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LEGAL FRAMEWORK ANALYSIS

NATIONAL REPORT: UNITED KINGDOM

ICA-EU PARTNERSHIP

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I. Introduction

The research falls within the scope of the knowledge-building activities undertaken within the partnership for international development signed in 2016 between the European Commission and the International Cooperative Alliance (ICA), which aims to strengthen the cooperative movement and its capacity to promote international development worldwide. It demonstrates that the absence of a supportive legal framework for cooperatives, or the presence of a weak or inadequate legal framework, can negatively impact cooperatives and their evolution. In contrast, the existence of supportive regulations can foster cooperatives' creation and strengthening, acting as a driver of sustainable development. For this reason, further knowledge and evaluation of cooperative legislation will become a tool for ICA members, cooperators worldwide, and other key stakeholders such as policymakers and cooperative legal scholars. With greater knowledge and access to a global, country-based legal framework analysis, ICA members can advance their advocacy and recommendations on the creation or improvement of legal frameworks, document the implementation of cooperative legislation and policies, and monitor their evolution.

The main objectives of the legal framework analysis are to:

-provide general knowledge of the national cooperative legislation and of its main characteristics and contents, with particular regard to those aspects of regulation regarding the identity of cooperatives and its distinction from other types of business organizations, notably the for-profit shareholder corporation (the *sociedad anónima lucrativa* in Spanish; the *société anonyme à but lucratif* in French).

-to evaluate whether the national legislation in place supports or hampers the development of cooperatives, and is therefore "cooperative friendly" or not, and the degree to which it may be considered so, also in comparison to the legislation in force in other countries of the ICA region (or at the supranational level).

-to provide recommendations for eventual renewal of the legal frameworks in place in order to understand what changes in the current legislation would be necessary to improve its degree of "cooperative friendliness", which is to say, to make the legislation more favourable to cooperatives, also in consideration of their specific identity.

This report presents the main results of the research to examine and analyse cooperative law in the United Kingdom, its general context and main elements, including how adequate it may be for cooperatives. Finally, conclusions and recommendations for the improvement of the legal framework are considered.

Sections II – V of this report are based on work by Cliff Mills, who practices as a consultant solicitor with Anthony Collins Solicitors in Birmingham, supported and coordinated by staff from Cooperatives Europe and the ICA. Sections III – V also

incorporate input from Co-operatives UK, the network for the UK's cooperative enterprises and an ICA member.

II. National cooperative law: United Kingdom

i. General Context

This report is concerned with the law of the United Kingdom which comprises England, Wales, Scotland and Northern Ireland. The principal legislation it covers is the Co-operative and Community Benefit Societies Act 2014 (the 2014 Act) which applies in England, Wales and Scotland, but also to those societies in Northern Ireland that choose to record their rules in England.[1]

Scotland is a separate and distinct jurisdiction and has its own legislation for company law. Although most of what follows below applies to Scotland as well, it needs to be borne in mind that in relation to matters outside the 2014 Act, it cannot be assumed that Scotland necessarily follows the law in England and Wales.

The 2014 Act provides for the registration of cooperative and community benefit societies in the UK. However, it is important from a UK perspective to distinguish between registration and regulation. The registrar for cooperative and community benefit societies established under the 2014 Act is the Financial Conduct Authority, and its functions in relation to registered societies are as a ***registrar***, not as a ***regulator***. Cooperatives in the UK are not therefore subject to regulation. This distinction is important, because as its title implies, the Financial Conduct Authority (FCA) is primarily a financial regulator, and its activities as registrar for societies is very much a side-line.

The 2014 Act is the main source of legislation in relation to "registered societies". This term encompasses both cooperative and community benefit societies, the latter being introduced into the legislation in 1939 when proper criteria for the registration of societies were first put in place.[2]

Although there is no regulation of cooperatives (or community benefit societies) as stated above, in relation to those societies registered under the 2014 Act, the registrar not only has a discretion whether to accept a society for registration as a bona fide co-operative or a community benefit society,[3] but there is a continuing obligation for registered societies to continue to meet the relevant criteria for registration thereafter. Where a society ceases to do so, the registrar has the power to suspend, and ultimately to cancel the registration.[4] This is a blunt instrument, but it provides a basis for the registrar to enforce compliance. The basis on which the FCA carries out its functions as registrar are set out in its Guidance which will be referred to further below.[5]

[1] https://www.legislation.gov.uk/ukpga/2014/14/contents
[2] The Prevention of Frauds (Investments) Act 1939
[3] Section 2 of the 2014 Act
[4] Power to suspend – s.8, power to cancel – section 5 of the 2014 Act
[5] https://www.fca.org.uk/publication/finalised-guidance/fg15-12.pdf

The UK does not have a written constitution and therefore there is no place for the higher recognition of cooperatives as a form of business. However a new precedent has been set by legislation in Wales, which is generally more supportive of cooperatives than England (see further below), specifically acknowledging cooperatives and requiring their promotion.[6]

The 2014 Act was a consolidation of previous legislation: the previous latest consolidation had been the Industrial and Provident Societies Act 1965, subsequent to which there had been a number of further Acts in the 1970s, and again in the new millennium. The 2014 Act brought all legislation together into one place.

