



WHAT IS A GUARANTEE COMPANY?

This Fact Sheet, which is one of a series we provide to assist Charities, is aimed at anyone or any Steering Group which is contemplating either setting up a Charity or changing an existing charity to one with limited liability.

Introduction

The technical name of a Guarantee Company is 'a company limited by guarantee but without a share capital'. It is one of the types of company, affording limited liability, which can be set up under the Companies Acts 1985 -1989.

Where a voluntary and/or community organisation enters into contracts, as it is likely to do in any active project work, it needs the benefit of limited liability to protect its Board of Trustees and its members, who are otherwise involved on a voluntary basis. Such contracts might for example include contacts of employment, the purchase of property, building contracts, contracts with fund-raisers, contracts with service providers, etc. That protection of limited liability can be supplied by the framework of a guarantee company.

In addition, a guarantee company provides a clear legal identity, the ability to own property in its own name and a democratic structure where its participants are required to adhere to the strict laws and regulations governing limited companies generally.

A guarantee company is often referred to as a 'not-for-profit organisation', meaning that its profits are not distributed to its members but are retained to be used for the purposes of the guarantee company. Of course this does not mean that the guarantee company cannot make a profit, as indeed it is almost paramount that it can and does so. It would therefore be better called a '**non-profit-distributing organisation**'. As such it is ideally-suited to many charitable and community initiatives where its purpose and assets remain in the charitable or community domain, rather than in the hands and ownership of individuals.

The main differences between a guarantee company and a company with shares are:

- its members do not receive share certificates and whilst they control the guarantee company, through decisions taken by them at General Meetings, they do each not “own” a proportionate part of the guarantee company.
- its members cannot receive any dividend, profit or other income from the guarantee company, nor can they receive a share of its assets if it comes to an end.
- its members enjoy limited liability, but usually have to pay an annual subscription (at a rate set annually by themselves at General Meeting) and, if the guarantee company is forced to come to an end through a liquidation, they are obliged to pay a final sum of £1 each to the Liquidator.
- the members (in most cases) elect the Board of Directors (usually called Trustees or Governors to avoid connotations of salaries and bonuses) which is responsible for setting and overseeing the policy of the guarantee company.
- the Directors also enjoy limited liability, provided that they have not acted negligently, or fraudulently, or have not permitted the guarantee company to continue trading when it was insolvent (this is known as “wrongful trading”).

Constitution of a Guarantee Company

The constitution of a Guarantee Company is known as ‘the Articles of Association’. In older Guarantee Companies, which predate the Companies Act 2006 (or which have not been amended to take account of the provisions of the current Act), the constitution is in two parts - the Memorandum of Association and the Articles of Association.

In such older constitutions, the Memorandum of Association explains:

- the type of company being created
- its main Objects (all of which must be charitable if the guarantee company is to be recognised as a charity, where they are referred to as the ‘Charitable Purposes’), which describe the maximum extent of the guarantee company’s ambit
- its Powers (to enable the Objects to be carried out)
- restrictions on money being paid out by the guarantee company to its members and Trustees
- the personal guarantee given by each member (usually £1) upon liquidation
- what is to happen to the surplus assets if the guarantee company comes to an end (which, if the guarantee company has been a charity, must be transferred to one or more other charities).

In older constitutions, the Articles of Association explain:

- how membership can be applied for and ended
- the rules relating to members’ meetings (known as Annual General Meetings or Extraordinary General Meetings)
- how Trustees are elected or appointed, their term of office and how they retire
- the rules relating to Board meetings and meetings of any Committees
- any provisions relating to Conflicts of Interest
- the appointment of the Company Secretary
- provisions relating to the finances and the annual accounts
- the appointment of the independent financial examiner (as Auditor).

In newer constitutions, written or amended under the Companies Act 2006, the Articles of Association amalgamate what was previous shown separately in the memorandum or the articles, so that these new composite articles now contain:

- the type of company being created
- its main Objects (all of which must be charitable if the guarantee company is to be recognised as a charity, where they are referred to as the 'Charitable Purposes'), which describe the maximum extent of the guarantee company's ambit
- its Powers (to enable the Objects to be carried out)
- how membership can be applied for and ended
- the rules relating to members' meetings (known as Annual General Meetings or Extraordinary General Meetings)
- how Trustees are elected or appointed, their term of office and how they retire
- restrictions on money being paid out by the guarantee company to its members and Trustees
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Advantages

- members' liability is restricted (usually to £1 each)
- the guarantee company can hold property and borrow money in its own name
- the guarantee company is subject to the democratic control of members - both in relation to fundamental decisions (e.g. a change in its constitution) and in relation to election/re-election of the Board.
- it is relatively easy to set up a wholly-owned subsidiary company, with a share capital owned by the guarantee company, which is particularly useful where the guarantee company is a charity and the subsidiary company is to be used for non-charitable trading (often called "a trading subsidiary").

