Community Energy England briefing. November 2024

Threat to community energy of the Law Commission's proposed reforms to the Co-operative and Community Benefit Societies Act 2014 (consultation)

The Law Commission review provides an opportunity – not taken up by the Law Commission – for Parliament both to modernise the law and to provide a suitable framework for growth.

A leading community energy co-op director has said, "These reforms pose a fundamental threat to community energy. Some of the sector's most vibrant organisations will be extinguished."

The government should ensure their and the Law Commissions aims are aligned. They should abolish the unnecessary distinction between Co-operatives and Community Benefit Societies.

This short paper examines:

What do the Law Commission reform proposals seek to do?

1. The Law Commission was tasked by the previous government to 'modernise' the law around co-operatives and "support a more proportionate and effective regulatory environment". 'Proportionate' to what or 'effective' for whom is not defined. Consequently there is no mention of the sector's huge potential contribution to carbon reduction and very little of the intended impact of the reforms on the sector, certainly not on helping it to grow. There are 219 pages and 87 questions but this briefing focuses on the proposed introduction into statute for the first time of a definition of co-operative and community benefit societies as these have the most

serious potential implications for the community energy sector. Numbers in brackets below eg (3.75) refer to paragraphs in the Consultation document.

What are the government's visions for co-operatives and the community energy sector?

2. The current government seeks to maximise economic growth and 'double the size of the co-operative economy'. It has pledged to *"deliver the biggest expansion of support for community-owned energy in history"* [Ed Miliband] offering up to £400m a year in low interest loans to communities to develop and build community-owned energy projects.
3. *"Community energy also reduces pressures on the transmission grid and the need for expensive investment, so community ownership will be critical."* It will also be crucial to *"saving families money and improving communities' energy security."* [Michael Shanks] and *"to help tackle fuel poverty, to unleash the dynamism and resources of local communities and to win the consent of local people."* [Ed Miliband].

4. The government understands the power and potential of supporting people and communities to take an active role in the net zero transition and has heeded the Climate Change Committee's warning that "if the people of the UK are not engaged in this challenge - the UK will not deliver Net Zero by 2050." In much of the rest of Europe (and beyond) the co-operative energy sector is a growing and vibrant part of the energy transition. In much of the UK it has stagnated over the last decade through previous government indifference and over-prescriptive approach by regulator. The government must empower the co-operative energy sector in any reform of co-operative regulation.

What do the Law Commission proposals contain?

5. The Law Commission has issued a 219 page consultation, with a deadline of 10 December 2024 for responses. The proposals for reform include:

    5.1. Defining "Co-operatives" and "Community Benefit Societies" (CBS) for the first time in legislation rather than in the Guidance of the Registrar.

    5.2. Continuing with the requirement that organisations will have to choose whether to be a co-operative or a CBS at the point of registration.

    5.3. Making any reform 'retrospective' so that existing societies will be forced to satisfy the requirements of the new definitions within 18 months. This will have a potentially disastrous impact on the existing renewable energy co-operatives and may force many of them to demutualise. It may force CBSs to dissolve and distribute their assets.

    5.4. Offering a limited option for "Green Energy Co-operatives"

5.5. Enshrining in law the Registrar's restrictive approach on what is a co-operative by limiting it to a business which trades with its members rather than taking a holistic approach to the co-operative principles, and ignoring other principles hitherto important to the existing worldwide co-operative ethos, namely:

5.5.1. 'One member one vote' (though this principle is endorsed)

5.5.2. Autonomy

5.5.3. Education

5.5.4. Co-operation

5.5.5. Concern for Community

Below we describe in more detail the situation for existing energy co-operatives and the Law Commission's proposals for 'Green Energy Cooperatives' and 'Community Benefits Societies':

Existing Energy Co-operatives:

7. The definition as proposed by the Law Commission of a co-operative will enshrine in statute wording which will make existing renewable energy co-operatives ineligible for re-registration as co-operatives. The current FCA Registrar has already forced the de-registration of one established and well run renewable electricity co-operative which adhered to the international co-operative principles. This was on the basis it could not sell electricity directly to its members and therefore was not a co-operative. This society converted into a company but remains recognised by Companies House as a co-operative. As a result it is not able to grow and expand its existing energy business due to the expense of and restrictions on companies raising money and issuing shares to the community through regulated share offers. This is the costly fate that we anticipate will await other energy co-operatives if the Law Commission proposals are implemented. It costs several thousand pounds to convert to a co-operative company. And to argue with the Registrar whether the society is satisfying the Registrar that the lawful activity which it conducts satisfies its interpretation of what a co-operative society is could be in the high tens of thousands of pounds - money which will be lost from business growth and for community benefit.

