

The Community Interest Company Regulations 2005

Consultation response for the consultation beginning on 11 October 2004 and ending on 4 January 2005

1 Background to the consultation

1.1 The community interest company (CIC) is a new type of company, designed for social enterprises that want to use their profits and assets for the public good. Community interest companies will be easy to set up, with all the flexibility and certainty of the company form, but with some special features to ensure they are working for the benefit of the community.

1.2 The concept of the community interest company was outlined in the Cabinet Office Strategy Unit report “Private Action, Public Benefit” published in September 2002. In March 2003 the DTI launched a technical consultation on community interest companies and subsequently published a response outlining the Government’s intentions.¹ Primary legislation to create community interest companies was in Part 2 of the Companies (Audit, Investigations and Community Enterprise) Act 2004 (“the Act”) which received Royal Assent on 28 October 2004.

1.3 The DTI launched a consultation on the draft Regulations to be made under Part 2 of the Act on 11 October 2004 and requested comments by 4 January 2005.² The consultation asked respondents for comments on the draft Regulations and in particular for answers to five specific questions (reproduced in Annex A). The questions covered the following areas:

- Organisations conducting activities only for the benefit of their members or employees;
- The distribution of residual assets on the solvent winding up of a community interest company;
- Whether dividend paying shares issued by a community interest company should be “index linked” to protect their value (applicable on a solvent winding up);
- Restricting the ability of investor shareholders to control community interest companies;
- The appeal procedures.

¹ “Enterprise for Communities: Proposals for a Community Interest Company: Report on the public consultation and the government’s intentions” (October 2003) available at <http://www.dti.gov.uk/cics>

² “Consultation on draft Regulations for Community Interest Companies” (October 2004) available at <http://www.dti.gov.uk/cics>

The consultation responses and the Government's intentions

2 Responses received

2.1 The Government received 13 responses to the consultation, and is grateful to those who responded as well as to the technical panel that assisted in discussing investment issues. A list of those respondents who were willing to have their names and responses disclosed can be found at Annex B.

2.2 This document summarises the comments made by respondents and sets out the Government's intentions in the following sections:

- Activities not to be regarded as benefiting the community - organisations conducting their activities only for the benefit of their members or employees
- The distribution of residual assets on the solvent winding up of a community interest company
- Dividend bearing shares – Dividend cap
- Dividend bearing shares - Possible “index linking” of shares to adjust their value for inflation in a solvent winding-up
- Dividend bearing shares - Restricting the ability of investor shareholders to control community interest companies
- The appeal procedures
- Further amendments to Regulations

3 Activities not to be regarded as benefiting the community - organisations conducting their activities only for the benefit of their members or employees

Background

3.1 The consultation document (Question 1) asked for comments on a regulation drafted to provide that activities that benefit only the employees or members of a particular organisation would not satisfy the community interest test, unless the activities were not being conducted solely for private gain.

3.2 The regulation was also drafted to ensure that an applicant could not argue that a particular type of company (for instance a mutual organisation or company owned by its employees) was inherently in the community interest and therefore satisfied the community interest test regardless of its activities.

Consultation response

3.3 Of ten respondents that commented, two supported the proposed regulation, four were opposed and four were unsure or did not express a clear preference.

3.4 The Government notes that those respondents who were not satisfied with the regulation commented on the lack of clarity in the drafting. Three respondents commented that it was difficult to understand and there were three further comments that the drafting was ambiguous in parts. Specifically two respondents commented that the term “private gain” was not defined and this made the regulation difficult to interpret.

3.5 One respondent commented that the Government should not attempt to regulate this type of organisation because to do so risked creating grey areas and an uncertain regulatory burden. Of those who were satisfied with the regulation, one respondent commented that further guidance would be required to explain how it works in practice.

3.6 Two representative organisations emphasised in their responses that the CIC should be seen as one option among others for social enterprises.

The Government’s intentions and amendments

3.7 The Government notes the suggestion that it should not regulate activities being conducted only for the benefit of the members or employees. However, we continue to believe it is appropriate to regulate in line with our desired policy objective. This is that activities that benefit the employees or members of a particular organisation should not satisfy the community interest test unless they also provide an additional community benefit. Noting the comments on the lack

of clarity of previous drafting, we have amended the wording of the relevant regulation to clarify our intentions.

