrive.

1.7 In addition to the measures covered by the consultation the Government proposes to implement a number of key reforms to IPS legislation. The first of these is the Co-operatives and Community Benefit Societies Consolidation Bill, which was announced in January 2012. The Consolidation Bill, which was welcomed by the sector, will consolidate existing IPS legislation in one place, and is an important step in reducing legal complexity for new and existing societies. The Government has today introduced the Consolidation Bill into the House of Lords, and the Bill is expected to complete its passage through parliament before the end of the current legislative session.

1.8 While the Consolidation Bill will make existing legislation clearer and easier to use for IPSs, it cannot be used to make substantive policy changes. Therefore, the Government is also taking other steps to modernise IPS legislation. The Government is bringing into force various elements of the Cooperative and Community Benefit Societies and Credit Unions Act 2010 (the 2010 Act). Specifically, the Government will commence:

- Section 1 which will allow societies to register as co-operative or community benefit societies, instead of Industrial and Provident Societies. This is a change requested by the sector, which believes that the new name is more appropriate and up-to-date;
- Section 3 which will apply the Company Directors Disqualification Act 1986 to IPSs. This will offer IPSs protection, because it enables directors found guilty of a variety of offences relating to the mismanagement of an IPS to be barred from holding office in a different IPS;
- Section 4 which will give the Treasury power by regulations to apply certain legal provisions relating to companies to IPSs; and
- Section 5, which will give the Treasury power by regulations to make legislative provision for credit unions corresponding to that for building societies. The Government does not intend to use the Section 5 power at present, but will keep the power under review.

1.9 Sections 4 and 5 came into force on 1 December 2013. Following on from bringing the 2010 Act into force, the Government proposes to make other changes in secondary legislation, through existing powers.

1.10 The consultation asked for views from the co-operative sector and other interested parties about six proposed measures. These were:

- Measure 1 – whether the withdrawable share capital (WSC) limit should be raised, and if so, what level it should be raised to;
- Measure 2 – making insolvency procedures available for IPSs;
- Measure 3 – making further insolvency procedures available, specifically for credit unions;
- Measure 4 – giving the FCA additional powers to investigate IPSs should their behaviour be deemed improper or unlawfull;
- Measure 5 – applying Companies Act 2006 provisions regarding the inspection of the register of members to IPSs; and
- Measure 6 – allowing IPSs to submit electronic copies of registration documents to the FCA instead of printing and posting conventional paper documents, although this would not be compulsory.

1.11 The remainder of this document summarises the views of consultation respondents on these proposed measures, and sets out the Government's proposed course of action in relation to each of them.

2 The consultation responses and Government decisions

2.1 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. A full list of respondents is included in Chapter 4.

2.2 Most of the Government's proposed measures were well received by the respondents. Some of the questions prompted particularly useful, technically detailed responses which have helped to shape the Government's proposed course of action. Respondents particularly welcomed a number of the measures, including, increasing the withdrawable share capital, being able to submit electronic copies of registration documents and making insolvency procedures available to IPSs.

Measure 1: Withdrawable share capital

2.3 The Government committed in Budget 2013 to consult on raising the limit of the amount of withdrawable share capital (WSC) that one individual member of a society may invest in a single society. WSC is important to societies, as it is one of their primary sources of capital.

2.4 The amount of WSC a member can invest in a particular society is limited under current legislation, primarily to prevent any one member having undue influence over that society. At present, the limit is set at £20,000; a limit that has been in place since 1994. Previous increases to the limit have been made in line with the Retail Price Index (RPI). If the Government took the same approach now, the limit would be raised to £31,000.

2.5 However, given developments in the IPS sector, the Government accepts that there are arguments for raising the limit to a higher level than £31,000. In particular, a higher limit could facilitate greater investment in societies in industries requiring higher capital input, such as agriculture, housing and energy. Therefore views were sought as part of the consultation.

Question 1: Withdrawable Share Capital limit: what the limit should be

The Government welcomes views on whether the limit for the WSC should be raised, and if so, views on the appropriate level for the WSC limit. It would also welcome supporting evidence and rationale for raising the limit to a particular level, and evidence on the benefits and risks of doing so.

2.6 22 of the 42 consultation respondents answered this question. 16 submitted answers in their capacity as senior executives within a co-operative or community benefit society, four as subject matter experts/legal advisors and two as industry/trade bodies.

2.7 All those who answered were in favour of increasing the limit from the current £20,000. However, only one respondent agreed with the figure being set at around £30,000 in line with the Retail Price Index. All other respondents called for higher limits ranging from £40,000 up to £100,000 with two of the respondents suggesting the limit should be removed altogether and left to the discretion of individual societies to decide an appropriate level. 15 of the replies suggested that a limit of between £60,000 and £100,000 would be a sensible figure.

2.8 The respondent in support of a limit of £30,000 but no higher, expressed concerns that higher limits may allow a small number of shareholders to inadvertently control the co-operative and that this may in effect override the guiding principle of one member one vote. Another respondent representing a small IPS said that raising the limit above £50,000 would result in an unacceptable adverse cash-flow risk to smaller societies if an individual decided to withdraw their capital.

2.9 Other respondents calling for a higher limit, or removal of the limit altogether, pointed out that the statutory limit would be permissive, and individual co-operatives could mitigate these risks by making provisions to limit individual holdings via their own rule books. Individual IPSs can review their own WSC limits as they deem appropriate.

