

Charitable Incorporated Organisations

Should your church become a CIO?

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The information in this booklet reflects Edward Connor Solicitors' understanding as at February 2020. It is produced for the purpose of knowledge sharing and does not constitute legal advice.

If your church currently operates through an unincorporated structure such as a charitable trust or as a charitable unincorporated association, you should consider switching to a CIO. This booklet takes you through the benefits of becoming a CIO, how Edward Connor Solicitors can help you and what you need to consider in the process. Let's start with the advantages of becoming a CIO:

1. Liability

The first advantage relates to liability of church officers and members for the actions of the church.

Charitable trusts and unincorporated associations are not regarded as a single legal entity and so they need legal persons to do things on their behalf such as entering into contracts with employees or building contractors. These are known as the "charity trustees." In a church context it is normally the elders or the elders and deacons together who fulfil the role of charity trustees.

When church officers within unincorporated churches sign contracts on behalf of the church, it is the individuals signing the contracts who are personally liable to fulfil the obligations of those contracts. The other church officers (and possibly the church members if they have approved the officers' decision) may also be held to be personally liable. If the church is unable to fulfil its contractual obligations from the assets held by the church, the personal assets of church officers (and church members) are at risk and it is unlikely that insurance will cover contractual obligations.

By contrast, when the church officers of a CIO sign a contract in the name of the church, neither the church officers nor the members are personally liable under the contract; it is the CIO alone that is liable and so only the assets of the CIO are at risk. In cases where a CIO has suffered losses because the charity trustees have breached their duty of care, the charity trustees may be required to reimburse the charity from their own personal assets for any losses suffered (as is the case with unincorporated structures). However, the charity trustees are only required to reimburse the CIO for losses it suffers; they are not required to pay the full amount of the debts owed to third parties by the CIO.

The benefit of limited liability for CIOs covers not only contractual obligations, but also negligence liabilities, e.g. personal injury claims connected with events on church premises. Where a church is operating through an unincorporated structure all the charity trustees will be held personally liable for the actions of the church, and in some cases the whole church membership may also be personally liable.

This means that in the event of a claim for actions (or inaction) carried out by the church, a claimant can simply bring their claim against the most wealthy church leader or member if the collective assets of the church are insufficient to meet the claim. Church insurance policies are available, but these may not cover all liabilities. However, where a church is operating as a CIO, only the CIO itself can be sued for the actions of the CIO in most cases.

Individuals who act carelessly could still be sued, but their own actions would not make the other church officers or members personally liable, which contrasts with the situation for unincorporated structures.

2. Property ownership

The second advantage concerns property ownership. As a legal person, a CIO can own and lease property in its own name.

A church does not have this ability if it operates through an unincorporated structure, but will need to use property holding trustees to hold property in their names on behalf of the church.

A church operating as a charitable trust or unincorporated association can use individual people as holding trustees, in which case a minimum of two holding trustees is required, or it can use a trust corporation as a sole holding trustee.

If the church uses individual holding trustees, the church will need to go through a conveyancing process every time those individuals need to be changed, e.g. when the

original individuals leave the church or want to retire. Failure to do this can lead to situations where the church has holding trustees in other parts of the country who no longer have any contact with the church.

If the property is held by a trust corporation, the church will need to consult with the trust corporation whenever it wants to enter into a mortgage, grant a lease or sell the property. The requirement to consult with the trust corporation can cause delays because the trust corporation is not part of the church and will need to take time to familiarise itself with the matter.

None of these complexities arise if the church operates as a CIO. The property is simply held in the name of the CIO. There is no need to go through a conveyancing process on the appointment and resignation of the charity trustees who run the CIO and there is no need to involve an external trust corporation.

3. Registered charity number

Another key feature of CIOs is that they are all registered at the Charity Commission regardless of their annual income. Therefore every church operating as a CIO will have its own charity number.

Currently, some churches that do not operate as CIOs are unable to register with the Charity Commission and obtain their own charity number because of the Charities (Exception from Registration) Regulations 1996. These regulations prevent churches from registering with the Charity Commission if their annual income is less than £100,000. Churches in this position are known as “excepted charities”. Excepted charities are fully regulated by the Charity Commission but they are excepted from the requirement to register with the Charity Commission and the Commission does not allow voluntary registration.

Legally, excepted charities are entitled to all the benefits of charities that are registered at the Charity Commission. However, in practice, not having a registered charity number can sometimes cause problems, because people are unaware of excepted status.