3.8 The Government will publish an accompanying note on the Regulations which provides more detail on the community interest test, including examples in general terms.³ The independent Regulator of community interest companies will subsequently publish guidance on the application of the test.

3.9 The Government agrees that the community interest company is one option for social enterprises. Although we believe it offers a valuable additional choice, it will sit alongside, and not replace, other options including the Industrial and Provident Society and other forms of organisation. This is not a policy that can be incorporated into legislation, but it will continue to inform the DTI's communications on community interest companies and social enterprise.

³ "Guidance note on The Community Interest Company Regulations 2005" available at www.dti.gov.uk/cics

4 The distribution of residual assets on the solvent winding up of a community interest company

Background

4.1 The consultation (Question 2) asked whether respondents agreed with the provisions for the distribution of a community interest company in a solvent winding up, after the claims of all creditors are satisfied. In summary the assets were provided by regulations to be distributed:

- (i) first to any investor shareholders that are entitled to such assets, but only up to the paid-up value of the shares;
- (ii) next, to an asset-locked body (community interest company, charity, Scottish charity or international equivalent) identified in a community interest company's memorandum or articles as a possible recipient of assets on winding up. The Regulator may decide not to allow such a distribution if, having received a request from a director or member of the community interest company being wound up, and having consulted where possible with other directors and members, he decides that the asset-locked body is not an appropriate recipient; and
- (iii) finally, if no asset-locked body is designated, or no designated asset-locked body is deemed appropriate, the Regulator may distribute the residual assets to any asset-locked body he deems appropriate.

4.2 Any member of a community interest company may appeal to the Appeal Officer against any direction or decision made by the Regulator under (ii) or (iii).

Consultation Response

4.3 Of ten respondents that commented, seven supported the Government's proposals, one was opposed and three were not sure or did not offer a clear preference. The Insolvency Service provided technical comments and the Government took these comments into account when coming to its conclusions.

4.4 The Government notes the broad support expressed in consultation for its approach to protecting the residual assets of a community interest company. Respondents confirmed that the level of intervention available to the Regulator seems sensible and offers adequate protection. One respondent argued that the Regulator should be given greater discretion to intervene without complaint from directors or members, where he feels it appropriate to protect the residual assets of a community interest company.

4.5 Another respondent stressed that sufficient provision must be made to ensure that investor shareholders receive assets only up to the value of the paid

up shares, so that the company's members would not be able to benefit from the distribution of assets of a community interest company. The respondent asked for the Government to underline the importance of this.

4.6 With regard to the Regulator's role where the CIC has not made an appropriate nomination of an asset-locked body to receive its assets, respondents generally agreed that the draft regulation achieves an appropriate balance between the role of the community interest company directors and the Regulator in determining to which body these assets should be transferred. One respondent suggested that the Regulator may prefer his responsibilities to be curtailed by setting a requirement for all community interest companies to identify in their memorandum or articles an asset-locked body to which their surplus assets should pass on winding up.

4.7 One respondent suggested that in those situations where there is no designated distribution, or the Regulator decides not to allow the distribution, directors as well as members of a community interest company should have a right of appeal against the Regulator's decisions/directions.

4.8 The response that did not agree with the Government's approach commented that where the Regulator considers the designated distribution inappropriate, there should be an obligation for the Regulator to consult only with the former community interest company's directors, though he should have the option, where he feels it appropriate, to consult also with its members.

The Government's intentions and amendments

4.9 The Government is encouraged by the confirmation from respondents that the draft Regulations provide an appropriate level of intervention for the Regulator to protect the residual assets of a community interest company.

4.10 The Government has noted the suggestion that the Regulator should be given greater discretion to intervene without complaint from directors or members, to protect the residual assets of a community interest company. However, in the light of the broad support in consultation and wider discussions in Parliament, we have rejected the suggestion, as we do not feel that it is necessary or appropriate to provide the Regulator with such a wide discretion to override a CIC's memorandum or articles without a complaint from the directors or members.