2.10 A number of respondents gave supporting rationale for raising the limit.

> "The current limit can result in a number of problems for Industrial and Provident Societies including: under capitalisation, over exposure to debt finance, limited ability to finance new investment and imposed constraints on new societies in capital intensive sectors."
>
> A co-operatives trade body
>
> "There is considerable inconvenience to both the society and members in having such a low limit. A limit in excess of £50,000 would be more appropriate."
>
> A co-operative

2.11 One key stakeholder quoted evidence from a paper by Regeneris Consulting, Economic Effects from the Current Limit on Withdrawable Share Capital: "Changes in earnings or asset prices over the period since the limit was set at £5,000 in 1975 would suggest that the limit should be reset at somewhere between £60,000 and £100,000... The modelling work suggests that the potential impact of the current limit could be adding £1.5 million to £2.5 million pa in annual financing costs, or a net present cost over 10 years of £12.7 million to £23.5 million. These costs would be reduced by increasing the current limit on withdrawable share capital, although we would only expect the costs to be eliminated by increasing the limit to around £100,000..."

2.12 This respondent concluded that they were in favour of the higher limit of £100,000 and a number of the other respondents endorsed these comments.

2.13 One respondent said that the low limit is a particular problem in capital intensive sectors such as energy and housing.

2.14 Another respondent from an agricultural society argued that some agricultural co-operatives are capital intensive, requiring increasing levels of capital from members and other sources to compete in terms of scale and service in the food industry. They also thought that the level of external (bank) lending to capitalise agricultural co-ops is related to the level of member investment and argued that increasing the £20,000 limit would help to increase both member investment and access to external lending. They also commented that the number of farmer-members in a typical agricultural co-op is small relative to the amount of capital required and the investment per member is necessarily high. They have experience of cases where the £20,000 limit on WSC has resulted in some agricultural co-ops using loan instruments to attract capital from members that is reimbursable in the future but that the complexity of some loan terms and conditions, and their risk status, have proven problematic in some cases. They were therefore very supportive of an increase in the WSC limit.

Government response

2.15 Increasing the limit in line with RPI to £31,000 would effectively retain the status quo and put the limit back to the same real-terms value as the last time it was increased, in 1994. However, the Government sees good reasons to go beyond this, and allow for a real-terms increase to the limit.

2.16 The Government has carefully considered the suggestions put forward by respondents and on balance has decided that a limit of £100,000 is appropriate. Increasing the limit to this level will provide a boost to co-operatives, particularly those in more capital-intensive sectors, such as agriculture, energy and housing and should provide enough flexibility to address the needs of the wide variety of IPSs in the sector.

2.17 On the points raised by some respondents about risks around cash-flow and domination of an IPS by an individual investor, the Government believes these risks are best managed by individual IPSs via their own rule-books.

2.18 **Therefore, in light of the responses to this question, the Government will implement this measure and increase the limit for withdrawable share capital to £100,000.**

Measure 2: Application of provisions of the Insolvency Act 1986 for company voluntary arrangements and administration to IPSs

2.19 At present, IPSs cannot enter administration or a voluntary arrangement with creditors – the only option for an insolvent society is to wind itself up or be wound up by the court. The Government committed at Budget 2013 to consult on the introduction of an insolvency rescue procedure for IPSs and credit unions. Specifically, the Government proposed to apply Part 1 (company voluntary arrangements) and Part 2 (administration) of the Insolvency Act (IA) 1986 and Part 26 (arrangements and reconstructions) of the Companies Act (CA) 2006. The Government has the power to do so under s255 of the Enterprise Act 2002. The insolvency procedures would be applied to all IPSs, except those societies which are a private registered provider of social housing or are registered as a social landlord. Societies of this description are excluded from the scope of the power.

2.20 The Government identified a number of potential benefits to enacting an insolvency rescue procedure, including the potential to:

- increase chances of rescue for troubled societies therefore protecting members and jobs; and
- address a specific problem for football supporter's societies which mean that they cannot own top-level football clubs (Football Association rules require clubs to have the power to go into administration).

2.21 Given the complexity of this proposal the majority of the questions in the Government consultation document (15 of the 20 posed) related to this measure. Views were sought on the general approach as well as a number of requests for technical expertise on specific points.

2.22 All of the respondents who commented on this proposal were supportive of the intent, with one respondent calling the measure "well overdue". 32 of the 42 respondents provided comments on some or all of the questions relating to this measure.

2.23 A summary of the detailed responses in connection with the questions asked relating to this measure follows below.

Question 2: General approach to drafting s255 order

Do you agree that legislation which applies Parts 1 and 2 of IA 1986 to IPSs should be broadly in line with what has been done with respect to building societies?

Can you draw attention to differences between building societies and IPSs which would require different provision for the IPSs?

2.24 There were 30 consultation responses to this question, all of which welcomed the proposal in principle. However, a number of the more detailed responses pointed out differences between IPSs and building societies that led them to generally favour greater uniformity with company law rather than that applied to building societies.

2.25 A number of the respondents also pointed out that a beneficial outcome of this measure would be in clarifying the ability of IPSs to access the Pensions Protection Fund.

Government response

2.26 The views that uniformity with company law may be more relevant have been taken into account when drafting for a number of the provisions, particularly in relation to the functions of the Financial Conduct Authority (FCA), as registrar and regulator, and of the Prudential Regulation Authority (PRA) and the Financial Services Compensation Scheme (FSCS) manager.

2.27 As the proposals have been worked up in more detail, full account has been taken of significant differences in the legislation being applied (between IPS legislation and the Building Societies Act 1986). This has tended to bring provisions generally more in line with provision made for companies.

Question 3: References to registrar of companies and the role of the PRA and the scheme manager

For the purposes of Part 2 (administration) is it appropriate that the PRA should generally cease to be empowered to do anything or have anything done in relation to it under a provision of that Part if it has revoked its authorisation of a society? If yes, are there any exceptions?

2.28 This question arose in connection with the need to apply insolvency rescue legislation to societies which are, or have been, authorised under FSMA 2000. 19 responses addressed this question, many of which expressed the view that uniformity with legislation for companies which are authorised persons (e.g. banks) was important here. In order to achieve such uniformity, the PRA would continue to have the relevant powers over firms who are, or have been, authorised persons.