As well as the 2014 Act, there are the following additional acts of Parliament which have some relevance:

- the Credit Unions Act 1979, which is separate legislation governing credit unions which are not covered by the 2014 Act;
- the Company Directors Disqualification Act 1986, now providing for the disqualification of individuals from acting as a director or officer of a society if guilty of misconduct; and
- the Insolvency Act 1986 which applies in relation to the winding up of societies.

In spite of the history of the cooperative movement and the establishment of the first modern cooperative society in Rochdale in 1844, UK law contains very little substantive legislation specifically relating to cooperatives. It wasn't until the 2014 Act that the word "co-operative" was even included in the title of the legislation.[7]

There is no express reference to the ICA Principles in the 2014 Act. However they become relevant through the registrar's Guidance. This document sets out the registrar's approach to its role as registering authority for societies under the 2014 Act.

In relation to the ICA Principles and how they apply to cooperatives, the registrar states first that: 'We generally consider something to be a bona fide co-operative society where it is *an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise'*. This obviously reflects the ICA definition of a cooperative.

In the Guidance, it then goes on to state that it generally expects: '*to be able to verify and validate whether principles 1 to 4 … have been met through the rules and governance arrangements of a co-operative society, along with the society's statements of intent about how it will operate*'.[8]

It goes on: '*We do not necessarily expect to be able to verify or validate principles 5 to 7 as indicators that the condition for registration is met; however evidence of compliance with those principles would be treated as a positive indicator*'.[9]

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[6] Social Services and Well-being (Wales) Act 2014, under which a local authority must promote the development in its area of co-operative organisations or arrangements to provide care and support and preventative services

[7] From the first legislation in 1852 through to 2002, they were known as Industrial and Provident Society Acts.

[8] Paragraph 4.13 of the Guidance

[9] Paragraph 4.14 of the Guidance

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Whilst it is helpful that the registrar chooses to adopt this approach to ensure that the ICA Principles have some relevance in UK law, (a) it is less than satisfactory that cooperatives do not have a definition based on the ICA Principles that is set out in UK law; and (b) it is a matter of continuing concern that such an important matter depends upon the approach taken as a matter of discretion by the current registrar in a document simply constituting "general guidance".

One result of the lack of any legal definition of cooperative in UK law is the consequential lack of legal protection of cooperative identity. In the UK, it is said that a cooperative can take any number of forms including a company limited by shares or by guarantee, a community interest company and a number of others beside.[10] None of these other legal structures protect cooperative identity, with the result that in the UK the word cooperative risks being devalued.

ii. Specific elements of the cooperative law

a) Definition and objectives of cooperatives

Definition of cooperatives- There is no statutory definition of a cooperative in UK law generally or in the 2014 Act. However in order to register a new society, the founders must satisfy the registrar that the proposed society meets the conditions for registration either as a "bona fide cooperative", or as a community benefit society on the grounds that the business of the society is being, or is intended to be, conducted for the benefit of the community.[11]

As explained above, the registrar sets out its approach to this in its Guidance based on the first four ICA Principles. There are two other provisions in the 2014 Act which are important to mention. The first is section 2(3) of the 2014 Act which provides:

'*For the purposes of subsection (2)(a)(i) "co-operative society" does not include a society that carries on, or intends to carry on, business with the object of making profits mainly for the payment of interest, dividends or bonuses on money invested or deposited with, or lent to, the society or any other person*.'

By expressly stating what is not included, namely organisations pursuing what would broadly be seen as a profit-maximising purpose, this provision rules out the possibility of using a cooperative to pursue such a purpose.[12] It is therefore an important provision as it draws a clear distinction between cooperatives and investor-owned companies.

The other relevant provision is section 14 of the 2014 Act which sets out those matters which must be covered by provisions contained in a society's rules in order to satisfy the criteria for registration. But this section only says which subjects must be covered by the

[10] For example it has been common for worker cooperatives to register as a company limited by guarantee, or in some cases a company limited by shares

[11] Section 2(2) of the 2014 Act.

[12] This was precisely the intention when this provision was introduced in 1939, as societies were being registered and used to avoid the prospectus requirements introduced into company law for capital raising.

rules, not what the rules must say. Otherwise, that is as far as the 2014 Act goes in terms of defining “cooperative”. Beyond that, it is a matter for the registrar’s discretion.

It has already been noted that in the UK a wide variety of different corporate forms are suggested for cooperatives.[13] In relation to legal entities other than registered societies, there is no control over their registration as “cooperatives” in terms of meeting any particular criteria. For example, a company limited by guarantee might be used as a vehicle for a cooperative, but there is no oversight at all in relation to the contents of its articles of association and therefore no protection of cooperative identity. By way of illustration, Co-operatives UK provides model governing documents for, amongst others, community interest companies, companies limited by share and companies limited by guarantee.[14]

The use of the word “co-operative” in a company or business name requires permission from Companies House as explained in guidance which sets out the conditions to be met.[15] No permission is needed to use the word “co-operative” in the name of a registered society.