Although these problems can usually be overcome, they can still cause difficulties that would be avoided by the church having its own registered charity number.

Excepted status for churches is currently due to end in March 2021, meaning that all excepted churches with an annual income of more than £5,000 would be required to register with the Commission. However it is possible that this deadline will be extended beyond 2021. If that is the case, then the only way for an excepted church, with an annual income of less than £100,000, to have a registered charity number is by setting up as a CIO

For churches that are already registered charities, you need to be aware that setting up a CIO will involve being given a new charity number. Therefore, once the CIO has been set up you will need to prepare amended stationery including issuing new Gift Aid forms.

4. Church name

When an existing church is setting up a CIO it has the freedom to retain its existing name or to adopt a new name, provided that the proposed name is not the same as the name of another charity.

CIOs have to state their registered names in all the locations, communications and documents in which a registered company has to state its name. If the CIO does not have "CIO" or "Charitable Incorporated Organisation" in its name, it needs to mention that it is a CIO.

5. Long term benefits vs short term costs

The long term advantages of limited liability and property ownership associated with CIOs need to be weighed against the short term costs and time required to set up a CIO.

There is no automatic process for a church currently operating as an unincorporated association or under a trust to convert to a CIO. Becoming a CIO involves setting up a new charity and then transferring all of the assets, liabilities and people from the existing charity to the new CIO.

The amount of work required to achieve this will vary greatly depending on the circumstances of your church, but a general overview of the steps required is set out in Appendix on page 17.

A note of the costs of setting up a CIO using Edward Connor Solicitors is available on page 11. An established church seeking to become a CIO should be able to go through the whole process in between six to eighteen months. For church plants, a typical timescale would be three to eight months.

6. Other incorporated structures

Churches can operate under other incorporated charitable structures that would also give the advantages of limited liability and property ownership. The most obvious alternative is a company limited by guarantee ("CLG"). The main drawback of using a CLG rather than a CIO is that a CLG is regulated both by Companies House and the Charity Commission and the company has an obligation to make annual returns to both organisations. There are also additional legal requirements under company law, such as in relation to company membership.

There may be cost savings in converting to a CIO for CLGs with an annual income of less than £250,000. This is because a CIO with annual income below this amount can prepare accounts on the basis of the receipts and payments method whereas all companies must use the accruals method and churches may find that the costs of having an independent examination are cheaper if the accounts are prepared on the basis of receipts and payments rather than accruals. You should take advice from an accountant if this is something you are considering to make sure that the receipts and payments method is appropriate for your church.

If a church is currently operating under an unincorporated structure, a CIO is likely to be a better option for the church than a CLG. In January 2018, a new regulatory regime came into force allowing charitable companies to convert directly to CIO status, retaining their existing charity number and bank accounts. Direct conversion is relatively quick and, therefore, is likely to make sense for most churches operating as a CLG (although there may be issues for churches which have charges registered over their assets).

7. Unfamiliarity with incorporated structures

The language associated with CIOs may seem alien to many Christians who are more familiar with the unincorporated structures, but churches should not be put off by this.

For churches that are happy to operate as charities, there is no theological reason we are aware of why an unincorporated structure should be preferred to an incorporated structure such as a CIO. The traditional structures of trusts and unincorporated associations are simply reproduced when a church becomes a CIO but with the added benefits of limited liability and the capacity to hold property in the church's own name.

8. Which type of CIO is right for you?

If you would like your church to operate as a CIO, you need to consider which type of CIO is right for you. In every CIO, whether a church or other type of charity, there are two sets of decision makers:

1. The members of the CIO (not to be confused with church members) - responsible for decisions such as amending the constitution and winding up of the CIO; and
2. The trustees of the CIO - responsible for the general control and management of the CIO.

The Charity Commission has created two different types of CIO which vary according to who the CIO members are:

Foundation CIOs

Under this type of CIO, the members of the CIO and the charity trustees are the same group of people, making the charity trustees the ones responsible for making all key decisions.

Association CIOs

This type of CIO has a wider membership, with some CIO members who are not trustees.

Using these two forms, we have developed a number of different model CIO constitutions for churches operating as CIOs to fit different church governance structures. In order to establish which model would be right for you, consider which of the following forms of church governance (CG) you operate:

CG1

With this form of church governance, the church members have formal voting rights that extend beyond the appointment and removal of church leaders/trustees and approving changes to the constitution. The extent of matters on which church members can vote will vary from church to church.