4.11 The Government welcomes the emphasis that respondents placed on investor shareholders receiving an amount only up to the paid up value of their shares. The draft Regulations provide that on the winding up of the company, the company buying back its own shares, or a reduction of share capital, the maximum amount that may be returned to members in respect of their shares in the company is limited to the paid up value of the share.

4.12 The Government has considered the argument that all community interest companies should be required to identify in their formation documents an asset-locked body, to which their surplus assets should pass on winding up. On reflection, we believe that this requirement would be too prescriptive. Community interest companies will be able to change the nature of their activities and, over time, the organisation that they identified in the formation documents may become less suitable beneficiaries for a particular purpose. Also, a community interest company may need time to investigate the sector in which it will operate before identifying a suitable organisation to nominate.

4.13 Under the draft regulations, a community interest company may identify, at an appropriate stage, the asset-locked body that it would like to receive any residual assets in the event of winding-up. If a company has not nominated an asset-locked body in its memorandum or articles, its directors and members will have an opportunity to indicate what body or bodies they think would be appropriate recipients of the company's residual assets when they are consulted by the Regulator, who is obliged to consult them to the extent he considers practicable and appropriate.

4.14 The Government has also considered the views on who can appeal against the Regulator's directions on where to distribute assets or to disallow a distribution. We have decided that both the directors and the members of a community interest company should have a right of appeal against the Regulator's directions. The Regulator is directed to consult members and directors when he makes any decision under regulation 23 (unless he considers it impracticable or inappropriate to do so) and so it is consistent to give directors and members equal rights of challenge in all cases. We have amended the draft Regulations to take account of this change.

5 Dividend bearing shares – Dividend cap

Background

5.1 The March 2003 consultation supported proposals that community interest companies should have the option of structuring themselves as companies limited by shares, with the ability to issue “investor shares” that could pay a capped dividend to investors. Consultation responses highlighted that although offering investor shares was not likely to be an option used by many community interest companies in the short term, it was right to allow community interest companies to do so with a view to a developing market for “patient capital”.

5.2 A variety of views were expressed in the 2003 consultation on how a cap on the amount of dividend paid should be set. The Government stated its intention to set a “dividend cap” in regulations noting the need to strike a balance between maximising potential access to finance and maintaining the integrity of the asset lock.

5.3 The October 2004 draft regulations set out a single cap on dividends that would impose a limit on the amount paid out per share per year in percentage terms. For instance if a the “dividend cap” was 10% in a given year and each share had a paid up value of £1 then the maximum that could be paid out a year would be 10p per share. It was proposed that the Regulator would set the “dividend cap” after consultation with the social enterprise sector.

The Government’s intentions and amendments

5.4 In revising the draft regulations we have thought further about the “dividend cap” for community interest companies which choose to issue dividend-bearing shares. We believe the capping mechanism could be improved so as to safeguard community interest company assets and to align the interests of those who hold such shares more effectively with the interests of other stakeholders in CICs.

5.6 If the “dividend cap” is based solely on the paid up value of the shares to which it applies, community interest companies which make only small amounts of profit, but have issued a significant number of shares, could pay out all or most of their profits to shareholders. A simple example of this is included at Annex C. This would not be in the community interest and could cause significant harm to the community interest company brand.

5.7 We have therefore revised the draft Regulations so that as well as there being a limit on the amount of dividend that can be paid out on each share, there is also an “aggregate dividend cap” which limits the proportion of a community interest company’s distributable profits that can be paid in dividends in a given year.

5.8 This will ensure that private investors in CICs do not receive an excessive rate of return, and that whenever a CIC has distributable profits, a substantial proportion of those profits is either re-invested in the business or used in some other way for the benefit of the community, rather than being distributed in the form of dividends to private investors. In order to maximise the proportion of CIC profits which are used for the benefit of the community, dividends paid to asset-locked bodies such as charities will be exempted from the capping rules.