Cooperative objectives- In UK law, beyond the criteria for registration set out in the 2014 Act, and the registrar’s exercise of its registration function as described above:

- there is no stated objective of cooperatives;
- no precise purpose is assigned to cooperatives;
- there is no requirement for or definition of member promotion;
- transactions with members have no relevance and are not treated as distinctive;
- there is no requirement for members to transact with their cooperative;
- there are no restrictions on transacting with non-members.

The only extent to which any of the above are taken into account is where they fall within the parameters set out in the registrar’s Guidance.[16]

Given the limited criteria to be fulfilled for registration as set out above, and the lack of any positive obligation to pursue member-promotion, cooperatives are relatively free to pursue objectives beyond member-promotion.

Having said that, the other type of legal structure which is capable of registration under the 2014 Act is a community benefit society which is broadly comparable to general interest cooperatives in other jurisdictions. Community benefit societies are not allowed to distribute any surplus to members or otherwise to benefit members: their objective is, as the name implies, the benefit of the community.

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[13] See for example Co-operatives UK’s “Simply Legal” guide to choosing a legal structure https://www.uk.coop/sites/default/files/2020-10/simply-legal-final-september-2017.pdf

[14] https://www.uk.coop/resources/model-governing-documents

[15] https://www.gov.uk/government/publications/incorporation-and-names/annex-a-sensitive-words-and-expressions-or-words-that-could-imply-a-connection-with-government#co-operative It should be noted that the protection to co-operative identity afforded by this process is stricty limited to the word co-operative, and does not include, for example, cooperative, co-op or coop.

[16] As already explained, the Guidance states that the registrar generally expects ‘*to be able to verify and validate whether principles 1 to 4 … have been met through the rules and governance arrangements of a co-operative society, along with the society’s statements of intent about how it will operate.*’

Both cooperatives and community benefit societies may carry on any lawful trading activity. A society which has withdrawable share capital may not be registered with the object of carrying on banking.[17] Otherwise, and subject to the need to fulfil specific regulatory criteria to carry out regulated activities such as financial services or healthcare, a society may carry out any legal economic activity.

b) Establishment, cooperative membership and governance

Establishment and governance- There is a Mutuals Public Register[18] which includes cooperative and community benefit societies, credit unions, building societies and friendly societies. In relation to cooperative and community benefit societies, this is the register of all of those societies currently registered under the 2014 Act (or under prior legislation now consolidated into that Act).

As explained above, since in the UK a cooperative may be registered using a number of different legal structures including different types of company, there is no comprehensive register of all entities that might be defined or present themselves as cooperatives (some will be included in the register of companies). Over the years, various annual reports or surveys of cooperative enterprises intended to document the state of the cooperative economy have been and continue to be conducted,[19] but these all have to define the parameters by which they have been carried out.[20]

Cooperative membership- The law requires a minimum number of members for a registered society.[21]

Since cooperatives are not subject to any form of regulation in the UK, there is no regulation of the admission of new members. There is merely a requirement that the terms of admission of members are specified in the rules.[22]

There is some scope to ensure that a registered society appropriately follows the principle of open membership. This is because at the point of registration, the registrar will need to be satisfied that the society's rules adequately cover this, and the Guidance states that the registrar expects to be able to verify and validate compliance with this principle.[23]

Whether or not the registrar has taken action to protect this principle or where it has been breached is not known.

In relation to the voting power at members' meetings of registered societies, this is one of the matters which the registrar will need to verify at the point of registration when considering the rules of the society. Section 14 of the 2014 Act specifies that the 'method

[17] Section 4(1) of the 2014 Act
[18] https://mutuals.fca.org.uk/
[19] Co-operatives UK has produced such a summary for many years and the latest is https://www.uk.coop/economy
[20] Efforts for the harmonisation of cooperatives statistics at the international level are also ongoing, Guidelines concerning Statistics of Cooperatives were adopted in October 2018 by the International Conference of Labour Statisticians.
[21] Section 2(2)(b) of the 2014 Act requires a society to have at least 3 members, or 2 registered societies as members
[22] Section 14 of the 2014 Act
[23] See paragraph 4.13 of the Guidance

of holding meetings and the scale and right of voting, and the method of making, altering or rescinding rules' are matters for which provisions must be included in the rules.

It is believed that the principle of "one member one vote" is generally required by the registrar, though it is also clear from the Guidance that the registrar recognises the diversity of cooperative enterprises.

Governance- There is limited provision in UK law regarding the internal structure of administration. Section 14 requires that the rules must contain provisions about 'the appointment and removal of a committee (by whatever name) and of managers or other officers and their respective powers and remuneration'. Beyond that, it is a matter for each society to decide its own governance arrangements.

