For BDCR General Meeting 25th November Nov 2018

Rules Change – Notes

A. **Introduction**

B. **Notes on specific new or changed Rules**

C. **The process**

D. **Converting to withdrawable shares – NOT included in this Rules change.**

A. Introduction

BDCR Directors have instigated these changes to our Rules for two main reasons:

(a) To make our environmental purpose explicit in the Rules. When in 2014 our 'bona fide co-operative' status was challenged by our regulator, the Financial Conduct Authority (the FCA), it was realised that although our environmental purpose was clear in our original share prospectuses, it was not explicit in our Rules.

(b) To ensure that the Rules are completely up-to-date. In particular, the existing Rules were adopted before the Co-operative and Community Benefit Societies Act 2014 came into force, so there were archaic references to the previous Industrial and Provident Societies legislation. There are also some new requirements inserted by the FCA for Registered Societies such as ourselves, and these are included in the notes below. The one that most affects Members is the FCA requirement that the responsibility for deciding on share interest rests with the Directors, not the Membership as a whole (see Rule 102 below).

B. Notes on specific clauses:

Purpose (Rule 4) : We have inserted the extra element (b) to make our environmental purpose explicit:

> The purpose of the Co-operative is to:
>
> (a) carry out its function as a co-operative and to abide by the internationally recognised co-operative values and principles of co-operative identity as defined by the International Co-operative Alliance;
>
> (b) pursue the objects stated in rule 5 as measures to reduce dependency on fossil fuels resources and thereby counteract the effects of climate change
>
> This rule may only be amended by an Extraordinary Resolution.

Of the new requirements introduced by the FCA, the following one is the one that most needs to be noted by Members:

Share interest (Rule 102):

An FCA requirement has removed the payment of share interest from the 'Application of Profits' clause (Rule 103) into a separate clause. This is because they regard share interest as a 'cost of capital', to be decided by Directors, not an item such as donations and dividends which can be made out of annual profits and decided by Members at the AGM.

The BDCR Directors both agree with and welcome this explicit clarification of their fiduciary responsibility. The setting of the interest rate is a decision made in light of many financial factors (necessary long and short-term reserves, budgeted plans, need to retain capital etc.) and is not directly or solely related to annual profits.

To date, BDCR Members have always been given the opportunity at the AGM to vote to approve the Share Interest rate 'recommended' by Directors. This is in fact the procedure described in the 2004 BDCR Share Prospectus. **Members need to note that the FCA's position supersedes the information in the original BDCR share prospectuses, and that in future the interest rate will not be an AGM agenda item requiring approval of Members.**

For the avoidance of any doubt or confusion the Directors asked for written confirmation of this understanding from Co-ops UK and this is their response:

> **Co-ops UK written response on Members Voting on Share Interest**
>
> **From Linda Barlow, Co-operative Governance Advisor, 20/6/18**
>
> *'With regard to your query on share interest, it is the FCA's view that payment of share interest is a cost of capital and not a distribution of profit see section 6.23 of the FCA's registration guidance. As such, it would be expected for the Board to determine, and not the members, how much interest is payable in advance of the period for which it is intended to be paid and is one of the criteria by which the society can demonstrate how the society is meeting its condition for registration. (para 6.25).'*

For reference, the FCA's registration guidance is online at:
https://www.fca.org.uk/publication/finalised-guidance/fg15-12.pdf

Other new clauses inserted by the FCA are:

14 Where it states that, as Membership is voluntary, it cannot be a condition of employment for anyone employed by the Society.

79 A technicality, on the Society acting beyond its powers (ultra vires). Explanation from Co-ops UK, with the summary in bold: *'we've had to add this in at the request at the FCA. Basically the Act sets out certain decisions that are required to be made by special resolution and then the Act defines what a special resolution means in that context. In this particular case, the provision is permitting members to pass a resolution to ratify an act of the Board that was outside of the powers of the society and then (if necessary) to pass a separate resolution to prevent the society to take action against the Board as a result of their directors duties.* ***In short, it is to protect third parties who are dealing with the society in good faith if it found that the contract a third party has with the society is invalid because the directors did not check if the society had the power to enter into it'.***

C. The Process

The proposed new Rules have been drawn up with support from the legal department at Co-ops UK to ensure that the Rules are compliant with FCA requirements. They are based on the Co-op UK's 'Model Rules' for a Registered Society which is a 'bona fide co-operative'

The procedure now is:
1) Members need to agree to new Rules at a General Meeting. (Extraordinary Resolution, requiring 75% vote, not simple majority).

Extraordinary Resolution
that the Rules of the Society be amended by deleting them in their entirety and substituting therefore the Rules provided **and** **that the Secretary be granted authority to make any administrative or unsubstantive changes required to enable the replacement Rules to be registered with the Financial Conduct Authority.**

2) Statutory Paperwork that (1) has happened.
3) Send to FCA for approval.

Co-ops UK will do all 2&3 with/for us.

Rules only take effect when agreed by the FCA.

D. Converting to withdrawable shares – NOT included in this Rules change.

There is one other area where the Directors had hoped to change the Rules, but cannot at present: BDCR shares are 'transferable' rather than 'withdrawable'. When the society was first formed, the Directors were led to believe that after 5 years the status of the shares could be converted from 'transferable' to 'withdrawable' by a change to the Rules, thus allowing the share capital and the membership to shrink if a decision was made to gradually wind down the project. This is mentioned in the original share prospectuses.

Investigations by the Directors in 2018 have revealed that this is an extremely complex issue, untested with the regulator. We have been advised that the FCA are likely to challenge anything which has the potential to undermine creditor protection. *Co-ops UK: ' to make the share capital withdrawable or redeemable could undermine creditor protections by providing shareholders a route to regaining their capital at the expense of creditors'.* As the withdrawing of shares is ALWAYS at the Directors discretion, it should be possible to have procedures which would prevent any withdrawal of shares except when there are sufficient funds to cover all creditors first. However as BDCR does not actually NEED shares to be withdrawable and we do not wish to risk the FCA rejecting this current Rules change due to this issue, the Directors have decided not to pursue this matter at the moment.

Sonia Kuznetsov, Director
Rachel Kennedy, Secretary