Disadvantages

- the guarantee company is bound by the terms of the Companies Acts and thus subject to more controls than any other legal structure. These controls are really designed to protect the shareholders of commercial trading companies and, however inappropriate these may sometimes seem to a community-run guarantee company, they have to be adhered to
- costs of setting up including legal advice may be substantial (although in some cases, particularly for charities, there may be grant aid available to assist in meeting these start-up costs)
- annual expenses are incurred - the audit or independent financial examination of the annual accounts and the company secretarial work (intimating to the Registrar of Companies

changes in the composition of the Board, lodging an Annual Return, lodging the annual accounts, arranging the AGM, etc.).

Constitution / Articles of Association

A number of issues will require to be considered by the promoters of the new organisation, which include:

- **Determining the Objects** which the new organisation intends to carry out. Particular care with the Objects requires to be taken where charitable status is to be sought as all of the Objects must be charitable, not just some of them. If only could be charitable, consideration should be given to setting up a separate but wholly-owned subsidiary company to carry out the non-charitable elements - where the charitable guarantee will own all the shares in its trading subsidiary company.
- **Determining whether there will be a membership**, as well as a Board of Trustees, as a 'two-tier organisation' or whether there will be only a Board of trustees, as a 'single-tier' organisation. Where there is to be a separate membership consideration will have to be given as to its composition; how members are to be appointed; whether there will be more than one class of member; and whether there are any different voting or other rights attaching to different classes of member.
- **Determining the membership subscription** (if any).
- **Determining the Board of Trustees** (although actually Directors of the Company, but not usually called 'Directors' in the charitable world); their minimum and maximum number; how they are to be elected, nominated and/or appointed; the length of a term of office; and the maximum time they can serve.
- **Considering any issues which will require a 75% vote.**
- **Considering the terms upon which the guarantee company would be wound up** and a mechanism to determine to which other charity or charities its surplus assets would be transferred.
- **Considering an appropriate name.** If it is a charity, it may wish to exclude the word "company" or "limited" in its name and to include, for example, the word "trust" or "partnership" (even though it is a company rather than an actual trust or partnership). It is possible to obtain preliminary approval to a name from the Registrar of Companies and would be essential to do so if the proposed name contains a sensitive word such as "Scotland", "Scottish". "Institute", "Authority", etc.

Formation of a Guarantee Company

- to prepare draft Articles of Association
- if the guarantee company is to be a charity, to send the draft to OSCR, with an application form and supporting documentation, for their informal opinion on its potential charitable status
- to seek approval from the Registrar of Companies to the proposed company name if it includes any sensitive words
- to finalise the Articles
- to select the Company Secretary (if there is to be one) and to choose the Registered Office
- to select the first Trustees ("the Subscribers" because they sign, or subscribe, the incorporation papers)

- to hold the Subscribers' meeting and to sign the incorporation papers
- to incorporate the company and obtain the Certificate of Incorporation
- if to be a charity, to obtain from OSCR its formal Charity Registration
- to hold the first meeting of the Interim Board.
- to hold the first General Meeting of members.

Publicity about a Guarantee Company

The name of the guarantee company must be displayed at its Registered Office and at any other business office at which it carries on its operation.

All stationery (notepaper, invoices, cheques, website, etc.) of the guarantee company must show its full name as stated on its Certificate of Incorporation, its Registered Office address, its business address (if different), its registered company number and the fact that it is registered in Scotland. One can decide whether to show the names of Trustees (directors) on the notepaper but, if so, all of the Trustees must be shown, not just some. If the guarantee company is also charity, this must be stated on its notepaper, chequebooks and other stationery and its website; it is advisable to include the Scottish Charity Number.

Charities and Trustee Investment (Scotland) Act 2005

The Charities and Trustee Investment (Scotland) Act 2005 has introduced another type of organisation which, like the Guarantee Company, provides limited liability - the Scottish Charitable Incorporated Organisation (the SCIO).

The SCIO provides a relatively simple type of charity which can be used either as a single tier model (where the Trustees are the only members) or as a two-tier model (where there is a membership and a separate Board of Trustees). The SCIO may have advantages particularly for charities which do not wish to be regulated both by the new Charities Act and the Companies Acts. Please see our Fact Sheet [“What is a SCIO?”](#) Our experience is that most charities require a tailor-made solution, along the lines we have been providing for many years. We will continue to provide this service, part of which will be to propose the type of organisation most fitting to your proposals.

It is possible for an existing Guarantee Company to apply to convert into a SCIO, should that be considered appropriate. This is a one-way system, however, as a SCIO *cannot* convert into a Guarantee Company.

*Although carefully prepared, this Fact Sheet is a guide only and is not intended to be comprehensive.
Specific advice should be requested on individual situations.*

Colin Liddell
Accredited by the Law Society of Scotland as a specialist in Charity Law
2015 edition

