Introduction

This trading form is used across the third sector and is applicable to charities, community projects, clubs, and societies. Most are not-for-profit companies, that is, they do not distribute their profits to their members but retain them within the company or use them for some other purpose. Unlike companies limited by shares, the need to define what happens to the profit or surplus of the company and to make provision for the distribution of assets in the event of the company being wound up by the members, means the Articles of Association need to be drawn up to meet this specific need. Because of this, I would strongly advise against purchasing a Company Limited by Guarantee off the peg.

The Advantage of a Guarantee Company

The main reason for a charity, community project, etc., to be a company limited by guarantee is to protect the people running the company from personal liability for the company's debts, just as a business may be set up as a company limited by shares for the same reason.

If a charity, community project, club, etc. is not registered as a limited company, then the people running it (typically the management committee, etc.) can be made personally liable for its unpaid debts. This can be a real risk. Some charities, community groups, sports clubs, etc. can be substantial enterprises, with liabilities that cannot easily be turned off. They may have leasehold premises, employ people, have equipment on finance contracts, etc. If the income does not meet these outgoings, the charity, etc. may become insolvent, and the people running it (though not usually the members at large who are not on the committee) can be made personally liable for the shortfall. This can happen because of unforeseen and unfortunate circumstances, such as the sudden withdrawal of financial support from a body such as the local authority.

With a company, on the other hand, the company itself is a separate legal entity and it, not the people who own or run it, is liable for its debts. In a company limited by shares, the shareholders' liability is limited to the amount the shareholder has agreed to pay for his or her shares. In a company limited by guarantee, the liability is limited to the amount of the guarantee set out in the company's articles, which is typically just £1.
In both a company limited by shares and one limited by guarantee, the people running the company (the directors) will only incur any personal liability for the company's debts if they have been guilty of some wrongdoing, such as wrongful or fraudulent trading.

What is different about a guarantee company?

A company limited by guarantee is much like an ordinary private company limited by shares. It is registered at Companies House, must register its accounts and an annual return each year, has directors, etc. A major difference is that it does not have a share capital or any shareholders, but members who control it.

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Members, not shareholders
In a company limited by guarantee there are no shareholders, but the company must have one or more members. Subject to any special provisions in the company's articles, the members will be entitled to AGMs and vote, and in most companies that means they can appoint and remove the directors and have ultimate control over the company.

The members meet at the Annual General Meeting and elect a committee to manage the club on their behalf, and subject to the rules in the club's constitution. If the club is a company, the same rules will apply and will be set out in the company's articles. By and large, the company law provisions relating to general meetings, resolutions, etc. in ordinary share companies apply to companies limited by guarantee.

Just as in a company limited by shares there may be different classes of share; it is possible to have different classes of members in a guaranteed company. There may be non-voting members, for example, or members who have restricted rights in some other way. In a sports club, for example, there may be junior members (those under a certain age) who cannot vote, or social members, who pay a lower subscription but are unable to use the sports facilities.

Directors
A company limited by guarantee, as a private company, must have at least one director. Most guaranteed companies have several. The directors may be given some other title, such as committee, management committee, board of managers, trustees, governors, etc. Whatever title they may be given, if they are in day-to-day control of the company, they are in law directors of that company. Their powers will depend on the terms of that company's articles, but typically they are given very wide powers of management. Just as in a company limited by shares, these powers are conferred on the directors collectively, when they are sitting as a board and passing resolutions for the management of the company. They may, of course, set up sub-committees, etc. and delegate powers to them, and may give directors special responsibilities, such as treasurer, membership secretary, etc.

In some companies, some or even all the directors may be appointed by one or more outside bodies, such as charities or local authorities who are backing the project. Some directors may be elected by particular interest groups.

No share capital
The fact that a company limited by guarantee cannot have share capital limits its fund-raising capacity, simply because it cannot issue shares to those who back it and join it. For this reason, some projects that are not essentially profit-motivated are set up as companies limited by shares. Many such companies impose subscriptions and/or a joining fee. A guaranteed company can borrow money and may issue debentures or debenture stock.

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As there are no shareholders, it is not possible to own a company limited by guarantee in the way that a company with share capital is owned by its shareholders. The members of the guaranteed company control it, in the same way as shareholders control a share company, but they do not have any shares or other security in the company that they can sell to another.

Debentures

A document that either creates a debt or acknowledges it, and it is a debt without collateral. In corporate finance, the term is used for a medium- to long-term debt instrument used by large companies to borrow money.

In some countries the term is used interchangeably with bond, loan stock or note. A debenture is thus like a certificate of loan or a loan bond evidencing the fact that the company is liable to pay a specified amount with interest and although the money raised by the debentures becomes a part of the company's capital structure, it does not become share capital.[1] Senior debentures get paid before subordinate debentures, and there are varying rates of risk and payoff for these categories. Debentures are generally freely transferable by the debenture holder. Debenture holders have no rights to vote in the company's general meetings of shareholders, but they may have separate meetings or votes e.g., on changes to the rights attached to the debentures. The interest paid to them is a charge against profit in the company's financial statements.

Not for profit

A company limited by guarantee is not prohibited from distributing its profits by the Companies Act or any other law, but it is commonplace for restrictions to be put on profit distribution in the company's articles. Such restrictions will usually apply both to profits while the company is running and to the distribution of assets (after paying creditors) when the company is wound up. In many cases, but by no means all, these restrictions are reinforced by a prohibition on any payment of salaries or fees to the directors.

Exemption from having 'Limited' at the end of the name

A not-for-profit company limited by guarantee can be exempted from having the word 'Limited' (or 'Ltd') at the end of its name if it is set up for certain objects. These are the promotion of commerce, art, science, education, religion, charity or any profession.

Charities

A charity need not be a company, but can be set up with a trust deed, when it will be an unincorporated association. In England and Wales, charities (other than very small ones) are registered with the Charity Commission, who have regulated powers over them. If limited liability is sought, the body would have to be registered both as a charity and as a company limited by guarantee, and certain provisions (such as the restrictions on profit distribution mentioned above) must be included in the memorandum and articles. A charity will need its articles to be drafted specially, and this is the main specialised work in setting one up.

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Community Interest Companies (CICs)
A CIC is one formed for the benefit of the community. The two main features are the asset lock and the Community Interest Statement and Report. Under the asset lock provisions, the assets and profits must be permanently retained within the CIC, and used solely for community benefit, or transferred to another organisation which itself has an asset lock, such as a charity or another CIC. With every application to form a CIC, a Community Interest Statement must be lodged. This must certify that the company is formed to serve the community rather than private profit motives and must describe the activities of the CIC.

A CIC may be limited by shares or guarantee. They cannot be registered electronically as each company has to be vetted by the CIC Regulator.

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