5.9 The Government has also decided that it is appropriate for the Regulations to set the initial levels of the ‘double dividend caps’ on the basis of the limited available information about the current cost of finance for organisations similar to CICs. The Government believes the level of the caps should be known well before the first CICs are established, so that their founders may make informed decisions about whether to use the option of dividend-bearing shares or performance-related debt. It may well be that, once there are significant numbers of CICs operating, there will be evidence to support changes in the general levels of the caps or for specific classes of CICs. The Regulations allow Regulator to review the caps and to change the levels after consulting with the sector and with the approval of the Secretary of State.

5.10 The return on shares will initially be capped (the ‘share dividend cap’) at Bank of England base lending rate plus 5%. This figure reflects the findings of the Bank of England report on the Financing of Social Enterprises which suggested that banks typically charge 2-4% over base rate for loans and overdrafts to social enterprises. The figure of 5% over base rate allows a small premium for the additional risk of equity compared to loans.

5.11 If a company is not able to (or decides not to) pay a dividend at all, or decides to pay less than the maximum dividend per share permitted under the share dividend cap in a particular year, it will be permitted to roll the resulting “unused dividend capacity” forward for up to five years, enabling it to pay more than the maximum dividend per share in respect of a subsequent financial year, so long as it can do so without breaching the aggregate dividend cap.

5.12 The proportion of distributable profits which may be paid out as dividends (‘aggregate dividend cap’) will be capped at 35% in any financial year (with no carry forward of unused capacity), so that each year as a minimum around two-thirds of profits are either ploughed back into the company or used for the benefit of the community. Worked examples of the ‘double dividend cap’ set at these levels are provided in Annex D.

5.13 As noted above, distributions of profits to asset-locked bodies such as charities are exempted from these restrictions.

6 Dividend bearing shares - Possible “index linking” of shares to adjust their value for inflation in a solvent winding-up

Background

6.1 The consultation (Question 3a & 3b) asked whether regulations should allow ‘investor shares’ to be “index linked” such that, in the event of a solvent winding-up, the value of the share could be adjusted to compensate for the effect of inflation. Some respondents to the 2003 consultation argued that allowing “index-linking” might help to make community interest company shares more attractive to investors.

Consultation response

6.2 There were 11 responses on this question with three in favour of index linking, two against and six not expressing a clear preference. Those against index linking argued that even this limited provision to maintain the real value of investment was contrary to the community interest. Those in favour did not offer any further reasons for that opinion but presumably supported the argument in the consultation document that this could help to encourage investment.

6.3 Of those that were unsure, three responses from large representative organisations noted that, although attractive in theory, index linking would be difficult to achieve in practice. One of these responses raised serious concerns, including the possibility that in periods of high inflation index linking could create a perverse incentive to wind up a solvent community interest company. They also argued that index linking would of necessity create capital gains tax complications for any CIC that chose to use it.

6.4 Six respondents offered a view on how the index-linking mechanism should work if allowed. Two responses made reference to the index following the RPI, two commented it should be left to the Regulator’s discretion to set an index and one suggested that an index linked to general share prices should be considered.

The Government’s intentions and amendments

6.5 The Government has consulted a panel of social enterprise sector finance experts and they concluded that index linking of shares would not create a significant additional incentive for investment in community interest company shares. They also pointed to further complications that would need to be dealt with, for example whether index-linking would apply if a community interest company bought back its own shares, and whether a community interest company would be expected to make provision in its reserves for the index-linking.

6.6 In the light of this, and additionally noting the disadvantages raised in the consultation, the Government has decided that regulations should not make provision to allow index linking of community interest company shares.

7 Dividend bearing shares - Restricting the ability of investor shareholders to control community interest companies

Background

7.1 The consultation document (Question 4a & 4b) asked whether the approach taken by draft regulations was appropriate to restrict investor control of community interest companies.

7.2 The draft Regulations drew a distinction between “investor shares” (those whose holders were entitled to receive dividend payments if the company declared a dividend) and “non-profit” shares held by “ordinary members” (who would not be entitled to receive dividends).

7.3 The draft Regulations provided that business could not be conducted at a CIC’s general meetings (i.e. AGM or EGM) unless the number of non-profit share votes that could be exercised was more than three times the number of investor share votes. This attempted to capture the Government’s stated intention (in the October 2003 consultation response) to limit the voting rights of investor shareholders to less than 25% of the total.