Green Energy Co-operatives

8. The consultation section 3.73 'Case study - green energy co-operatives' recognises that not being able to trade electricity directly with members presents problems and this is welcome. To overcome this it proposes various conditions in (3.74.) i.e. "First, members choose a green energy tariff. Second, for any surplus generated by the co-

operative, if the co-operative pays a member dividend, that dividend is calculated as a proportion of each member's energy consumption."

9. There are a number of objections to this proposal.

   9.1. It would penalise people who were tackling climate change and who had already reduced their consumption (by investing in energy efficiency and/or rooftop solar on their home, for instance) and might, perversely, incentivise and enable people to continue to consume more. Returns from an organisation dedicated to the community good of reducing energy consumption and emissions should not incentivise investors to do differently. Indeed we do not believe that members will be prepared to continue to invest on this basis.

   9.2. No renewable energy project produces electricity to match 100% of consumption. The supplier will still be drawing from other sources to ensure certainty of supply. A model that purports to cover 100% of a member's consumption is a purely financial arrangement without reference to what is actually produced.

10. Paragraph (3.76) of the Green Energy Co-operative' case study says, "Simply to put green energy into the national grid" is "laudable". It continues, "If that was the only characteristic of the society, we think it aligns more closely with a community benefit society." We would point out that it is very rare for that to be the sole ambition of a co-operative energy society. It may be (and often is) the first step or building block for future development, which may include such activities as energy saving/fuel poverty advice and remediation which often saves more carbon than the renewables but needs a source of funding which the renewables project can provide. This development will now be constrained or even prevented.

11. Members of societies cannot at present or as proposed derive any additional benefit from the successful operation of the CBS. So, a scheme to supply cheaper local energy to members (when that is made possible) would probably not be an activity compatible with being a CBS – that is the role of a co-op. However, although a co-op can convert into being a CBS a CBS cannot convert into a co-operative. This should be enabled if the co-operative has an asset lock. A charity can convert into a community interest company and if the co-operative has an asset lock then the community capital will be protected.

Community Benefit Societies:

12. The Law Commission's proposed definition is that a CBS must carry on a business 'for the sole benefit of the community'. 'Sole' is a new restriction but the purpose behind it and its likely impact is unclear. The Law Commission "provisionally agrees with the current approach of the FCA that the sole purpose of a Community Benefit Society

should be to benefit the community" and that funds raised by a CBS should not be applied for the benefit of private individuals and that benefits should not be contingent on membership. In other words, CBS's are supposed to not trade with their own members at a discount or give them any other form of preferential treatment.

13. Introducing the adjective 'sole' to the community benefit purpose of a CBS only adds ambiguity to this already unclear purpose as 'the community' is already ill defined. For example, is delivering fuel poverty alleviation to an individual in difficulties in the private rented sector a 'benefit to the community'? Or is it a private benefit to the individual in question or even to their landlord who can then justify raising the rent on the improved property (as has happened in practice). In the case of a street based heating scheme there may not always be a poverty alleviation aspect but it might fall under a climate reduction benefit for the community which appears to be acceptable. However the uncertainty is not helpful.

14. The FCA has also refused to accept that it is an acceptable activity for a CBS with solar panels on the roof of a supermarket to sell the electricity generated to the supermarket. According to the FCA this constituted a private benefit to that supermarket. This was regardless of whether the supermarket was a member of the CBS or not. However selling electricity to an electricity supply company is deemed by the FCA to be a permissible activity for a CBS. Are the reforms and the government's plans compatible?

Are the reforms and the government's plans compatible?

15. Restricting energy co-operatives as proposed by the Law Commission will damage the government's growth mission both for the mutual sector and for community energy and its mission to decarbonise the power system by 2030 while sharing ownership and benefits more widely.

16. The scale of growth required by the government targets of 8GW of municipal and community energy by 2030 will not be achievable if the sector is restricted to operating mainly under the CBS rules as these reforms envisage.

17. The Law Commissions reforms must be 'proportionate' to the societal challenges that co-ops are uniquely well placed to address. To be 'effective' they must accommodate and encourage future growth and adaptation to changing conditions.

18. A leading community energy co-op director has said, *"These reforms pose a fundamental threat to community energy. Some of the sector's most vibrant organisations will be extinguished."*

19. Thankfully the consultation notes *"It is for Government to decide whether to accept our recommendations."*

What are the impacts of the proposed reform on community energy organisations?

20. We welcome the proposal to continue the relatively light touch regulation for co-operatives and CBSs, leaving control to members. However regulation of energy co-operatives is anomalous and will seriously hamper the growth of the sector. The reforms must resolve this.

21. It is helpful to have a modernisation and clarification of the law. However this aspect of the proposals will have negative effects that will greatly outweigh any benefit. Additionally the proposed retrospective nature of the changes are a cause for concern and are expected to impact on some existing funding arrangements and longer term contracts

    The proposals will:

    21.1. stifle growth in community energy if organisations cannot set up as co-operatives and trade as a business.