The general approach is for the members to elect a committee or board to manage the society on their behalf. Where a society reaches a size where it needs to take on a significant workforce, the most common approach is for the committee or board to appoint a manager or chief executive to manage the day to day business, but not to be a board member themselves. Whilst this can be said to be the general approach, there are obviously many variations to this. For example:

- occasionally the chief executive may be a board member;
- there may be intermediate structures between the grass-roots membership and the board – for example local area committees, and regional committees.

It is uncommon in the UK for the members in the general meeting (the "general assembly" in other jurisdictions) to play more than a nominal role in terms of exercising any real powers in the business. It may pass resolutions or motions, and make decisions about profits or surplus, but generally in the UK (of course there are exceptions, worker co-operatives for example) there is a tendency to follow the traditional approach in investor-owned companies where power within corporations tends to be centralised within the board. Culturally our approach to governance is more transatlantic than European, in the sense that the all-powerful board of directors as required for listed companies is seen as the norm.

In a cooperative enterprise registered other than as a society, there is nothing to ensure member control. In registered societies, the registrar's Guidance refers to verifying and validating that the second principle has been met in the rules. However, the Guidance does not expand on that, leaving the interpretation of democratic member control open to doubt.

It is a matter for the rules of each registered society to determine whether or not directors must be members. Generally, they are.

The duties of directors and senior executives of registered societies are in practice no different from those of any other trading corporate entity. In relation to ethical standards, there is nothing in UK law which requires directors of a cooperative society to meet any particular or different standard.

Where directors fail to meet legal standards and are found to be unfit by a court, they may now be disqualified from serving as a director of a society or a company under the Company Directors Disqualification Act 1986.

Directors can also be liable to the society itself for any breaches of their duties towards it. That liability can take the form of a damages claim by the society against the director or senior executive for its losses, or a claim to any profits that the director or executive has made personally from breaching their duties. However, such claims are difficult to pursue and are seldom made in practice.

c) Cooperative financial structure and taxation

There is no minimum capital requirement for cooperatives, although a registered society must have some capital. The only specific requirement in relation to capital is that the rules must include provisions:

- determining whether any or all shares are **transferable**, and the provision for the form of transfer and registration of shares, and the consent of the committee to transfer or registration; and
- determining whether any or all shares are **withdrawable**, and provision for the method of withdrawal and for payment of the balance due on them on withdrawing from the society.

It is for the rules of a registered society to specify the capital contributions required from members. It is not uncommon for this to be nominal (£1).

Where capital contributions are nominal, then members are likely to contribute equally. Where members' capital is used to fund the society's business then diverse contributions are common.

In consumer societies, capital contributions are not linked to the volume of transactions. It might be in worker or producer cooperatives, but that would be a matter for the rules.

In relation to member exit or dissolution, it is for the rules of the society to provide whether capital is returned to a member. Generally it is, subject to scale, solvency, etc.

Lastly, it is appropriate to mention that legislation imposes a maximum level of interest which an individual who is a member may have in the withdrawable share capital of their society, and that current limit is £100,000 (section 24 of the 2014 Act).

It should be noted that capital is not needed for certain other types of corporate entity e.g. a company limited by guarantee.

Allocation of profits- The way in which profits are to be applied is one of the matters which rules must cover.[24]

Otherwise, legal provisions concerning profits are more related to what is not permitted, than what is required. As set out above, the only help that UK legislation gives to defining a "cooperative society" is section 2(3) of the 2014 Act which states what is *not* included

[24] Section 14

in the phrase, namely '*a society that carries on, or intends to carry on business with the object of making profits mainly for the payment of interest, dividends or bonuses on money invested or deposited with, or lent to, the society or any other person*'.

As such, there is no positive legal obligation about how profits *must* be allocated – just a prohibition in the terms above. In paragraph 4.8 of their Guidance, the registrar sets out the features that they would look at in a society's accounts in order to ascertain whether a society was falling foul of this provision, and these include:

- amounts of surplus distributed to members in proportion to their participation;
- the level of interest or bonuses paid on money invested, or deposited with, or lent to the society, against amounts distributed to members as dividends, and levels of interest etc. paid to comparable investor-owned businesses; and
- the nature of the relationship between members and the society.

There is no legal requirement to establish reserves.

A cooperative would only be permitted to distribute profits to members in proportion to capital subscribed if its rules permitted this, and it is unlikely that the registrar would register a society with such a provision in its rules or accept such an amendment to its rules. Such an approach would be difficult to justify against the 3rd principle, and so it seems unlikely.

It would be difficult to assert that a cooperative must distribute profits only according to the volume of cooperative transactions, but for the reasons set out above this is broadly how the law is interpreted in the UK. This is subject to other factors, such as the ability of a cooperative to use profits for other social and community purposes if its rules so provide (which they commonly do).

There is no recognition in UK law of any distinction between profits generated from trade with members and trade with non-members. As far as is known, societies do not maintain accounts which observe any such distinction.