7.4 This approach was adopted after the Law Society had commented on a previous version of the regulations published in draft in February 2004. That version would have restricted investor shareholders to no more than 24% of the total votes in a community interest company. The Law Society suggested that this would not be workable when there were circumstances such as a death or sudden bankruptcy among non-investor shareholders making it impossible to achieve the 75% “non-profit” shares quorum at a meeting.

Consultation response

7.5 There were ten responses on this question with five in agreement with the proposed approach, four disagreeing and one unsure. Those in agreement with the suggested approach were largely satisfied that the proposal would leave control with non-profit shareholders and prevent investors running the company for short-term gain.

7.6 Those who disagreed did so for different reasons. Several responses noted the proposed controls could prevent the effective running of the community interest company. Meetings may be inquorate because the necessary numbers of non-profit shareholders do not attend. The proposal would also effectively prevent certain types of employee-owned organisations from becoming community interest companies, which would not be in line with policy intentions.

7.7 Two respondents argued that investor controls would create a disincentive for investment in community interest companies. One also argued that those

with a financial stake in a community interest company might well contribute useful and necessary business judgement. Additionally we received informal comments suggesting that in practice the proposed controls on investors could probably be circumvented. We believe that these criticisms would also be valid of the investor controls set out in the February 2004 draft regulations.

The Government's intentions and amendments

7.8 Having considered the comments received the Government has concluded that investor controls of the kind envisaged could not be guaranteed to be effective and could be counter-productive. However, we believe the new 'double dividend cap' obviates the need for restrictions to prevent investors from seeking to run companies for short-term gain. The 'double dividend cap' constrains the use of profits in such a way that investor control cannot lead to excessive payments being made to shareholders through dividends.

7.9 The decision to issue dividend-bearing shares is one for each community interest company to consider. Community interest companies will not have to issue dividend-bearing shares and may constitute themselves as companies limited by guarantee to make it clear beyond doubt that they will not do so. Those that do choose to issue such shares may, if they wish, impose restrictions on them in their constitutions as some existing social enterprise companies have done when making share offers.

7.10 Moreover, it may be appropriate for investor shareholders to have considerable control over a community interest company, particularly when stakeholders are investors, e.g. local residents owning shares in a community interest company providing services in their area.

7.11 These are matters for the members of each CIC to decide for themselves within the broad framework set by the legislation: a "one size fits all" approach in this area would be inappropriate and could be counter-productive in some cases. The Government therefore does not now intend to impose restrictions on the voting rights of investors.

8 The appeal procedures

Background

8.1 The consultation (Question 5) asked for comments on appeal procedures, including the time limits and procedures set out in the draft regulations. The regulations aim to allow the Appeal Officer flexibility to conduct the appeals in what he considers to be the most appropriate way.

Responses

8.2 The Government received 3 responses commenting on this question.

8.3 One respondent expressed support for the appeals process set out in draft regulations and emphasised that it is appropriate and fair.

8.4 Another respondent asked the Government to note the need for the appeals process to be clear and accessible for employees and employee shareholders, who may be disadvantaged.

8.5 A respondent also suggested that the time limit for lodging appeals against the Regulator's directions on a community interest company's residual assets on a solvent winding-up should be increased from two to three weeks arguing that two weeks might not allow sufficient time to compile and collate the necessary documents, particularly in situations where the appeal might require legal advice and/or mutual consultation between appellants.

The Government's intentions

8.6 The Government has noted the need for the appeals procedure to be clear and accessible. We do not believe that the regulations are an appropriate place to do this but will ensure that it is reflected in the practical arrangements for hearing cases.

8.7 The Government has considered the reasons for allowing an increased time limit of three weeks for appeals against the Regulator's directions on a community interest company's residual assets on a solvent winding-up and on consideration is happy to accept this. Increasing the time limit for appeals to three weeks on receipt of notice of the Regulator's direction will allow interested parties an additional week to consider the Regulator's direction, and to compose and send a notice of appeal to the Regulator. The increased time limit will still allow the Regulator to distribute the assets within a reasonable time frame. Regulations have been amended to reflect this.