This is an Association CIO - the church members will be the members of the CIO.

CG2

Under this model of church governance, church members' formal voting rights are limited to the appointment and removal of church leaders and approving changes to the constitution. Church members may be consulted on other issues, but not as a formal vote.

This is an Association CIO - the church members will be the members of the CIO .

CG3

Under this form of church governance, new leaders are appointed by the existing leaders. The congregation may be consulted in this process but their formal approval is not required. All decisions are made by the church leaders. Under this form of church governance there may not be any formal membership system at all.

This is a Foundation CIO - the members of the CIO are the trustees and church membership is distinct from CIO membership.

Statement of Faith

The objects of the CIO will generally refer to "the advancement of the Christian faith in accordance with the Basis of Faith set out in Schedule 1". Some churches may decide to adopt the Basis of Faith of their umbrella organisation or denomination in full, others may have developed their own Basis of Faith which they would like to continue to use. Some churches may prefer to keep their Basis of Faith relatively simple, and use other statements which are set out in their Church Handbook (commonly known as Doctrinal Distinctives or Ethical Statements) to give greater detail and explanation as to the church's beliefs. It is a matter for each individual church as to what their Basis of Faith

should include and we are happy to discuss this further with you, in particular the protections which certain statements can provide in relation to equality legislation.

9. Next Steps

Having decided which type of CIO you want to set up, one further question is whether to close down your current charity once everything has been transferred to the CIO or whether to retain it for legacy purposes - this does not apply to church plants because in these cases there is no existing charity.

There is currently a gap in the law so that, in some cases, legacies made to the original charity will fail if it does not still exist on the death of the donor, even if the merger of the original charity with the CIO has been registered with the Charity Commission.

Churches that receive significant funding through legacies would be well advised to retain their original charity in existence to receive legacies after the CIO has been established. However, most churches do not receive significant funding through legacies. Therefore, in many cases, the best course of action will be to close down the existing charity and then make an announcement advising that people who have made legacies to the church should consult their advisor to ensure that the will has been drafted so that the legacy will go the CIO.

10. Support from Edward Connor Solicitors

We love to work with churches and we are expert at helping them set up as a CIO. We can provide all the following services:

- 1. Preparation of the necessary legal documents for forming the new CIO.** This will be based on drafts which have been approved by the Charity Commission although it is never possible to absolutely guarantee the Charity Commission will register a charity as they deal with them on a case by case basis.
- 2. Advice and help with transferring assets from the existing charity to the new CIO.** Depending on circumstances this may not need legal help but in other circumstances help is crucial. These issues are covered further in this information sheet and an additional cost

will be payable if assistance from solicitors is required.

- 3. Completion of the detailed Charity Commission application form.
- 4. Handling of all correspondence with the Commission up to registration.

11. How much will it cost?

We work hard to make specialist legal advice accessible to churches. Each church is different and we provide a bespoke service to ensure that the needs of your particular situation are addressed. We have broken down the CIO process below and provided an estimate of the costs involved for each part. We endeavour to work within these estimates wherever we can, and will keep you updated on the costs as we go through the process.

Establishing the CIO

For existing charities, this includes advising you on the process of conversion and the legal parameters set out in your existing constitutional documents. This is an important part of the process, because your current structure may have significant implications for how the CIO documents are drafted and how the subsequent transfer of assets is dealt with.

For all charities, this includes reviewing your application form and associated documents, drafting an appropriate constitution (and church handbook, if required), and preparing the application for submission to the Charity Commission.

The costs are likely to be as follows (all costs ex VAT):

	Non-church charity	Discounted church	Discounted FIEC
New church/charity	£1,400	£1,120	£1,050
Existing church/ charity	£1,800	£1,440	£1,350

We will ask for an initial amount of money on account of costs, for reviewing the application and associated documents, and advising you on the process of conversion. We will let you know the amount in our formal letter of engagement, but for existing churches it is likely to be around £720 plus VAT. For new churches it will be £150 plus VAT. These amounts will be used against our initial invoice (in other words, they are a down-payment

against the costs set out above).

Transfer of Assets

For existing churches, there may then be additional costs in relation to the transfer of staff, assets and property from the current entity to the new CIO. This includes applying to the Charity Commission for consent to the transfer, which will be required where the majority of the existing trustees will be appointed as trustees of the CIO. This also includes advising you on the process throughout, including on the closure of the existing charity if applicable.