    21.2. reduce the ability of the sector to innovate and evolve, if the definition of what a co-operative (and CBS) can do is further restricted and continues to insist on some form of direct or indirect trading of energy. This is particularly the case in the energy sector which is going through a process of radical technological and social change, in addition to the considerable changes being brought about by digitalisation and "sharing".

    21.3. need to be legislated by Parliament and this can take many years, creating long-term uncertainty and instability for projects and investors.

What are the potential future impacts of the proposed reforms?

22. The existing interpretation of the co-operative regulations prevent community energy organisations that want to function as businesses directed co-operatively by their members from registering as member co-operatives due to the difficulty of trading energy in the UK. Many of our most dynamic organisations are just such organisations - not investment vehicles for those "seeking a return on an investment" (3.75) Yet, since 2015, these dynamic businesses have not been able to register as member co-operatives.

23. The many uncertainties and the various limits placed on CBSs will prevent CBSs operating in the energy sector from taking full advantage of future developments that will be necessary for the sector to grow. This will thwart government ambition to "deliver the biggest expansion of support for community-owned energy in history". It will also prevent existing CBSs engaging in local trading to meet the government's goals outlined in 3. above: "*reducing pressures on the transmission grid and the need for expensive investment,"* by flexibly balancing local supply and

demand; "*saving families money and improving communities' energy security*". and *"tackling fuel poverty"* by supplying cheaper, clean power to local residents. All these projects *"unleash the dynamism and resources of local communities and [help] to win the consent of local people"* without which, as the Climate Change Committee warns, we will not achieve net zero.

24. Making the reforms retrospective will damage existing co-operatives and CBSs, making many unviable and putting them in contravention of their previous share offers.

25. If the activities of a CBS cannot function under the new definition it will be liable to be dissolved and its assets distributed.

26. It could remove investor, lenders and contract counterparty certainty and damage confidence in the sector, thus further hampering its ability to grow. This is particularly the case with new energy infrastructure where arrangements are necessarily very long term. There are already reports from members of potential infrastructure partners raising concerns.

What needs to happen?

The government should:

1. Instruct the Law Commission Review to ensure they are seeking to achieve outcomes compatible with government policy and goals by delivering a framework that would enable the sector to thrive.
2. Abolish the co-operative/CBS distinction, introduced in 1939 to prevent share pushing, (given that share pushing is now effectively prevented by regulation). The distinction is not made anywhere else in Europe. Co-ops UK also recommends this course of action.
3. Substitute a single new broader statutory definition of a mutual organisation that enshrines the spirit of the ICA Seven Principles and would accommodate a greater range of participants, each deciding for themselves how best to operate. A more balanced view of compliance with the principles should be adopted - as occurs at Companies House - not the present FCA (and proposed Law Commission) approach of focussing on one aspect within the principles and ignoring the rest. No one principle – member trading – should be elevated above another and it should be accepted that not every detail of every principle must be met. The Seven Principles indicate with a broad brush a direction and an approach to doing business in a co-operative manner.
4. If the co-operative/CBS distinction remains, allow community energy organisations to register as member co-operatives if the new restrictions prevent or may prevent them from delivering their business model, such as supplying electricity locally to members.

5. Allow CBSs to convert to co-operatives if their business model necessitates it e.g. supplying electricity locally to members and the co-operative has an entrenched asset lock to protect any community asset created in the CBS.
6. Not make any reform retrospective as this would be too disruptive to the existing co-operative and CBS sector. Retrospection cuts across established legal principles of precedent. It is not generally done in other reforms. It was not done when the present distinction between co-operatives and CBS was brought in: pre-existing organisations could continue to operate in line with then law. The uncertainty on what changes would be made would make funding difficult and cause issues when entering into contracts such as joint ventures. If a retrospective approach is taken it could cost a society many thousands of pounds as it seeks to argue with a Registrar taking a very narrow approach, as at present, to the definitions of a co-operative and community benefit society.
7. Require the Registrar to adopt an approach to the discharge of its functions which is based on good regulatory practice - that is an approach having regard to:
    a. the likely impact on those who may be affected by the discharge of those functions
    b. whether it advances or has a deleterious effect on Government policy
    c. the outcome of consultations with societies, with organisations representing societies and others with relevant experience
8. Allow discretion within permissive bounds to future Registrars to enable the sector to propose innovations and adapt to changing circumstances in accordance with Government policy.
9. It is vital that the capital intensive community energy organisations can continue to operate as mutual societies. Regulated share offers would be prohibitively expensive and would rule out most activities and prevent the sector growing at all.

Contact

Duncan Law Head of Policy and Advocacy, Community Energy England

d.law@communityenergyengland.org 07958 635181

About Community Energy England

Community Energy England (CEE) was established in 2014 to provide a voice for the community energy sector, primarily in England. Membership totals more than 300 organisations mostly community energy businesses, but membership extends across a wide range of organisations that work with and support the community energy sector.
www.communityenergyengland.org