

☑ SECTION: GOVERNANCE

# Setting up a CLG How to Establish a Company Limited by Guarantee

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## ARTICLE ON HOW TO ESTABLISH A COMPANY LIMITED BY GUARANTEE

The purpose of this article is to explore the relative advantages of a company limited by guarantee when compared with other legal forms that a charity might take and to outline the documents required to be completed, and the information required to be submitted, for the purposes of incorporating a company limited by guarantee.

### 1 Summary of Different Legal Forms

There are three distinct and separate legal forms that a charity may take:

- A company;
- a trust; and
- an unincorporated association.

#### 1.1 Company

A company has a legal personality which is separate and distinct from that of its members. As a company is a separate and distinct legal person, only the company can be sued for its obligations (unless, among other things, it were clear that the existence of the corporate structure was put in place only as a vehicle for fraud or to avoid existing legal obligations).

Most forms of company come with the important feature of limited liability. In the event of such a company failing, shareholders only stand to lose their investment.

##### **There are two types of company limited by guarantee:**

- a company limited by guarantee; and
- a designated activity company (limited by guarantee, with a share capital).

A company limited by guarantee does not have shares or share capital like typical limited companies. As there is no share capital, its “shareholders” are referred to as its “members”. Members receive their interest in the company in return for guaranteeing to pay a fixed amount of money to the company in the event of it being wound up (usually a nominal sum such as €1). The fact that this amount is fixed, means that there is no value in a member’s interest in the company and no possibility of profit in the event of a member selling their interest. There is no limit on the number of its members (unless its memorandum and articles of association provide otherwise).

This elimination of the element of profit and the ability for there to be an unlimited number of members has attracted charitable bodies to this form of entity. References to a “company” in this booklet are, therefore, references to a company limited by guarantee.

There is a second type of guarantee company, a designated activity company (limited by guarantee) that has a share capital, but it is a rarity. Members are obliged to take shares, as well as to give a guarantee. There is a limit of 149 on the number of members.

#### 1.2 Trust

In simple terms, a trust is an arrangement, often governed by a deed of trust, under which a person or persons (trustees) hold property or funds on behalf of other persons or objects. The underlying reason for a trust’s existence is to protect and use the property for the benefit of some other person or object so that the real benefit accrues to that other person or object.

The trust has historically been the form adopted by bodies established for charitable purposes.

#### 1.3 Unincorporated Association

An unincorporated association is simply a collection of individuals, often bound by a set of rules and having identifiable members. An unincorporated association has no existence in law separate from its members.

Charitable bodies often start out life as an unincorporated association and those that grow in organisational complexity tend to incorporate as companies limited by guarantee.

## **2 Benefits of incorporating as a Company Limited by Guarantee**

This section explores the relative advantages of a company as the appropriate legal form for a not-for-profit body.

(i)

A company provides for a more suitable corporate structure and more modern method of governance than a trust or an unincorporated association because:

- a company has perpetual succession;
- a company automatically brings about transparency in reporting;
- a company is the preferred structure for government or public grant funding providers of finance; and
- the internal controls of a company can be stated more explicitly.

(ii)

A company structure relieves the trustees of automatic unlimited personal liability.

(iii)

A limited company does not impose unlimited personal liability on members.

(iv)

A company structure facilitates a more straightforward implementation of the requirements of the Charities Act 2009 (the "Charities Act") given the overlap in reporting and other requirements.

### **2.1 Perpetual Succession**

Trusts and unincorporated associations, not being legal entities in their own rights and having no separate existence in law, cannot hold property on their own behalf. Individual trustees or representatives must undertake this responsibility on behalf of the trust or association. Therefore, every time there is a change in trustee or representative, property documents must be executed to vest ownership of the trust property in the new trustee or representative. With a company, the company itself is the permanent owner of the trust property. A change of director of a company is an unremarkable administrative act that does not require the title to property held by the company to be vested in the new director.

### **2.2 Transparency in Reporting**

Companies are obliged to comply with a number of record-keeping and filing obligations. While this brings consequent professional and administration costs (legal, accountancy, audit, company secretarial), obligations similar to those affecting companies are now imposed on all charitable bodies by the Charities Act.