Government response

2.29 Part 24 of FSMA 2000 (insolvency) provides for the application of insolvency legislation in relation to companies which are authorised persons, and will be applied with modifications in relation to relevant societies. This will give the FCA and PRA functions in relation to voluntary arrangements made for societies authorised under FSMA 2000 and the administration of such societies. This approach provides uniformity with company legislation and a more effective means of providing for regulators' functions in the case of a relevant society which is an authorised person. It also recognises the need to make separate provision for the FCA's registration functions under IPSA 1965. For all relevant societies, whether or not authorised

under FSMA 2000, the FCA (as registering authority under IPSA 1965) is to have the functions conferred by the applied legislation on the registrar of companies.

2.30 With reference to the specific point in Question 3, this means that the PRA, like the FCA, may or may not have functions in relation to a relevant society in administration (or subject to a voluntary arrangement) which is, or has been, regulated by the PRA. The position is determined by Part 24 of FSMA as applied by the Order.

Question 4: Applying Part 1 of IA 1986

Do you agree that enabling IPSs to conclude binding and effective arrangements with creditors would be beneficial, particularly for societies which are in financial difficulty but are not actually insolvent or which are insolvent but have prospects for recovery?

2.31 There was support from all 24 respondents who provided comments on the question of applying Part 1 of IA 1986 to relevant societies.

2.32 The most significant issue to arise in connection with this question was how far members' claims for the payment of money due in relation to deposits or other sums in respect of shares should count as "debts" for the purpose of Section 1 of IA 1986. In the case of a building society a reference to debts includes a reference to liabilities owed to the holders of shares. Responses generally supported the view that the formula "amounts owed in respect of shares" would be too wide for identifying the sums owed by a society to a member which may be included within a composition in satisfaction of debts.

2.33 Another issue which emerged in responses to this question was whether Section 5 of IA 1986 should make the approval of a voluntary arrangement binding on members so far as they are entitled to the payment of money due in relation to deposits.

Government response

2.34 In line with the consultation responses, the Government will enable IPSs to conclude binding and effective arrangements via the creditor's voluntary arrangement (CVA) procedure with creditors. In doing so, the Government will take into account that a member may be a creditor of a society in relation to a sum to which the member is entitled other than as a member or shareholder. As regards a sum owed in respect of shares, the member is to be treated as entitled to the payment of a debt for the purposes of a CVA if: (a) the society is an authorised deposit taker; and (b) the amount concerned is owed in respect of a deposit. This does not mean that the member is generally to be treated as a creditor. It gives the member certain rights of a creditor in relation to the society's liability to account for the member's deposits where this is appropriate.

Question 5: Prosecution of delinquent officers

Do you agree that this is an appropriate modification of section 7A?

2.35 This question was in reference to the Government's proposal to modify section 7A so that the FCA is the appropriate authority for investigating reports of suspected offences in connection with the moratorium or voluntary arrangement with respect to a relevant society (rather than the Secretary of State in England and Wales and the Lord Advocate in Scotland, as is the case for companies); that either the Director of Public Prosecutions or the FCA is the

prosecuting authority; and that the PRA also should have power to investigate and prosecute in the case of an IPS which is a PRA-authorised person.

2.36 23 people responded to this question. While the majority were in broad agreement that the FCA and PRA should have these additional powers, a number of responses indicated that the Secretary of State should continue to have a role in the investigation and prosecution of offences connected with a moratorium and questioned the need to make different provision for societies which are authorised persons.

Government response

2.37 In light of the responses received, the Secretary of State and Lord Advocate will be retained as investigating and prosecuting authorities. This is in line with provision for companies, but also, in recognition of the role of the FCA as registering authority under IPSA 1965, these functions are also to be exercisable by the FCA.

2.38 In recognition of the long standing role of the Lord Advocate as head of the system of public prosecution in Scotland, and the exclusive jurisdiction of the Lord Advocate as regards the bringing of public prosecutions in Scotland, section 7A prosecutions in Scotland will be brought by the Lord Advocate.

Question 6: Schedule A1 to the 1986 Act (the moratorium)

Do you agree that smaller IPSs ought to be able to obtain a moratorium? Do you agree with these proposals on qualifying limits?

2.39 24 respondents answered this question. There was unanimous agreement that smaller IPSs should be able to obtain a moratorium. Where views differed was around whether the more appropriate criteria for determining whether a relevant society qualifies as small (and therefore for obtaining a moratorium) would be the qualifying conditions for companies or provisions exempting small societies from accounts and audit requirements in the Friendly and Industrial and Provident Societies Act 1968.

2.40 Some of the respondents favoured uniformity with company law. Slightly more responses however, expressed a preference to use the audit exemption criteria and drew attention to the advantage of relying on an existing classification for small registered societies and the possibility of confusion if a new classification was introduced. Three respondents suggested that the test should follow company law in requiring two out of three conditions to be satisfied.

Government response

2.41 The Government has decided that there should be no criteria determining eligibility for a moratorium according to the size of a registered society. A relevant society which has Part 4A permission to accept deposits is ineligible by virtue of paragraph 2(2)(b) of Schedule A1 to IA 1986. This means that credit unions and other relevant societies which are deposit takers will, like building societies, be outside the scope of Schedule 1A. The Order omits paragraph 3 (eligibility conditions) but does not modify paragraph 2(2)(b), with the result that all relevant societies except deposit takers may benefit from the moratorium. The exception is consistent with the position for other deposit takers; the reasons for excluding companies and building societies are equally applicable in the case of other mutual deposit takers.

Question 7: Applying Part 2 of IA 1986

Do you agree that enabling IPSs to go into administration upon the appointment of an administrator or the making of an administration order would be beneficial, particularly for societies which are in financial difficulty but are not actually insolvent or which are insolvent but have prospects for recovery?

2.42 23 of the 42 respondents provided commentary for this question. Responses were supportive of the proposal to apply Part 2 of Insolvency Act 1986. Some concern was however expressed from some respondents about the need to protect the interests of members, particularly in relation to retaining the society's status as a mutual body, or of the community for whose benefit the society's business is conducted. Some responses suggested that these interests should be reflected in the objective of administration or should be the overriding objective.