As a broad estimate these costs are likely to be as follows (all costs ex VAT):

	Non-church charity rates	Discounted church rates	Discounted FIEC rates
Transfer of staff and assets other than property	£900	£720	£675
Transfer of registered freehold property (per property)	£800	£640	£600
Transfer of registered leasehold property (per property)	£1,200	£960	£900
First registration of properties not yet registered at the Land Registry	£1,650 - £2,700	£1,320 - £2,160	£1,240 - £2,025

There are some situations which may trigger extra costs. Here's a list of possible circumstances where extra costs may be incurred:

- If your existing constitutional documents need amending to make the transfer process work—sometimes an application to the Charity Commission will also be needed
- Major contracts with third parties for goods or services which need a formal novation agreement
- Costs and fees payable to third parties (such as Land Registry Fees)
- If there is a mortgage on the property and, for example, the mortgage lender requires the church to enter into a new mortgage

- If the property is held by a separate trust-holding company, or by individual trustees, and they take independent advice, there may be additional costs in liaising with those separate advisers. Our cost estimate assumes that any separate property trustees are broadly in agreement with the decision to convert to a CIO and the instructions of the church's managing trustees
- If the original title deeds for the whole of the property concerned aren't available
- If the church is the tenant of a lease and formal consent/licence from the landlord is required. Often landlords will also ask for their legal costs to be covered, if a formal licence is required. There may also be additional costs in relation to dealing with a management company or a third party that has rights over the property, or addressing any amendments or variation to the lease where it cannot simply be transferred
- If the church is the landlord of the property, we may need to review whether the tenancy can be transferred, or you may need to enter into a new tenancy agreement for the CIO - a model Assured Shorthold Tenancy and guidance notes can be purchased from our website. Again, additional costs would apply if the transfer means that amendments to the current arrangements are required
- If there are third party rights in the property, such as shared equity arrangements, or the property is part-owned by a trustee
- If there are occupational pension schemes that would trigger liabilities for the church (employee pensions such as those arranged under auto-enrolment obligations would not apply here).

12. What else do we need to consider?

Current Legal Structure

1. *Do your existing governing documents prevent you from setting up a CIO or place restrictions on the type of CIO that you are able to set up?*

This is only likely to be an issue if the church building is held under a property trust that is prescriptive about how the church meeting within the building has to organise itself, and even in those cases, a CIO can usually be set up in a manner that is consistent with the requirements.

2. *How many charities currently exist in connection with the church and who are the trustees?*

Many churches have two or three charities connected to the church, e.g. a property trust covering the church building, a charitable unincorporated association or a working funds trust for the congregation's working funds and a separate manse trust. It is important to identify this at the outset and to know who the trustees are for each charity. Will the CIO take over from all the charities connected to the church or just some of them? Do the trustees of each charity have to follow the wishes of the congregation / church leaders or do the trustees have their own decision-making powers and are they in agreement with the project?

If you are not familiar with your current governing documents, Edward Connor Solicitors can review them and report back to you on these matters. This review and report is included in the cost of setting up a CIO for an established church.

Pension arrangements

3. Is the church part of a multi-employer pension scheme?

Some churches are or have been part of a multi-employer pension scheme. A multi-employer pension scheme is one where a number of different employers contribute towards the same scheme that is administered by a trustee on behalf of all the employers. With this type of scheme, certain events (known as "cessation events") can trigger an obligation on the church to make a payment towards any deficit within the scheme. One of the most common events is ceasing to have any more employees participating in the scheme. A change of legal structure may also be regarded as a cessation event. Therefore, if the church is or has been part of a multi-employer pension scheme, you need to take advice from a pensions lawyer as to how the CIO project will affect the church's liabilities under the scheme.

Mortgages / secured loans

4a) If the church has a mortgage, how much will the lender charge for transferring the loan agreement to the CIO?

If the church has a mortgage, the consent of the lender will be required if you are intending to transfer the land that the mortgage relates to into the ownership of the CIO. Additionally, in some cases the consent of the lender will be required for setting up the CIO at all, and it may be necessary to enter into a new mortgage agreement. It is unlikely a lender would want to prevent the church from setting up a CIO, but the lender may well

make a charge for granting its consent and you need to factor this in to your decision-making on whether the benefits of setting up a CIO will outweigh the costs.

4b) Does the new CIO intend to obtain a mortgage?