The concept of patronage refunds is therefore not recognised as distinct from dividends. It should also be pointed out that in the UK, cooperatives use the word "dividend" to describe a profit distribution proportionate to transactions with the society i.e. a patronage refund, whereas in the context of investor-owned companies, "dividend" denotes a distribution of profits based on shareholdings. This use of terminology is unhelpful, because it results in people in the UK misunderstanding the nature of a cooperative "dividend".

It is not uncommon for societies to pay interest on members capital at a rate specified in the rules (or at a rate to be determined in accordance with the rules), but this again is subject to the prohibition contained in section 2(3) of the 2014 Act.

In its Guidance in paragraphs 6.23 – 6.28, the registrar sets out its general approach towards payment of interest by registered societies, and specifically in relation to cooperatives in paragraphs 6.29 – 6.30.

Financial instruments- UK law is relatively sparse in its provisions regarding financial instruments for cooperatives, and reference has already been made above to section 14 of the 2014 Act requiring minimum provisions in relation to shares. The law is generally understood to be permissive in relation to the issuing of financial instruments, within the parameters previously noted above.

In relation to "investor members", following the introduction of the European Cooperative Society, a guidance note was issued by the registrar setting out parameters within which investor members would be accepted should any society seek to introduce rule amendments to permit them. This is now contained in paragraphs 6.31 and 6.32 of the registrar's Guidance.[25]

Other forms of member financing are also used, more so in particular sectors such as agriculture. Section 14 of the 2014 Act provides that a society's rules must include provisions determining '*whether a society may contract loans or receive moneys on deposit subject to the provisions of this Act from members or others, and if so under what conditions, under what security and to what limits of amount*.'

Dissolution etc.- It is for the rules of a society to determine the destination of a capital surplus on a solvent winding up; there is no statutory basis to ensure a disinterested distribution. Similarly there is no protection against the risk of conversion into, or transfer of engagements to a company (the most common alternative), and this was the reason for a change to the law in 2002 (the Industrial and Provident Societies Act 2002) which introduced higher thresholds on a resolution to convert into or transfer engagements to a company. Such a resolution, in addition to being passed by a 75% majority of eligible members who vote, can only now be passed if at least 50% of the society's members eligible to vote actually vote on the resolution.

Further protection of capital surplus has been introduced into the rules of the majority of the UK's large retail societies with provisions essentially ensuring that on a solvent winding up, any capital surplus would be transferred to another cooperative society or Cooperatives UK. Other societies have also introduced such a provision. However it remains open to the members of any of these societies for the time being to amend their rules to remove such protective provisions. Although restrictions are normally included to make such rule amendments more difficult, ultimately it is not possible to preclude any such rule amendments under UK law.

[25] The Guidance refers to "indicators that the society is complying with its condition for registration", and that are (a) including express provision in the rules allowing for non-user investor shares and the terms attached to them; (b) restriction, in the rules, of the rights of non-user investor shareholders including prevention from their voting on a resolution to convert to a company; and (c) ultimate control remaining with members other than non-user investor members at all times.

iii. Other specific features

d) Cooperative internal and external control and cooperation among cooperatives

External control- Cooperatives are not subject to external control. They are treated just like any other private legal or corporate entity. There is no audit process for cooperative representative organisations to carry out.[26]

Self-control is not promoted by the law, not least because the legal nature of cooperatives is not recognised by UK law. But as mentioned above, as a condition of registering a cooperative society and permitting the continuation of such registration, the registrar expects to verify and validate compliance with ICA Principles 1 to 4, including autonomy and independence. If it therefore became apparent that a cooperative was, for example, no longer independent or autonomous because it was controlled by another entity (a lender, for example) rather than by its members, then the registrar might take the view that the society no longer complied with the condition for registration.

Cooperation among cooperatives- This principle is not implemented in UK legislation. Even the registrar acknowledges that they do not expect to be able to validate principle 6, though "*evidence of compliance … would be treated as a positive indicator*" (paragraph 4.14 of the Guidance).

Cooperation among cooperatives is permitted in the UK, subject of course to competition law, but it is neither mandatory nor regulated.

In addition, there is a variety of different apex or federal organisations through which cooperatives work together. These are generally sector-based, but they include:

- Co-operatives UK, the national apex body for all UK independent co-operatives
- Federal Retail Trading Services for the UK's retail societies;
- CCH, the Confederation of Co-operative Housing, for housing co-operatives, tenant-controlled housing organisations and regional federations of housing co-operatives; and
- SAOS, the Scottish Agricultural Organisation Society, providing services for Scotland's farming and rural business communities.

Cooperative taxation- Cooperatives are not subject to a particular tax regime; they are subject to the general tax regime applicable to all other business organisations.

It is not possible at the moment to argue that the tax regime is inconsistent with the nature of cooperatives, because there is no recognition of that legal nature. In this sense, the UK tax regime is not supportive of cooperatives, nor can it be until the legal nature of cooperatives is recognised in UK law.

There are two further points which are worth making in relation to taxation.