2.43 Another issue which emerged from this question is whether a relevant society which is an insurer should be covered by the Order or by the Financial Services and Markets Act 2000 (Administration Orders Relating to Insurers) Order 2010.

2.44 Consultation responses were generally in favour of members' equal participation (with creditors) in the administration process.

Government response

2.45 Regarding the application of Part 2 generally, the Government does not have power to change the purpose of administration or introduce a new objective via secondary legislation. The application of Part 2 does not stretch to enabling a society to enter administration on different grounds or with aims which compete with the interests of creditors.

2.46 To address concerns relating to the need to respect the mutual principle of one member one vote, the Order will provide for separate meetings of creditors and members. The court will determine the outcome if either meeting fails to approve proposals or substantial revision. As a society can only be rescued as a going concern if it continues to be a bona fide co-operative or to be conducted for the benefit of the community, members will quite rightly have a more prominent role to play in its administration than shareholders in the administration of a company.

2.47 The interests of members and of the community benefitted by a society are partly protected by modifications which give members certain rights in parallel with the rights of creditors, to ensure that members can participate on an equal footing and enable the FCA to participate in the proceedings. Additional measures have been included to protect against major structural change and the use of administration as an easier route to demutualisation.

2.48 As regards relevant societies which are insurers, the Government has taken the view that insolvency rescue legislation should be applied to them by the Order and not by the FSMA (Administration Orders Relating to Insurers) Order 2010. This will treat relevant societies which are insurers in the same way as other relevant societies rather than other insurers, and is considered to be the best way to respect their status as mutuals.

Question 8: Appointment of administrator by holder of floating charge

Do you agree that the holder of a floating charge given by an IPS should be entitled to appoint an administrator? If yes:

1 should the holder of the charge be prohibited from appointing a receiver?

2 are any of the exceptions made for companies in sections 72B to 72GA of IA 1986 relevant (so that a qualifying charge holder should be able to appoint a receiver under any equivalent provision)?

3 should 'administrative receiver' have the same meaning in substance as it does for England and Wales and for Scotland in Part 3 of IA 1986?

2.49 The 23 responses to Question 8 were overwhelmingly in support of the proposal to allow the holder of a floating charge to appoint an administrator and, in consequence, to prohibit a floating charge holder from appointing an administrative receiver. All agreed that the meaning of "administrative receiver" for these purposes should follow the company law meaning.

2.50 Most of the responses to part 2 of the question were in support of providing for exceptions to the prohibition against the appointment of an administrative receiver by a floating charge holder on the ground that societies should be treated in the same way as companies. Some responses stated that equivalent exceptions would not be relevant. One respondent stated that the appointment of an administrative receiver would in many cases, be inconsistent with the objectives of rescue as a going concern, but that the exclusion for urban regeneration projects (section 72DA of IA 1986) would be useful.

Government response

2.51 The Government will proceed with these measures which will be in line with company insolvency legislation. The prohibition against appointing an administrative receiver for companies is in Part 3 of IA 1986, which does not apply to relevant societies, so self-standing provision for societies will be made. The prohibition does not apply to societies registered in Scotland because the holder of a floating charge given by a society whose registered office is in Scotland is not competent to appoint a receiver. Also, as for companies, transitional arrangements apply the prohibition in relation to charges created after a specified date. These measures will ensure that a floating charge is enforced by an administrator with duties to all creditors and not, in England and Wales, by an administrative receiver with duties only to the floating charge holder.

2.52 Responses supported the proposal to define administrative receiver for these purposes in line with the definition in Part 3 of IA 1986, therefore a definition in substantially the same terms has been included.

2.53 Despite many of respondents believing there was an argument for treating relevant societies in the same way as companies in regard to company law exemptions, little evidence was provided that arrangements which depend for their effectiveness on allowing the appointment of an administrative receiver are in fact made by relevant societies. The Government will therefore not include these, or alternative, exemptions.

Question 9: Floating charges and the prescribed part (section 176A of IA 1986)

Do you agree that the administrator of an IPS should be required to comply with section 176A?

2.54 23 responses were received for this question. Responses were broadly supportive of the proposal. No responses highlighted any drawbacks of requiring the administrator, where a floating charge relates to property of a relevant society which is in administration to make a prescribed part of the society's net property available for the satisfaction of unsecured debts, as required by section 176A.

2.55 One respondent expressed the view that the net property of a relevant society is more likely to be less than the prescribed minimum, so that the administrator is more likely than the administrator of the average company to be entitled to conclude that the cost of making a distribution to unsecured creditors is disproportionate to the benefits (in which case the requirement does not apply).

Government response

2.56 Section 176A will be applied with the small modification that for "company" one will read "relevant society". Also, the Insolvency Act 1986 (Prescribed Part) Order 2003 will be applied to a relevant society which is in administration, so that the prescribed minimum for the purposes of section 176A(3) is £10,000 (minimum value of the society's net property), and the prescribed part is to be calculated in the same way as for a company and is subject to the same ceiling of £600,000.

Question 10: Application for administration order and notification of appointment

Do you agree that the regulators should be entitled to apply for an administration order?

Are there any circumstances under which a member of an IPS (as a contributory or otherwise) should be entitled to apply for an administration order?

2.57 24 respondents answered this question and their responses were broadly in agreement that the regulators should be entitled to apply for an administration order. Some responses suggested that the FCA should be able to apply only on the grounds linked to its role as the registrar or regulator (in the case of approved persons), others that it should not have power unless it would have similar power over a company.

2.58 Regarding the question of circumstances under which a member of an IPS should be entitled to apply for an administration order, responses again were broadly in agreement that a member should be entitled to apply for an administration order. Some responses expressed the view that members should only be permitted to apply on specified grounds such as, if there is an irresolvable problem with the governance of the society, the society is not being governed in accordance with its rules or is not functioning as a bona fide mutual body.