9 Further amendments to Regulations

Performance related loans - cap

9.1 The draft Regulations published with the consultation in October 2004 set out that performance related loans, debt and debentures with “equity-like” characteristics, because the rate of interest payable varies with the company’s financial performance, should be subject to a cap on the return they can provide. The Government now intends to set this cap in regulations with the Regulator able to review and make changes with the Secretary of State’s approval.

9.2 The return on performance-related loans should be capped at base rate plus 4%. This figure reflects the finding in the Bank of England report on the Financing of Social Enterprises that banks typically charge 2-4% over base rate for loans and overdrafts to organisations similar to CICs.

9.3 There is no cap on the interest rate for ordinary debt where interest payable is not linked to a CIC’s performance and CICs may borrow through the market in the usual way. However, the Regulator will be able to intervene if a CIC pays an excessive rate of interest that circumvents the asset lock.

The Community Interest Statement

9.4 The Government has reflected further on, and discussed with the Regulator designate, what should be required in the Community Interest Statement sent on application to become a community interest statement. In the October 2004 draft, the statement required only a general declaration that the organisation would carry on its activities for the benefit of the community.

9.5 We have concluded the statement should also include information on how the company’s activities will benefit the community. This will provide the Regulator with more information when taking the decision on whether an organisation passes the community interest test in the first instance.

9.6 This will not restrict the ability of community interest companies to be flexible in their activities. However, they should be aware that it may be appropriate to conduct a dialogue with the Regulator if they intend to change their activities in a way that does not have an obvious benefit for the community. The Regulator is expected to publish a template community interest statement as part of the package of guidance for community interest companies.

Fees

9.7 As indicated by DTI Ministers, and in the consultation document, fees for community interest companies are additional to those charged by the registrar for

incorporation and on filing of the annual return. The fees specific to community interest companies are set in regulations as follows:

- £15 on application to become a community interest company;
- £15 on application by an existing company to transfer to be a community interest company;
- £15 on filing of the Community Interest Company Report.

General redrafting to ensure clarity

9.8 The Government has reorganised or redrafting particular provisions so as to make the Regulations easier to understand and/or a clearer expression of the Government's established policies on CICs. This intention underlies changes relating to political activities and the definition of a "section of the community".

Consequential amendments

9.9 These amendments relate to the changes already covered in sections 3-8. These include expanding the provisions on the contents of the community interest report to take account of the details of the new dividend capping rules, or tweaking the provisions on appointment of directors to take account of the removal of any distinction between "investor" and "ordinary" shareholders.

10 Next steps

The Government has laid the Community Interest Company Regulation before Parliament and they will be subject to affirmative resolution. The Government expects, subject to Parliamentary debate, to be able to bring these Regulations into force on 1 July 2005 in order that applications will be accepted by the Regulator's office from that date.

The first Regulator will take up post on 1 April 2005 and his office will be issuing detailed guidance on CICs prior to 1 July.

11 Who to contact

For further information on community interest companies please contact:

The Office of the Regulator of Community Interest Companies
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Companies House
Crown Way
Cardiff
CF14 3UZ
Phone : 02920 380212

Web address - www.dti.gov.uk/cics

ANNEX A: CONSULTATION QUESTIONS

Question 1 - Draft regulation 4, paragraph (e) aims to allow organisations conducting their activities for the benefit of their members but not solely for private gain to become community interest companies. Do you think that the draft regulation achieves this aim in an appropriate way? Please provide reasons for your view if you think it does not.

Question 2 - Does draft regulation 21 allow an appropriate level of intervention by the Regulator to protect the residual assets of a community interest company?

Question 3a - Should Regulations allow “index linking” of investor shares such that the value of the share (applicable on winding up of a community interest company) would be adjusted to reflect the equivalent loss of the original value of the investment due to inflation?

Question 3b - If so, how should such an “index linking” mechanism work?

Question 4a – The Government is committed to restricting the ability of investor shareholders to control community interest companies which issue investor shares. Do you think that the draft Regulations (and in particular paragraphs 5 and 6 of Schedule 3 to the draft Regulations) will achieve this objective in an appropriate way?