A company must also display (among other things) its CHY number, its company registration number and a list of its directors on its letter head paper. The constitutional documents of a company (memorandum and articles of association) and details such as the identity of the directors and first members of a company are required to be made available to the public in the Companies Registration Office ("CRO"). This is not the case for a trust. While this permits a trust to retain a level of confidentiality, the lack of publicly available information for trusts may be construed by stakeholders as being unnecessarily secretive.

The Charities Act requires that information in respect of all charitable bodies (incorporated or not), including the names of the trustees, its registration number and its objects, must be made available to the public on the register of charitable organisations. While the Charities Act does not expressly require that the governing documents of charitable bodies be made publicly available, the Charities Act gives the Minister for Rural and Community Development the power to prescribe information to be included in the annual report of a charity, which may subsequently become publicly available. The nature of what might be included in such information is not limited by the Charities Act.

### **2.3 Financial Matters**

It is becoming the trend that financial institutions, when lending money, and government bodies, when providing grants, prefer to deal with companies rather than unincorporated entities. A company is able to give security over more classes of assets than a trust can.

### **2.4 Internal Controls**

Regardless of the structure of an organisation, its governing body must have in place systems to ensure that its decision-making processes are transparent and that there are clear lines of responsibility for the work and actions of the organisation. A company structure requires the creation of these lines of responsibility and is a structure with which many are familiar.

With a company, the members are the stakeholders or owners of the company while the powers of management of a company's business are vested in its directors who are accountable to the members in respect of the management of its business.

A company structure allows for certain explicit controls to be put in place which can protect those with interests in the company such as:

(i)

ensuring that the principal objects clause of the company's memorandum of association is finely crafted so as to specifically limit the capacity of that entity to engage in activities that conflict with its express objects or in any wayward activity that would be outside of the intended purpose of the company;

(ii)

seeking to ensure a constant representation of the members on the board of directors of the company;

(iii)

using the disciplines of the Companies Act 2014 such as:

- publication of accounts to members;
- convening of general meetings of members; and
- rotation and renewal of the board of directors;

in order to remind the board of directors of its accountability to the members; and

(iv)

the embedding of veto rights in favour of the members, and, where necessary, third parties, in the memorandum and articles of association of the company.

### 2.5A company structure relieves the trustees of automatic unlimited personal liability

At present, trustees have unlimited liability for the debts and liabilities of a trust, although they of course have recourse to the assets of the trust. But where those assets fall short of the liabilities, the individual trustees are personally liable. On the other hand, the directors of a company do not have unlimited personal liability, in the absence of fraud, reckless trading or failure to keep books of account.

The Charities Act provides some protection to trustees by allowing a court to relieve a trustee, in whole or in part, for a breach of trust for which they are or may be liable where it appears to the court that the trustee acted honestly and reasonably. However, in the case of a trust, it is for a court to absolve the trustee of liability, rather than in the case of a company where unless the court imposes such liability, the director does not have that liability.

### 2.6 A limited company does not impose unlimited personal liability on members

All companies have members as well as directors. In a guarantee company, the members' liability is (typically) an undertaking to pay €1 in a winding up. (In a company with shares, the members are the shareholders, with liability limited to the amount they commit to pay for the shares when first issued.)

### 2.7 Charities Act

Incorporation does mean on-going professional fees related to the maintenance of a company and its compliance with its filing requirements. However, regardless of the structure, there will be legal, accounting and auditing fees in any event, and the Charities Act imposes many similar filing and compliance requirements on charities, whether or not such charities are companies.

## 3 The Incorporation Process

To incorporate a company, documents containing certain information must be submitted to the CRO together with the incorporation fee.

The documents typically comprise the following:

- (i) Form A1;
- (ii) Form G5;
- (iii) Memorandum of Association; and
- (iv) Articles of Association.

### 3.1 Form A1

The Form A1 is a CRO form and is available for download from [www.cro.ie](http://www.cro.ie) [3].

The information required to properly complete the Form A1 includes:

Information	Comment
Company Name	The availability of a preferred company name needs to be confirmed by the CRO.
Principal Activity	Details of the principal activity of the company which must correspond with the principal object of the company as described in the memorandum of association.
Place of Activity	Address of the place or places in Ireland where the company proposes to carry on an activity.
Central Administration	Address of the place (in Ireland or elsewhere) where the central administration of the company will be carried on.