[26] There is a voluntary Co-operative Corporate Governance Code published by Co-operatives UK https://www.uk.coop/sites/default/files/2020-10/co-op_corporate_gov_code.pdf

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The first is that payments of dividends or distributions to members of a cooperative (no payments to members are permitted in a community benefit society) are treated in the society's accounts as an expense of the business and therefore deductible for corporation tax purposes. Similarly, payment of interest on share capital is deductible. This contrasts with the payment of dividends to shareholders of a company which are paid "below the line" after tax.

The second is the concept of fully mutual trading, where members form a cooperative to conduct trade for their mutual benefit (for example purchasing or marketing cooperatives). Such a cooperative is not liable for corporation tax, provided that the cooperative complies with a number of requirements, on the basis that the transactions concerned will be included within the affairs of individual members for tax purposes. The requirements are that all surpluses go back to members and to no-one else; contributors to and participants in the cooperative are identical; that the return of surplus is in proportion to transactions with the society; and members control any common funds.

III. Degree of "cooperative friendliness" of the national legislation

National cooperative legislation plays a part in the "cooperative friendliness" of a jurisdiction, and it follows from what has been said above that because of the lack of the recognition of the legal nature of cooperatives as distinct from other legal entities, UK legislation is a barrier to the development of cooperatives. Cooperatives are marginal in the UK economy, and currently there is no realistic prospect (in the writer's view) of cooperatives becoming anything other than marginal unless the distinct legal nature of cooperatives is recognised. It is only once that is achieved, and hard-edged legal requirements introduced for cooperatives (such as the setting aside of surplus and the maintenance of indivisible reserves) that there can be any argument that cooperatives should be treated any differently from other legal entities. In this respect, the tendency in the UK to say that a cooperative can take any form is, in the view of the national expert, counter-productive and ultimately self-defeating.

It must be pointed out, however, that this view is not held by Co-operatives UK. As observed above, they promote a wide range of legal structures for those wishing to establish a cooperative venture, and they see the flexibility in the choice of legal form as an enabler.

It is also important to recognise that it is not simply the legislation dealing with the establishment and maintenance of legal structures (e.g. the laws under which cooperatives are registered) which determines the "cooperative friendliness" of a jurisdiction. Other important factors include:

- the extent to which other general legislation makes assumptions about the type of legal structures that will be utilised. For example, in regulated sectors where statutory provision is being made for non-state bodies to assume certain activities

and functions, if the assumption is that such bodies will inevitably be a company, then the possibility of a cooperative fulfilling such a role may be precluded.[27] It is also not uncommon in the process of making new laws to make provision for companies, but not to include cooperatives.[28] This is more likely to be due to lack of familiarity with cooperatives, and perhaps also the fact that the main UK business department is responsible for companies but not cooperatives;

- it is obviously possible for legislation to counter this tendency to "isomorphism" by expressly providing for cooperatives, and it is possible to go further by positively encouraging the use of cooperatives. There is no history of such positive encouragement generally in the UK, but there is a good example of this in Wales (under devolved powers where the Welsh Assembly has statutory responsibility) which is generally more cooperative friendly than the Westminster Parliament for the UK as a whole. This is exemplified by the Social Services and Well-being (Wales) Act 2014 which expressly requires the promotion of cooperatives and certain other types of organisation (section 16); and
- the predominant commercial context, market expectations, competition law and procurement law, all of which can act to make it difficult for cooperatives to act and have relationships with other parties in a way which is consistent with their values and principles, but where these other factors (whether individually or collectively) leave them no choice other than to behave just like investor-owned enterprises trading for private benefit.

It would be a significant exercise to map all of those areas of law which damage cooperatives or hamper their development, but competition law and procurement law are perhaps the most obvious examples.

Co-operatives UK also highlight the location of the registration function within the FCA as a barrier to cooperative development. They argue for the transfer of the function to the Department for Business, Energy and Industrial Strategy which has departmental responsibility for companies. In the national expert's view, there is a clear argument for locating responsibility for all types of legal structure within one government department, but this would also require both an appropriate mechanism for protecting and promoting the distinctive identity of cooperatives and community benefit societies in the registration function, and also the appointment of a minister with specific responsibility for such distinct entities.

There is one further barrier to mention. The lack of recognition in the UK of cooperative identity, and the local tendency to see the use of multiple legal forms as an advantage, results (in the view of the national expert) in a low level of legal innovation in relation to cooperative law. Cooperatives are capable of providing a radically different mechanism

[27] A good example of this is in education, where schools can convert into "academies" to secure direct funding from central government, independent of local authority control. But the legal vehicle they must use is a company limited by share, with no option of using a cooperative or community benefit society.
[28] A good example of this is the recent emergency legislation for the pandemic, amending corporate insolvency law, and also allowing general meetings to be held virtually. In both cases cooperatives were initially not included in the legislation until Co-operatives UK raised the issue.

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for addressing the needs of humans at a time of great danger to humanity. But for this to be realised, legal innovation is essential to open up contemporary challenges to cooperative solutions. There are currently few cooperative law specialists in the UK, and fewer still with a perspective of the wider opportunities which cooperatives can afford because they have not had exposure to what is available in other legal systems.

