



## Guidance

# Industrial and provident societies

This document sets out the Charity Commission's ('the Commission's') position in relation to Industrial and Provident Societies and the payment of interest on share capital.

Industrial and Provident Societies (IPSs) are registered with the Financial Services Authority (FSA). Currently, those that are charities are **'exempt' charities**. They cannot register with the Charity Commission, but are otherwise subject to charity law. HMRC decides whether they are eligible for tax relief as charities.

The Charities Act 2006 will require all exempt charities either to have a principal regulator to oversee their compliance with charity law, or (where there is no suitable body to act as principal regulator) to lose their exempt status and be regulated by the Commission. It is unclear how charitable IPSs will be regulated in future; the Government has not yet made a decision about this.

Some IPSs are set up as co-operatives, which cannot be charities, but others are set up as community benefit societies, which can be charities in certain circumstances. The activities of charitable IPSs include such things as redevelopment, regeneration and housing projects.

Some IPSs for the benefit of the community receive tax benefits as charities but have the power to pay interest on share capital. While the rules of industrial and provident societies often make a distinction between interest and dividends, they also indicate in many cases that the payment of interest is out of profits and so is clearly a distribution of profits.

The Commission considers that a power to distribute profits is fundamentally incompatible with charitable status. This is because a power of a corporate body to apply its property and assets for the purpose of making profits and devoting the resulting profit to the distribution of dividends among the members is considered by the courts to be incompatible with charitable status.

We have looked at the legal framework in this area and discussed it with the FSA and HMRC. We are now satisfied that there are circumstances in which limited payments of interest may be made, which would not amount to a distribution of profits.

The Commission's position is that a power of a community benefit society to pay interest on shares is not incompatible with charitable status, provided that the following features are required by the society's rules:

1. The interest rate is set at a level which is not in itself a motivation to buy shares and which the charity trustees can justify as being in the interests of the charity by reference to available commercial rates for borrowing.
2. The cost is part of the society's revenue expenses and met before the surplus is determined.

3. The rates are declared in advance of the period for which they will become payable, just as for a bank or building society account, and never retrospectively.
4. There is a power to suspend interest payments in the interests of the society.
5. There is a power of the society to withhold repayment of the shares, either temporarily or indefinitely and to write the value down below the nominal £1.
6. The shareholding does not confer any rights to the underlying assets of the society.
7. In the event of a solvent dissolution, shareholders can not be paid more than the nominal value of their shares.

The Commission will continue to discuss the issue with the FSA, HMRC, DCLG and representatives of other Government departments and organisations affected.