Registered Office	This address must be in Ireland and an address at which post is capable of being readily delivered by the postal service.
Directors	The name, address, occupation, nationality, date of birth and other directorships of each director. The minimum number of directors of an Irish company under Irish company law is two. However, in order to obtain a charitable tax exemption from the Revenue Commissioners, there must be a minimum of three directors, the majority of whom must be Irish resident.
Company Secretary	The name and address of the company secretary who may be one of the directors.
Members	If the company is going to register as a charity, the names and addresses of a minimum of three members should be inserted. These individuals will be required to sign the incorporation papers.
Statutory Declaration	One of the directors or the company secretary must swear a statutory declaration which forms part of the incorporation papers. The statutory declaration is to verify that the company will carry on an activity in Ireland and that the company has complied with the requirements of the Companies Act 2014 in respect of registration of the company.

### 3.2 Form G5

This is a CRO form and a copy is available for download from [www.cro.ie](http://www.cro.ie)[3].

This form is required if a company wishes to avail of the exemption to dispense with using the words “company limited by guarantee” in its name. The exemption is only available where:

(i)

the objects of the company are the promotion of commerce, art, science, education, religion or charity; and

(ii)

the following requirements are included in the company’s Memorandum or Articles of Association:

- the profits of the company (if any) or other income are required to be applied to the promotion of its objects;
- payment of distributions to its members is prohibited; and
- all the assets which would otherwise be available to its members are required to be transferred on its winding up to another company whose objects are the promotion of commerce, art, science, education, religion or charity and which company meets these requirements.

The Form G5 takes the form of a statutory declaration and must be signed by one of the directors or the company secretary.

### 3.3 Memorandum of Association

A company’s memorandum of association sets out the fundamental scope of its existence, capacity and activity. Company law prescribes clauses which must be contained in the memorandum of association of a company limited by guarantee including:

#### Name Clause

The name clause of a company sets out the name of the company in its entirety.

#### Company Limited by Guarantee

This clause states that the company is a company limited by guarantee.

#### Objects Clause

The objects clause of a company sets out the parameters of the permitted corporate activity of that company. The objects clause would ordinarily run to a number of sub-clauses to ensure that such parameters are as broad as possible, with the first clause detailing the company’s “principal object” and the subsequent clauses setting out the “subsidiary and ancillary objects” of the company.

For a company that is a charity, its objects must be written so that every object to which its income or property is applied is charitable. In addition, its principal object must be the prevention or relief of poverty or economic hardship, the advancement of education, the advancement of religion and/or any other purpose that is of benefit to the community.

#### Liability Clause

This clause provides that the liability of the members of the company is limited.

#### Winding Up Clause

This clause provides that upon the winding up of a company, the members shall contribute certain amounts not exceeding the limit of liability specified.

### 3.4 Articles of Association

A company’s articles of association are the internal rules or regulations of the company and govern relations between the company and its members and between the members as and amongst themselves. The articles of association, together with the memorandum of association are, in effect, the constitution of the company.

The form of articles of association for a company limited by guarantee is set out in Schedule 10 of the Companies Act 2014. This provides for a “one-page constitution”. However, for the purposes of clarity and transparency, particularly for companies that are charities, it is worthwhile considering adopting articles of association that clearly set out the rules that govern a company.

The articles of association of a company will usually include “rules” to deal with the following areas:

- (i) Identification/appointment of members;
- (ii) Meetings of members;
- (iii) The board of directors;
- (iv) Appointment of the board of directors;
- (v) Proceedings of the board of directors;
- (vi) Other “rules”, relating to matters including:
  - (vii) the secretary of the company;
  - (viii) the use of the company seal;
  - (ix) the requirement to keep proper books of account;
  - (x) the appointment of auditors; and
  - (xi) the service of notices to members.

#### **4 Conclusion**

If you would like any further information in relation to establishing a company, particularly a company that carries out charitable activities, we would be happy to provide you with assistance.

MASON HAYES & CURRAN

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#### **Links:**

- [1] <http://knowledgenet.carmichaelcentre.ie/contributor/alice-murphy>
- [2] <http://knowledgenet.carmichaelcentre.ie/printpdf/479>
- [3] <http://www.cro.ie/>