Examples of best practice- It is difficult to identify any areas of best practice for cooperatives in UK legislation because (a) cooperatives are not recognised as a distinct type of organisation; (b) there is no national or public promotion or encouragement of cooperatives except from within the cooperative movement; and (c) if anything the dice are loaded against cooperatives in areas such as procurement because of the predominance of investor-owned business and the prevailing business culture. There is a dominant narrative in the UK that sees investor-owned businesses driven by the profit motive as the norm, and little incentive to accommodate anything else.

It could be argued that the wide range of legal forms available in the UK which can be used by those seeking to set up a cooperative is an advantage. However, as already pointed out there are distinct disadvantages with this approach, and in addition:

- it makes it really important for those setting up a cooperative to get good advice about how to ensure compliance with cooperative principles. Generally, however, the establishment of new cooperative ventures is based on the use of toolkits and model constitutions, assuming that those using them can “do it themselves”; and

- as explained above there is limited protection of a capital or cooperative surplus if the legal form used is a registered cooperative society, but there is no real protection of a capital surplus in any other case.

Degree of cooperative friendliness of national legislation

Against the following scale of friendliness:

a) *It is very much so*
b) *It is quite/rather/significantly so*
c) *It is only limitedly so*
d) *It is more cooperative friendly than not*
e) *It is more cooperative unfriendly than friendly*
f) *It is cooperative unfriendly*

the national expert concludes that the UK is ***cooperative unfriendly***. In reaching this conclusion, he would highlight the following as the basis for that opinion.

There is no recognition of cooperatives as a distinct and legitimate type of organisation which could be of benefit to the common good. By way of comparison, the UK clearly recognises charities as a “good thing”, and consequently has a clear definition of what it means to be a charity (having a defined charitable purpose), has a gate-keeper to regulate those organisations entitled to call themselves charities (the Charity Commission), and encourages the existence of such organisations by providing clear fiscal benefits both for charities themselves in carrying out their charitable activities, and

for individuals voluntarily giving money to charities. None of this exists for cooperatives, and the starting point for this deficit, the expert believes, is that there is no recognition that cooperatives bring any positive benefit to the state, to the economy, or to the wider community. It is arguable that this is changing slowly, with growing interest in concepts such as social value e.g. via the Public Services (Social Value) Act 2012, but such progress feels somewhat limited. This makes the UK a fundamentally unfriendly place to establish cooperatives, though even within the UK, there is a distinct difference in Wales. As a result of devolution, Wales is now able to enact legislation which is more cooperative friendly than England, as already mentioned.

As there is no recognition that cooperatives bring any social or economic benefit, there is no attempt (nor any basis to attempt) to secure different tax treatment for cooperatives. Consequently, cooperatives are treated no differently from companies, which means that for many people there is little if any point in adopting a cooperative business form, with the additional complexity of member democracy.

Since there is no legal recognition of cooperatives as a distinct legal form, there is no real basis of principle for protecting a capital surplus against demutualisation. There is no equivalent to indivisible reserves in other jurisdictions, which would both sustain a cooperative business in the long term and defend it against conversion to or take-over by an investor-owned company. Capital surpluses therefore effectively remain at long term risk of demutualisation and capture for distribution to shareholders.

Because there is no recognition of a cooperative as a distinct type of business, there is no statutory definition of a cooperative, and the only protection that the law provides is through the function of the registrar. Helpfully the registrar now publishes detailed Guidance (referred to above) about how it approaches the discharge of its functions, and this includes clear and helpful statements about how it seeks to give meaning to and protect the integrity of cooperatives. However, this Guidance is within the power of the registrar and in theory could be changed. The status and integrity of that Guidance at least in part depends on where the function of registrar is located, and currently it is located within the Financial Conduct Authority (FCA). As its name implies, the FCA is primarily a financial regulator. It is the conduct regulator for 59,000 financial services firms and for financial markets in the UK and the prudential supervisor for 49,000 firms, setting specific standards for 19,000 firms. Its main focus of attention is therefore on investor-owned businesses. Cooperatives and other mutual societies do not sit comfortably within this context, and are certainly not “core business” for the FCA;

According to a previous study concerning the treatment of indivisible reserves of EU member states, the UK and Ireland were amongst the five states which did not have any requirements for setting aside indivisible reserves.[29]

Co-operatives UK take a similar but not identical view about the cooperative friendliness of the UK, also concluding that it is ***more cooperative unfriendly than friendly***.

[29] The study can be found here https://www.feps-europe.eu/resources/publications/709-who-owns-europe-and-why-it-matters-for-progressives.html See the conclusions on pages 125 and 126.

International comparisons- The legislative changes that are needed in the UK are of a fundamental nature and not easy to achieve. The European legislation which the national expert has reviewed is for very different legal jurisdictions. He is also aware that legislation in, say, Canada and Australia (which might be more comparable) have a very different starting point, though some aspects may be helpful.