CIOs remain relatively new and it may take time explaining the status to other parties such as banks and funders, especially if a CIO needs to borrow funds at an early stage. This potential disadvantage can be pre-empted by starting discussions at an early stage of planning the CIO with potential lenders. Please contact us at the office if you would wish to discuss this further.

Leases

5. If the church has a lease, how much will the landlord charge for transferring the lease to the CIO?

If your church owns its property by way of a lease, you need to check whether the consent of the freeholder is required to transfer the lease to the CIO. It is unlikely that the landlord could completely withhold consent, but the landlord may charge a significant sum for granting consent. You should find out what these costs would be before committing to setting up a CIO.

Providing services on behalf of public bodies

6. If the church carries out services for public bodies, what impact will setting up a CIO have on the contracts?

Some churches carry out services on behalf of public bodies, e.g. running homeless shelters or forms of social care under a contract with the local authority. These services are often carried out under long-term contracts and when the contract comes to an end the church will need to compete against other potential services providers to continue providing the service. There are two key issues here for churches providing these services.

First, if the church becomes a CIO during the current term of a contract, will the public body agree to transfer the contract to the new CIO for the remainder of the term? You would need to liaise with the public body to address this matter.

Second, when the public body retenders the contract and the church submits a bid as a CIO, will the public body take into account experience gained by the church when it operated under a different legal structure or will the change in legal structure lead the local authority to see the church as a brand new entity with no previous experience? Government guidance issued in November 2012 and then revised in 2015 (PPN Action Note 04/15, paragraph 35) indicates that public bodies should take the previous experience into account, but they may not always follow that guidance. Therefore you should check with the public body whether such experience would be considered (referring to the Government guidance).

There may also be implications under equality legislation for how the church delivers its services on behalf of the public body. We can advise you on this separately, if required.