Question 4b - If not, how do you think the draft Regulations should be changed so as to limit investor shareholder power in a more appropriate way?

Question 5 - Do you have any comments on the procedures set out in draft regulations 33 to 38 on the conduct of appeals to the Appeal Officer from decisions of the Regulator of Community Interest Companies?

ANNEX B: LIST OF CONSULTATION RESPONSES

Name	Description
National Housing Federation	Representative Organisation
Bates, Wells & Braithwaite	Other – law firm
Institute of Chartered Secretaries & Administrators	Representative Organisation
Association of Chartered Certified Accountants	Representative Organisation
Green Pastures Partnership	Social Enterprise
National Council for Voluntary Organisations	Representative Organisation
Social Enterprise Coalition	Representative Organisation
cdfa	Representative Organisation
Eaga Partnership Ltd	Social Enterprise
Royal National Institute of the Blind	Other – voluntary sector
Triodos Bank	Other – finance sector
Insolvency service	Central Government

ANNEX C: WORKED EXAMPLE OF OLD DIVIDEND CAP CALCULATION (SINGLE CAP ONLY RELATING TO PAID UP VALUE OF SHARE)

Facts

A CIC has a number of shareholders, all of them individuals who have invested in the company in order to acquire shares. The size of the different shareholders' holdings varies, but between them, they hold 15,000 shares.

Each share has a paid up value of £1, and all the shareholders are entitled to receive a dividend, in proportion to the number of shares they hold, when a dividend is declared.

The company's shares were all issued would only be subject to the statutory share dividend cap of 9.75% (Year 1).

In Year 1, the CIC makes distributable profits of £1,500.

Calculation

The maximum dividend per share is the applicable share dividend cap multiplied by the paid up value of each share.

The applicable share dividend cap is the share dividend cap in force at the beginning of the first day of Year 1, which was 9.75 per cent. The paid up value of each share is £1.

The maximum dividend per share is therefore £1 x 9.75 per cent, or 9.75 pence. Given a total of 15,000 shares in issue, a dividend paid at this rate would result in an aggregate dividend (i.e. the total dividend to all shareholders) of £1462.50 (i.e. 15,000 x 9.75 pence).

This would leave only £37.50 to be reinvested in the company or used for the community benefit. If the company's distributable profit remained at this level profits could be absorbed by shareholders in this way over a long period of time.

ANNEX D: WORKED EXAMPLE OF NEW 'DOUBLE DIVIDEND CAP' CALCULATION

Example 1

Facts

A CIC has a number of shareholders, all of them individuals who have invested in the company in order to acquire shares. The size of the different shareholders' holdings varies, but between them, they hold 1,000 shares.

Each share has a paid up value of £5, and all the shareholders are entitled to receive a dividend, in proportion to the number of shares they hold, when a dividend is declared.

The company's shares were all issued when the statutory share dividend cap was Bank of England base lending rate plus 5 per cent, and on the first day of the CIC's first financial year (Year 1), Bank of England base lending rate was 4.5 per cent.

In Year 1, the CIC makes distributable profits of £12,000. On the first day of Year 1, the statutory aggregate dividend cap was 35 per cent.

Calculation

The maximum dividend per share is the applicable share dividend cap multiplied by the paid up value of each share.

The applicable share dividend cap is the statutory share dividend cap in force at the beginning of the first day of Year 1, which was 9.5 per cent (i.e. 4.5 per cent + 5 per cent). The paid up value of each share is £5.

The maximum dividend per share is therefore £5 x 9.5 per cent, or 47.5 pence. Given a total of 1,000 shares in issue, a dividend paid at this rate would result in an aggregate dividend (i.e. the total dividend to all shareholders) of £475 (i.e. 1,000 x 47.5 pence).

This is well within the maximum aggregate dividend of £4,200 (i.e. £12,000 x 35 per cent).

The £475 can therefore be distributed among the shareholders by way of dividend according to the number of shares which each of them holds if the directors decide to recommend such a dividend and the shareholders approve their recommendation.