In order to provide a source of inspiration or a template for change, it may be appropriate therefore to look at other legislation in the UK, e.g. for the registration of charities, and also a range of different foreign jurisdictions. It is not obvious to the national expert (with limited knowledge of jurisdictions outside the UK) that any one jurisdiction on its own is likely to be a particular source of inspiration.

It is also known that Belgium recently introduced radical reforms for companies and associations (March 2019) with significant changes for cooperatives.[30] There are two aspects of these reforms which may justify further consideration in seeking ways of improving UK cooperative law:

- first, exploring how these new laws established a basis for cooperative identity, and the mechanism for the protection of such identity; and
- the process by which such new legislation came about. Initiating a process for reviewing cooperative law, when cooperatives play a marginal role, is challenging; lessons should be learned from elsewhere wherever possible.

IV. Recommendations for the improvement of the national legal framework

It follows from what is argued above that the most fundamental necessary changes are, in the view of the national expert, to make provision for the recognition of a cooperative as a distinct and protected type of organisation in UK law. Amongst other things, this will require:

- a statutory definition of "cooperative", with which compliance is needed for registration;
- that this definition is linked in some way to the ICA principles, so that compliance can have a clear basis in law and is based around internationally accepted principles which can be verified in the rules of a society. These should include the establishment and maintenance of reserves at least part of which should be indivisible. It is this which seems to be capable of founding an argument for different tax treatment; and

[30] These reforms are discussed further in Thierry Tilquin and Maïka Bernaerts, National Report for Belgium, ICA-EU Partnership, Legal Frameworks Analysis, Cooperatives Europe, August 2020.

- enhanced powers for the registrar to act as a gate-keeper and also as a regulator (not just a registrar) to ensure that only organisations which meet the definition are registered in the first place, and are able to maintain their registration.

Fundamental changes of this nature will inevitably lead to the significant rewriting of other parts of UK cooperative law.

Aside from the changes referred to above, another important area of concern from a statutory point of view are the provisions for capital. There have been discussions over a number of years about making express provision for the establishment of a different type of financial instrument from that mainly used in UK cooperatives at the moment, namely withdrawable share capital (WSC). As well as being withdrawable, cooperative capital differs from capital in an investor-owned company because cooperative capital is variable, whereas company capital is fixed.

WSC was an ingenious invention in Victorian times as it allowed cooperative stores to act as local banks, with members having the ability to deposit and withdraw funds. But WSC today is more problematic, as the ability of members to withdraw their funds leads to uncertainty for the business. The ability to withdraw has historically been seen as a necessity in order to enable a member to exit.

The solution that has been developed is to create a type of share which can be repaid by the cooperative, enabling the society to maintain control over its own capital. Such shares might be issued on a term basis (e.g. 5 years, or 10 years), enabling the member to know that there are specific points of exit should the capital be needed.

Considerable progress has been made in developing these ideas, which also include providing that such shares provide no entitlement to a share in any capital surplus, so that the members rights are limited to repayment of the share and such compensation (interest) as may have accrued during the time of holding the share. A draft Cooperative Capital Bill has been prepared but there has not been an opportunity for this to be considered for enactment.

Co-operatives UK also argue that the following specific reforms should be made:

- that legislative and policy-making responsibility for societies should be moved from HM Treasury to the Department for Business, Energy and Industrial Strategy;
- for the registration function for societies to be moved from the FCA to something better-purposed, better resourced and closer to the orbit of the Department for Business, Energy and Industrial Strategy and Companies House; and
- that the law should be changed to give cooperatives societies the option of either or both of non-distributable assets and indivisible reserves.

Making UK law more cooperative friendly- Co-operatives UK argue that it is important that Brexit legislation must take account of the immediate needs of agricultural co-operatives.[31]

[31] https://www.uk.coop/get-involved/influencing-policy/search-policy-activity/protecting-farmers-ability-co-operate-after

V. Conclusions

Although it is widely regarded as the birthplace of cooperation, UK cooperative law remains comparatively under-developed with the result that the UK is an unfriendly environment for the establishment and promotion of cooperatives.

UK cooperative legislation has now been helpfully collected together in one place (the 2014 Act), but this was merely a consolidation of existing laws. Since its origins in the nineteenth century, there has never been a formal and proper review of UK cooperative law with a view to optimising the contribution it can make to the common good of all in the UK. By contrast, UK company law is thoroughly reviewed and (if necessary) fundamentally reformed every generation or so.[32]

The work of this Legal Framework Analysis project is therefore important in two respects. First, it requires individual jurisdictions to take stock of the state of their cooperative law and thereby to enable comparison with other jurisdictions. Second it thereby provides a platform for cooperation between nations, their parliamentarians and jurists and their cooperative agencies in identifying areas where their cooperative laws lag behind and can address deficiencies with a view to optimising this vital area of law for the benefit of all humanity.

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[32] For example, the latest major reforms were 1948, 1985/6 and 2006.