2.59 One response thought that safeguards would be needed to stop abuse by disaffected members. Another said that allowing a defined proportion of members who met appropriate criteria to apply for an administration order would be in keeping with the principle of operating societies in a democratic way with and for members. One respondent thought that it would be inappropriate for individual members to be entitled to apply for an administration order.

Government response

2.60 Greater stress has been laid since the consultation paper was published on the distinction between the FCA as registrar and the FCA as regulator of approved persons, and the question of the FCA's power to apply for an administration order has been considered separately in relation to both capacities.

2.61 The Government's view is that the FCA (as registrar) should be in a position to apply for an administration order. The registrar of companies is not empowered to apply for an administration order for a registered company, but does not have functions equivalent to those conferred on the FCA by IPSA 1965.

2.62 The Government does not believe it is necessary to limit the grounds for an application expressly by reference to the FCA's role. The grounds on which the FCA applies will rest on a consideration of matters within the FCA's sphere of responsibility. All decisions taken by the FCA must be taken in the proper exercise of its functions, whether as registrar or regulator of approved persons.

2.63 As regards applications by the regulators, Part 24 of FSMA 2000 (as applied to relevant societies) empowers the FCA, as regulator of approved persons, the PRA and the scheme manager to apply for an administration order in relation to a relevant society which is (or in some cases has been) an authorised person. In this respect relevant companies will be in the same position as companies authorised under FSMA 2000.

2.64 Provision has been made to allow any member to apply for an administration order provided that they would be entitled to petition for winding up. To the extent that there is a risk of inappropriate applications by members, the interests of creditors and other third parties are protected by provision requiring the court to be satisfied that an order is reasonably likely to achieve the purpose of administration.

2.65 In the case of a credit union a single member could apply provided that the share in respect of which they are a contributory must have been held for at least six months. As there should be at least 21 members, no member would apply on the basis that the number has been reduced below two. For other societies any number of members may apply.

Question 11: Process of administration (involvement of members)

Do you agree that these are appropriate modifications for meetings and the participation of members in the process of administration? How should the expenses of a members' meeting under paragraph 52(2) or 56 (1) (as modified for an IPS) be met? Should they be payable out of the assets of the IPS as an expense of the administration?

2.66 Of the 24 responses to this question there was overwhelming support of the proposals for member participation in the administration process, including the proposal that the expenses of members' meetings be met out of the society's assets as an expense of the administration. It was generally considered that this reflects the democratic nature of the management and control of registered societies.

2.67 One response suggested that the costs of members' meetings should be publicised to all members and be subject to an appropriate ceiling. Another suggested that provision should be made in relation to the quorum of a members' meeting so that the number of members required for making valid resolutions is in accordance with the society's rules and allows for societies with a small membership.

Government response

2.68 The Government's view is that the quorum laid down for meetings of members of a society in administration should be regulated by the society's rules. While this may result in administrators' proposals for different societies being approved or rejected in meetings with varying requirements for a quorum, it ensures that a given society applies the same rule about the quorum for these meetings as it applies in the case of other meetings. Where there are no such rules, the default position is the same as for contributories of companies, the insolvency rule concerned requires at least two who are entitled to vote.

Question 12: Powers of the administrator – general

Do you agree that the order should provide a safeguard for this purpose in the legislation? Do you agree that the order should provide a safeguard for this purpose and that the FCA should have a supervisory function?

2.69 Respondents unanimously supported proposals for the safeguards outlined in Question 12, including the provision requiring proposals for amending the society's rules to be supported by a statement of compatibility with mutual principles issued by the FCA (unless the administrator is proposing demutualisation); and not to include any measure contrary to the provisions of the legislation which governs the society. Similar provision is made with respect to a compromise or arrangement proposed for the purposes of, or in connection with, a scheme for the reconstruction of a relevant society or the amalgamation of a relevant society with any other relevant society or any company.

2.70 Two issues emerged from consideration of these questions. First, what provision is needed to ensure that the administrator's power to borrow is modified to reflect accurately constraints on borrowing by registered societies? Secondly, is it necessary to provide for the possibility of conversion of a relevant society to a charitable incorporated organisation ("CIO") as an outcome of administration?

Government response

2.71 Regarding the administrator's power to borrow, the administrator of a company has a broad power to borrow. Applying Schedule 1 in relation to a registered society does not enable the administrator to borrow free of restrictions to which the society itself would be subject outside administration. Referring expressly to constraints on borrowing does not mean that the administrator's power to borrow would otherwise be unfettered, but ensures that the power will be read compatibly with the legal position.

2.72 The borrowing power is subject to specified enactments. Separate provision is made for credit unions and other societies. In each case the power is also subject to such other enactments and society rules as restrict or regulate power to borrow.

2.73 One response raised a question about the application of insolvency law to a registered society which has converted to a Charitable Incorporated Organisation (CIO). As such a society would cease to be a registered society on conversion to a CIO, it would become subject to the Charitable Incorporated Organisations (Insolvency and Dissolution) Regulations 2012 and would cease to be a relevant society for the purposes of the section 255 Order. Sections 228 to 234 of the Charities Act 2011 are not yet in force and will not be brought into force before the Order. The Government will consider at the appropriate time what provision needs to be made to allow for the possibility of conversion of a relevant society to a CIO as an outcome of administration.

Question 13: Powers of the administrator

Do you agree that the administrator of an IPS should have power to effect amalgamation, transfer of engagements and conversion into companies?

2.74 The majority of the 24 respondents supported the proposal that the administrator of a relevant society should be able to propose amalgamation, transfer of engagements and conversion into companies, and give effect to what is proposed if the members and creditors agree. They supported the view that these options should be available as an outcome of administration, but attached significant qualifications.

2.75 One response opposed the proposal as set out in Question 13, which would not require a special resolution of the members. This was on the grounds that there is no argument in favour of conversion to a company; and other amalgamations or transfers could be inappropriate and should be the subject of a special resolution to go before the members.