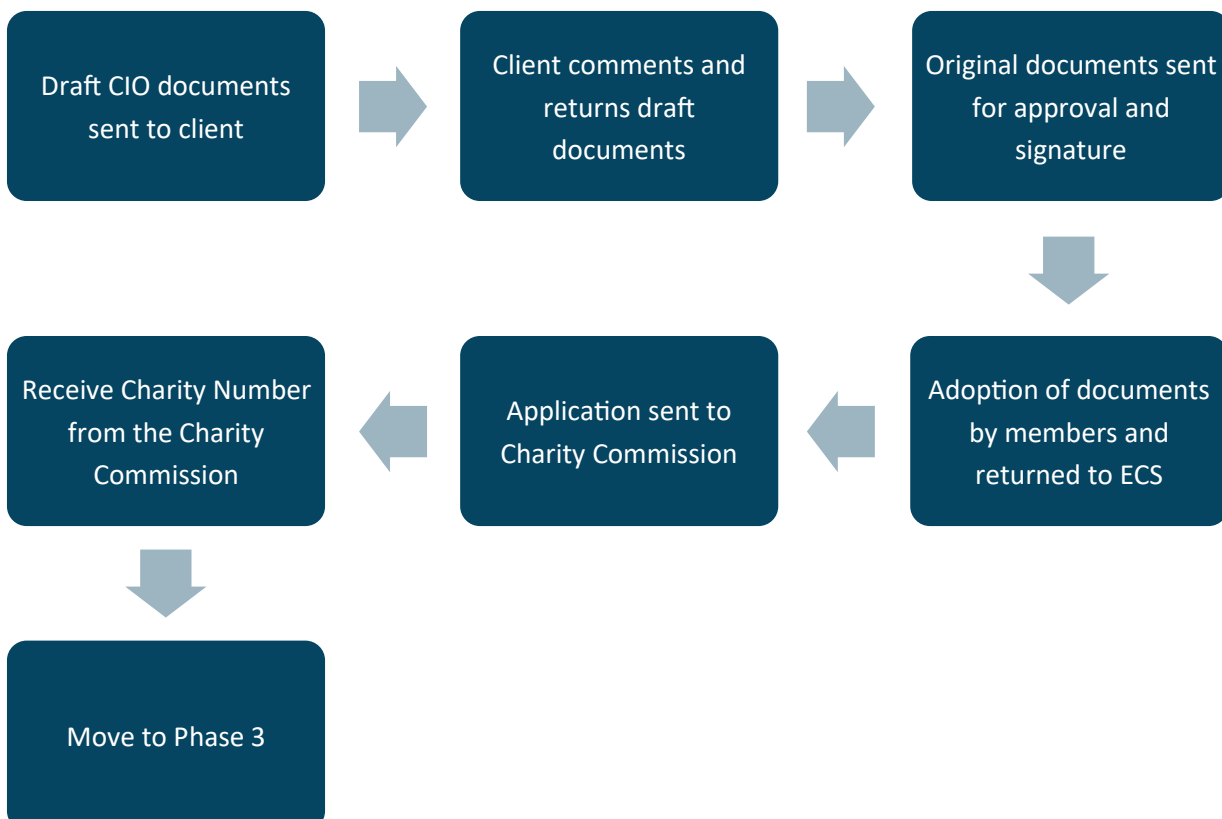
Appendix

The CIO application process with Edward Connor Solicitors (ECS)

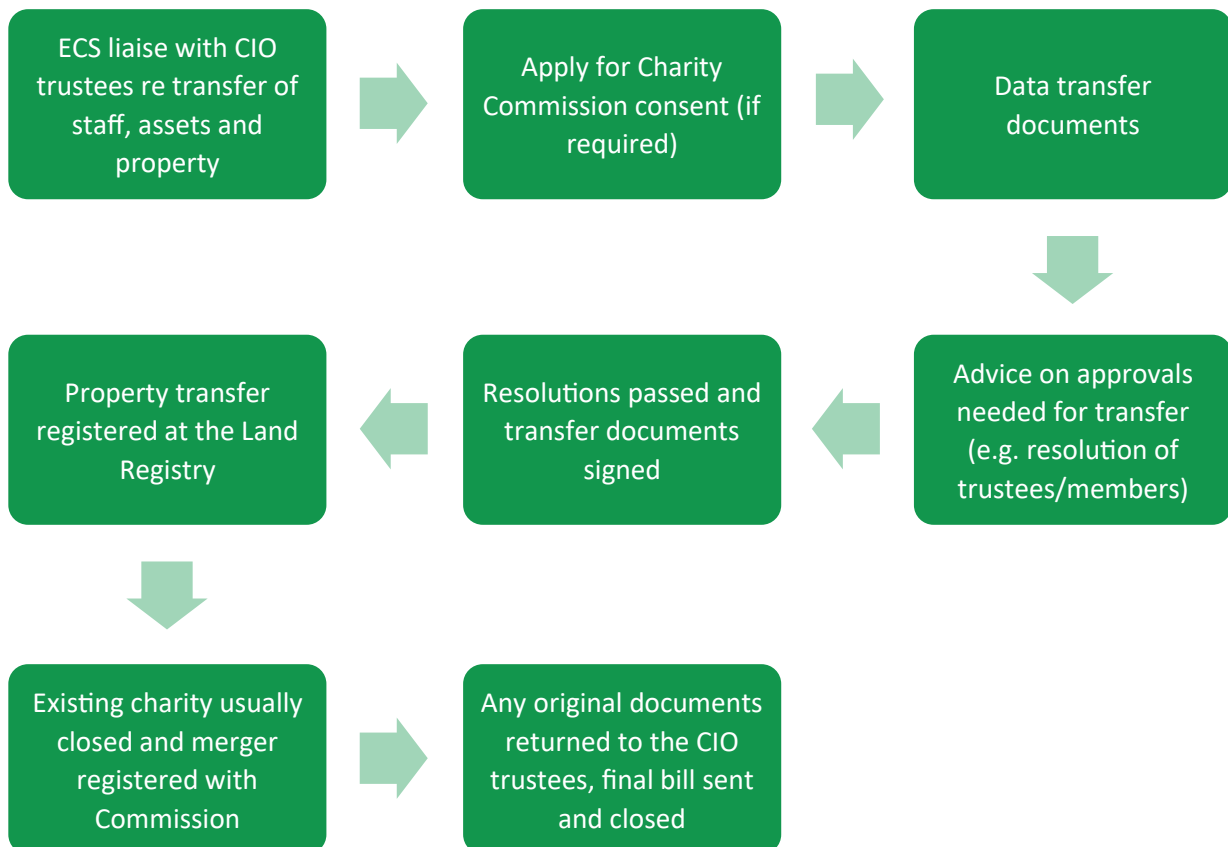
Phase 1 - Gathering information and opening a file



Phase 2 - Setting up CIO



Phase 3 - Transfer of assets to the CIO from the CUA







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