



Membership organisations - governance issues

Many charities and not-for-profits are large membership organisations with several thousand members, which have particular problems in respect of their governance.

Size of trustee body. Some membership charities, notably agricultural societies, have very large governing boards or councils, with over sixty or seventy trustees, where it is likely that the role and responsibilities of a trustee are not properly understood and are confused with the position of a member.

Representation of members. Some organisations try to allow for this by having a board of trustees/directors who are elected by the sections or geographical regions of the organisation. The problem is that the Board is then trying to combine the functions of membership representation with the responsibilities of a trustee/director body, so that neither role is performed effectively.

Two-tier structure. One way to resolve this, and the problem of large trustee boards, is to separate the roles of membership representation and governance by the trustees. The trustee body could be reduced to, say, 7-12 trustees, joined at meetings by the chief executive and other senior staff. The trustees will work with senior management to create strategy, fix budgets, recruit staff and make key decisions, preserving the distinction between governance and management.

A separate body, perhaps called a Council of Members or Members' Forum, would represent the members, who at the AGM can elect any number of representatives to sit on the Council, say, from 15 to 50 individuals. This would allow for regional or sectional representation of the membership.

The Council would select and appoint the trustees from its number, and have the power to hold them to account and to dismiss them. The Council would perform a monitoring role without also carrying the legal responsibilities – and liabilities – of charity trustees and company directors.

The Council members can take on specific non-governance roles, such as the organisation of events or sitting on committees advising on special matters. The Council would form a bridge between the large membership of the organisation and the small trustee body, or Board. Such a Council of Members might wish to meet, say, two or three times a year.

This two-tier model may be a suitable one for many charities and not-for-profits and is one which has recently been adopted by the National Trust. The smaller body of trustees

could also undertake the type of induction and training programme recommended by the Charity Commission for trustees/directors, to achieve the high standard of governance which is necessary to take any organisation forward.

Nominated directors. Where some or all of the directors are nominated by sections or regions of the membership, there may be an expectation that the director will act on the instructions of the members who appointed him. However, under charity law all trustees must act independently and not allow themselves to be controlled by any third party. Such trustees must act in the best interests of the charity as a whole and not as mere representatives for the interests of the body or persons who appointed them to their role as charity trustee.

The same principle applies under company law to the directors of corporate not-for-profits. Their first duty is to the organisation itself regardless of who appointed them.

Classes of Membership. An organisation may wish to enlarge its membership to obtain support for its objects from new sources and also to generate further income by way of subscriptions.

However, such an extension of membership could lead to problems if the “one member, one vote” rule is preserved, in that control of the organisation could be taken over by lobby groups or special interests, who could pass an ordinary resolution to remove some or all of the Board under the Companies Act 1985.

It is increasingly common for large membership organisations, in the charitable and non-charitable/not-for-profit sector, to introduce a new class of non-voting “Associate Members”. This involves the recruitment as members of individuals or bodies who support the objectives of the organisation but do not necessarily want to exercise voting rights, or to have a role in determining its governance, constitution and direction.

“Full Members” paying a higher subscription would be entitled to voting rights and other special benefits. There could be formal events or members' meetings which give non-voting members a forum and the opportunity for some input in respect of the activities of the organisation.

Criteria for admission as members. Membership of charities should in theory be open to all, to meet the public benefit test, but it is permissible to have some limiting

criteria, such as residence in a particular area or observance of a particular faith.

The membership criteria for both charities and not-for-profits should be clear, objective and non-discriminatory. If admission is controlled by the directors, then the purpose of the directors' approval should be merely to establish whether or not a particular applicant fulfils the published admission criteria. The directors should exercise the power to admit members in good faith and in the interests of the organisation as a whole, not just to protect the interests of one section of the membership.

Where membership of a non-charitable/not-for-profit association is in practice, if not in law, required in order to participate in a commercial activity, the criteria for admission will be subject to competition law. If an association has a wide membership within a particular commercial sector, there is a greater risk that its activities will contravene competition law if a large proportion of market participants are excluded.

Quorum provisions. These may need to be reviewed if there is an expansion either in the number of members who hold voting rights or in the non-voting membership. A person or body must be entitled to vote in order to be counted in a quorum. If a single member holds more than one vote, its representative is still only counted as one person for the purposes of the quorum.

A minimum of at least 50% of members would be a high quorum for any membership organisation. A meeting which is inquorate cannot pass valid resolutions. If a quorum is too low, it could allow an organisation to be taken over by a dissident and active minority.

We recently attended the EGM of a membership organisation with over 2000 individual and corporate members. The EGM was convened to pass a special resolution to amend the constitution, but only six members attended, one of whom represented two organisations, so just achieving the quorum of seven.

A quorum could be set at a fixed number of members, or a percentage such as 20% of the voting members, whichever is the greater.

Weighted voting rights. Instead of the normal "one member, one vote" rule, some not-for-profits confer weighted voting rights on a certain class of members, or to reflect different financial contributions made by members, or the size and value of property units held by them. Sometimes a member is given enhanced rights on particular resolutions, although care should be taken in the context of resolutions to amend the articles, where such provisions may be invalid under company law.

"Non-distribution" clauses. The phrase "not-for-profit" frequently causes confusion as many not-for-profit companies are intended to generate profits and indeed often make very large profits. The phrase instead means that any profit that is produced is not distributed as a dividend to members but instead applied for the purposes of the company.

"Non-distribution" clauses are compulsory for charities but also normal for non-charitable, not-for-profit companies, to prohibit the distribution of income and capital profits to their members. Such "asset lock" provisions usually also include a dissolution clause which provides that any surplus assets on a winding up of the company should be transferred to another organisation with similar objects or to a charity, and not distributed to the members of the company at the time of winding up.

The inclusion of such non-distribution clauses in a company's memorandum makes it clear to members that the purpose of membership is not to make a personal profit for themselves but rather to support the public benefit, social enterprise or community purposes set out in the company's objects. Its members control the company but do not have ownership rights in it.

The inclusion of non-distribution clauses is also required if a company wishes to omit the word "Limited" from its name under s.30 Companies Act 1985.

Some so-called "not-for-profit" organisations may specify that none of the members are entitled to any dividend on profits but they can with the approval of a 75% extraordinary resolution of the company have a share in the surplus assets of the company on winding up. This right for members to participate in a division of surplus assets does not accord with the status of a not-for-profit company.

Such provisions can also be difficult to apply. In 2001 former members of the RAC claimed in a court case that they should have been notified of the proposals for demutualisation of the RAC and the sale of its motoring services business, as in ignorance of the proposals they had allowed their membership to lapse, and so been denied the chance to share in the windfall profits received by members on the RAC register at the time of the sale. (*Peskin and Milner v. Anderson and others* [2001] BCC 874.) The claimants failed in that case - but former members of an organisation who could not share in a division of assets on a winding up might still challenge the process. Voluntary winding ups can occur on the reconstruction or amalgamation of a company.

Alteration of Articles. Charitable and non-charitable companies can usually alter their Articles of Association, including the provisions relating to its membership structure, pursuant to the power in s.9 Companies Act 1985. It would be necessary for a special resolution to be passed by a 75% majority of those members attending and voting at an AGM or EGM convened on proper notice.

The topics above are just some of the issues which need to be reviewed by membership organisations – we will be happy to advise further.

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