2.76 Among responses which generally supported the proposal there were a number of additional comments and points raised. Several drew attention to section 22 of Credit Union Act 1979, which provides that section 52 of IPSA 1965 (conversion into, amalgamation with, or transfer of engagements to company) does not apply to credit unions. Some, including the single response which expressly supported the proposal not to require a special resolution, said that the FCA should have power to prevent such steps if they did not appear to be necessary as part of the rescue. Others took it for granted that the administrator would have to propose any such arrangement in the best interests of the society.

2.77 Another respondent agreed in general terms but said that the required majority of members voting in favour of any such arrangement should be in line with what is required for such arrangements proposed outside administration (i.e. special resolution). Another raised concerns that the administrative process should not become an opportunity to remove asset locks or charitable status. A number of the respondents asked the question whether the purposes of administration should be adapted so that retaining mutual status is a primary objective (to avoid "rescue" through amalgamation, transfer of engagements or conversion to a company without good cause).

2.78 While concerns were expressed in different ways, one overriding view was that administration should not offer an easier route to demutualisation. Also, there was little support for allowing structural change proposed by an administrator to be approved by a majority of members (assuming that creditors also approve) rather than by the majority required for a special resolution outside administration.

Government response

2.79 The proposal was that the administrator should be able to recommend any of the arrangements in sections 50, 51 and 52 of IPSA 1965 for approval by the members and creditors. The requirements of those sections, except the requirement for a special resolution, would still be applicable, as would the restrictions in section 21 and 22 of CUA 1979.

2.80 In particular, there is no question of allowing a credit union to be converted into, amalgamated with, or have its engagements transferred to a company. Section 52 as applied to registered societies applies subject to the exclusion for credit unions. As applied to relevant societies in administration it is also subject to that exclusion.

2.81 Given the lack of support for requiring no more than a majority of members to vote for structural change, particularly where this could allow administration to be used as an easier route to demutualisation, the Government have decided that proposals involving any arrangement under sections 50 to 52 of IPSA 1965 must be approved by special resolution. Those sections will apply to a society in administration with modifications designed to bring that procedure into line with the procedure for approving administration proposals and the powers of the administrator.

2.82 This achieves greater uniformity for the approval of structural change for relevant societies, whether or not they are in administration. The administrator would call the initial general meeting, at which a resolution in favour of the change is to be proposed. If the subsequent meeting does not confirm the resolution, the administrator must report to the court.

Question 14: Applying Part 26 of CA

Do you agree that the application of Part 26 would be beneficial for IPSs?

Question 15 Provision to ensure that Part 26 measures are compatible with governing legislation and principles and rules for mutual status

Do you agree that the order should provide a safeguard for this purpose and that the FCA should have a supervisory function? Are any other modifications required?

2.83 The majority of respondents supported the proposal to apply Part 26 to relevant societies with the safeguards described. A small number of respondents however wondered whether Part 26 would be of much use to smaller societies.

Government response

2.84 In line with the majority of responses, Part 26 will be applied with the modifications outlined.

Question 16: Distributions to creditors

Do you agree that these are necessary modifications of rules relating to distributions?

2.85 The central question was about when a member of a relevant society is to be treated as a creditor in relation to amounts owed by the society, particularly for the purpose of distributions made by the administrator, including provision for equal ranking of unsecured debts and mutual credits and set-off. Where a member is entitled to a sum in a capacity other than as a member, they will be a creditor in relation to that sum. Where a member is entitled to a sum in respect of the member's shares, they are generally to be treated as a shareholder in relation to that sum. The consultation asked what exceptions should be made to this general rule.

2.86 One response stressed that it is vital to ensure that amounts owed by or to a member which arise from dealings with the society in a capacity other than as member (e.g. from selling to or buying from a co-operative or as an employee) are ordinary debts of the member or the society and must be dealt with as if the member were a third party debtor or creditor.

2.87 Another respondent raised a question about provision proposed for making distributions to members (in relation to sums due in respect of shares). Another question arising from detailed consultation was whether a member who withdraws capital should be treated as a creditor in insolvency proceedings started after the date of notice of withdrawal but before payment has been made.

Government response

2.88 Nothing in the Order affects the position of a member, as a creditor, in relation to sums to which the member is entitled in a capacity other than as a member. A credit union depositor who is a child under the minimum age for membership is not a member and has the rights of an ordinary creditor. Also nothing in the Order affects the position of a member as a contributory in a winding-up of the society. As for a member of a company, no contribution is to exceed the amount, if any, unpaid on shares. In the case of a withdrawable share which has been withdrawn a person ceases to be a member in respect of that share as from the date of the notice or application for withdrawal.

2.89 The Government has concluded that a member should be treated as a creditor with respect to deposits made as a shareholding member of a society which is an authorised deposit taker in administration, whether or not they have given notice of withdrawal of the deposits. The member must be owed an amount in respect of shares (i.e. an amount to which the member is entitled as a member); the society must be an authorised deposit taker; and the amount concerned must be owed in respect of a deposit. For other sums due in respect of shares, such as dividends or bonus declared but not paid when the society goes into administration, the member has no more than the rights of a shareholder.

Measure 2 Overall – Government response

2.90 Given the support for applying the insolvency rescue provisions to IPSs the Government will proceed with this measure, with relevant modifications.

Measure 3: Application of Part 2 of the Banking Act 2009 (bank insolvency) to Credit Unions

2.91 The Government committed in Budget 2013 to consult on the introduction of a special administration regime for credit unions, over and above the insolvency rescue procedures it proposed to introduce for societies registered under the IPSA, including credit unions. The Government sought views on the merits of applying Part 2 of the Banking Act (BA) 2009 (bank insolvency) to credit unions, in addition to Part 2 of the Insolvency Act (IA) 1986 (or Part 3 of the Insolvency (Northern Ireland) Order 1989) (administration).

2.92 The consultation document suggested that the potential benefits of introducing credit union insolvency under section 131 of BA 2009 were to:

- ensure that credit union members were treated in the same way as depositors in other types of credit institution;
- ensure that there could be a speedy Financial Services Compensation Scheme (FSCS) payout in the event of default; and
- allow flexibility to move into ordinary administration, but failing that provide a more suitable procedure for winding up.

Question 17: Applying Part 2 of the Banking Act 2009 to Credit Unions

Do you agree that applying Part 2 of BA 2009 to credit unions would provide a more effective and flexible procedure for dealing with financial difficulties and insolvency? Do you agree with the benefits identified above? How far would this measure carry risks of prejudicing credit unions in the ordinary course of business?

2.93 22 of the consultation respondents chose to answer this question. All of those that provided comments thought there was some merit in aligning credit union procedure with banks and building societies.

2.94 The majority of the responses provided little detail beyond a broad agreement with the measure or wanted to point out the importance of ensuring there are mechanisms for the protection and transfer of members' funds to other credit unions so they are kept in the sector and used for their original purpose.

2.95 The response from Association of British Credit Unions Ltd (ABCUL) supported this measure. They thought that benefits would include mitigating the risks that exist from the current non-formalised arrangements for credit union insolvency and would also have additional reputational benefits for a credit union by an orderly and effective resolution.

2.96 Four of the respondents with subject matter expertise either in insolvency or from a legal background also supported the measure and held the view that as credit unions are increasingly operating in a similar way to retail banks then it was important that the same specialised form of winding up to be applied in the case of credit unions. Two respondents welcomed the proposal to speed up FSCS payouts and mentioned it would be particularly helpful where current account services are offered by credit unions.

Government Response

2.97 The Government notes that the majority of respondents who answered this question expressed support for this proposed measure. However, after careful consideration, the Government does not intend to proceed with this measure at this time.

2.98 The implications of this measure have been considered in more detail since the consultation. The Government's view is that there is insufficient evidence at this time to determine whether any benefits over and above those which will be brought about by implementing the IPS insolvency rescue procedures (which include credit unions) would be achieved as a result of these further changes. It may also place an increased unnecessary legislative burden on to credit unions. The Government will therefore wait to judge the impact of the new insolvency rescue procedures for IPSs, before returning to the question of whether an additional special administration regime for credit unions would bring significant net benefits.

Measure 4: Application of Parts 14 & 15 of the Companies Act 1985 (investigations) to IPSs

2.99 This proposal would give the FCA additional powers to investigate IPSs should their behaviour be deemed 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 IPSs. This proposal aimed to create a level playing field with the requirements that companies face and increase confidence in the IPS form. As noted in Chapter 1, the Government commenced section 4 of the 2010 Act in December. Section 4(2)(a) of the 2010 Act gives the Treasury power by regulations to

apply Parts 14 and 15 of the Companies Act 1985 to IPSs. Under the proposals, a number of key powers under Part 14 of the Companies Act 1985 would be made available to the FCA.

2.100 These powers would 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 an IPS. 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 IPS has been conducted in a way which unfairly prejudices a group of members or for unlawful purposes. Other powers concerned the expenses of the investigation and would be payable in the first instance by the FCA but recoverable from the IPS investigated. The measure also proposed to give the FCA or an authorised investigator power to give directions to an IPS 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 an IPS on the grounds set out in section 448(2).

2.101 The Government also asked whether additional bodies to which disclosure can be made should be included in the list in Schedule 15C and invited views on the sanctions and offences in Part 14 of the Companies Act 1985 which are proposed to be applied in the case of investigations of IPSs.

Question 18: Investigations regulations

The Government welcomes views on the application of the powers of investigation from the Companies Act 1985 to IPSs. In particular do you agree:

1 that the circumstances for appointment of inspectors set out in section 432(2) of the Companies Act 1985 are suitable for IPSs?

2 with the proposal that the costs of the inspection should be recoverable from the IPS? (recognising that the FCA will first try to soak these costs up into their existing budget)

3 that the FCA, inspectors and section 447 investigators should be given the proposed powers?

4 that Schedules 15C and 15D (permitted disclosures of information) need to be adapted for IPSs, and if so, how?

5 that the sanctions and penalties in the Companies Act 1985 are suitable for IPSs?

6 that section 48 of the Industrial and Provident Societies Act 1965 could be repealed?

7 with the proposal not to apply the sections of the Companies Act 1985 listed in 3.51?

2.102 24 respondents answered this question. 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. There was also a suggestion that additional legislation may be needed to ensure that the regulator powers could operate effectively alongside each other.

2.103 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.

2.104 14 respondents called for Co-operatives UK and ABCUL to be added to the list of bodies to which disclosure can be made.

Government response

2.105 In line with the consultation responses, the Government will proceed with making these changes.

2.106 Despite the concerns raised about a possible regulatory power overlap for certain types of society the Government is not intending to exempt any IPS from this measure. The FCA's functions are analogous to those of Companies House and the Secretary of State.

2.107 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.

2.108 It is not possible to add ABCUL and Co-Operatives UK to the list of bodies to which disclosure can be made. Information gathered under requirements under the Companies Act is only to be disclosed to persons carrying out public functions and it would not be appropriate to include trade associations on this list. If an IPS wanted to share details of an investigation with their trade association they can, of course, do so.

Measure 5: Application of provisions in the Companies Act 2006 relating to inspection of register of members to IPSs

2.109 This proposed measure would increase IPSs' ability to prevent members from seeing their duplicate register of members, by giving them the right to refer the matter to court when sight of the register is sought for an improper purpose. The Government believed that this would be helpful because it gives IPSs options for avoiding unnecessary expense in response to vexatious or unlawful requests for information (the register contains private information about the members of the society), and would match provisions in companies legislation.

Question 19: Inspection of the register provisions

The Government welcomes views on the application of Companies Act 2006 provisions about the inspection of the duplicate register of members to IPSs. In particular do you think that:

1 IPSs should be given the right to apply to the court where they believe an application by a member to view the duplicate register is for an improper purpose?

2 there should there be choice of applying to the High Court or county court as in the Companies Act 2006?

2.110 While formal responses to the consultation tended to favour the proposal, further engagement with key stakeholders following the closure of the consultation revealed concerns that the measure may not address the type of behaviour they were most concerned about, and that the risk of damaging members' democratic rights were not outweighed by the potential benefits.

2.111 Four respondents felt that more information was needed before agreeing or disagreeing and in particular wanted to see a clearer understanding of what would constitute an 'improper purpose'. It was also suggested that other additional criteria should be added when members request to view or have a copy of the duplicate register such as a certain percentage of members being required. Another respondent thought that a potential penalty of up to two years in prison for non-compliance was excessive.

2.112 The question of fees to be charged also provided mixed results with the majority disagreeing with a fee being charged to view the duplicate register or to receive a copy while others accepted that a small fee for a copy may be justified.

Government response

2.113 Given the concerns expressed by a number of the respondents that this measure would infringe on the democratic rights of IPS members, and the decision by a key stakeholder to withdraw support for the measure, the Government will not proceed with this change.

Measure 6: Amendment of section 2(1) of Industrial and Provident Societies Act (IPSA) 1965 to amend requirements for registration documents to be submitted electronically for new IPSs

2.114 This proposed measure will provide an additional procedure to allow new societies to submit electronic copies of registration documents to the FCA instead of printing and posting conventional paper documents. This will give the FCA the option of allowing societies to submit registration documents online, but will not be compulsory as societies will be still be allowed to send in documents by post. This additional electronic submission process aims to make it quicker, easier and cheaper to register a new society.

Question 20: Electronic submission of registration documents

The Government welcomes views on the amendment of section 2(1) of the IPSA 1965 to allow IPSs to submit registration documents electronically.

2.115 29 of the respondents answered this question. All but two of those who commented on this proposal were supportive of the approach and welcomed the changes. There was a general view that the current requirements are out of date in terms of modern electronic communications and that the measure will be beneficial to societies and bring their registration systems into line with companies.

"This overdue measure will clearly be beneficial to societies and will bring their registration systems into line with companies and make them fit for purpose in the twenty first century. There are no obvious disadvantages to such a measure so long as it remains an option for societies and they have the alternative of submitting in hard copy only if they choose."

An individual response

2.116 Two respondents who agreed with the change also wanted to ensure that the option to submit conventional paper copies was retained because of concerns that some small societies may not have the capacity or desire to submit documents electronically.

2.117 One respondent representing a society expressed concerns about the risk of allowing electronic registration rather than physical signatures may undermine the legally binding contract on all parties and wanted to see signatures retained as part of good governance.

Government response

2.118 Given the support from respondents, the Government will proceed with this measure.

2.119 Once the measure is introduced IPSs will still be able to submit paper copies of registration documents if they choose to do so.

2.120 In relation to the risk which was raised about electronic registration replacing physical signatures, the ability to submit documents electronically already exists and this change is purely to remove the need to submit two signed copies of the society's rules. This measure would not remove the need for signatures as the signed documents would be scanned and sent in an electronic format.

3 Summary and next steps

Summary of Government decisions

3.1 Following consideration of the responses received to this consultation, the Government has made the following decisions in relation to the six measures.

- Measure 1 – Withdrawable share capital: the Government will **proceed** with increasing the limit for withdrawable share capital to £100,000;
- Measure 2 – Introduce insolvency rescue procedures for IPSs: the Government will **proceed** with this measure;
- Measure 3 – Apply provision for bank insolvency rescue to Credit Unions (Part 2 of the Banking Act 2009): the Government will **not proceed** with this measure;
- Measure 4 – Reproduce Companies Act provisions for IPSs with regard to investigative powers of the registrar (FCA): the Government will **proceed** with this measure;
- Measure 5 – Reproduce Companies Act provisions onto IPSs with regard to inspection of the register of members to prevent vexatious use of the register by disaffected members: the Government will **not proceed** with this measure; and
- Measure 6 – Allowing IPSs to submit electronic copies of registration documents to the FCA: the Government will **proceed** with this measure.

Next steps

3.2 The Government will now proceed with taking the necessary legislative steps to pursue this package of measures, as set out above, in tandem with the passage of the Co-operatives Consolidation Bill. The Government anticipates that both the Bill and the package of measures will be on the statute book by summer 2014.

4 List of respondents

Association of British Credit Unions Ltd

Business Recovery Services Department, PwC

Chelmsford Star Co-operative Society Limited

Community Power Cornwall Limited

Co-operative Development Scotland

Co-operative & Mutual Solutions Ltd

Co-operatives UK Ltd

Development Cornwall Limited t/as KABIN Ltd

Dina Devalia, Cork Gully LLP

DWF LLP

Ekopia Resource Exchange Ltd

Energy4All Ltd

Gareth Morgan, Sheffield Hallam University

GeoCapita Mutual

HM Land Registry

Home Group

Ian Snaith

Infinity Foods

Insolvency Lawyers' Association

Nathan Brown, Cooperantics LLP

National Allotment Society

Nicholas Hayes

Northern Ireland Insolvency Service

PACE Trustees Limited

Peter Turnbull

Radical Routes Ltd

Scottish Agricultural Organisation Society Ltd

Shared Interest Society

Somerfield Pension Trustees Limited

Sovereign Housing Association

Tamworth Co-operative Society

tCG Pension Trustees (Northern) Limited

tCG Pension Trustees (North West) Limited

tCG Pension Trustees (Scotland) Limited

tCG Pension Trustees (Southern) Limited

The Low Carbon Fund

The Low Carbon Society Limited

The Midcounties Co-operative Limited

The Southern Co-operative Limited

Trowers & Hamlins LLP

Wales Co-Operative Centre

Wrigleys Solicitors LLP

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