

CO-OPERATIVES UK

**Community
Shares**



**AMANAH
ADVISORS**

Global Islamic Finance
& Fintech Services

A Guide to Shariah Compliant Community Shares

Background to Community Shares

Community shares are a popular approach to raising finance in which ordinary people and organisations can invest and become co-owners of vital enterprises – from swimming pools to shops, community housing to heritage buildings. It is a form of investment unique to co-operative and community benefit societies and has been utilised successfully across the UK.

Ten years ago, community shares were almost unheard of. Yet since 2012, £200 million has been raised by more than 126,000 people supporting more than 670 vital businesses – an impressive 92% of which are still trading. Co-operatives UK, through the Community Shares Unit and Booster Fund, have been at the forefront of this rise in community owned business made possible by community shares.

Community shares are particularly appealing as they offer a flexible and patient form of equity investment that is different to loans and grants. They help directly connect money in communities to projects that really matter to people.

You can read more about community shares here: www.communityshares.org.uk

Background to the project

In 2020, The Booster Fund grant funded some specific advisory work for Bradford Community Energy on whether they could certify their live community share offer as Shariah compliant to appeal more broadly and be accountable to the Muslim communities in their community of benefit.

This advisory work was delivered by Mufti Faraz Adam at Amanah Advisors who provided a comprehensive Shariah compliance review of their governance and business model. Amanah Advisors is an independent, globally recognised Shariah advisory firm based in Leicester. They take a holistic and ethical approach to enabling Shariah compliant finance solutions.

It was found that the community share offer as it stood was not quite Shariah compliant, but the process itself was enlightening for both Co-operatives UK and Amanah Advisors.

This opened conversations on how community shares and the society model they are based on had real potential to become a Shariah compliant method for community-based, co-operative, and other social

sector organisations to raise flexible, ethical finance. Most mainstream social investment options are variations of debt finance¹ which for the most part is not Shariah compliant, therefore excluding Muslim communities from accessing this type of finance. It was theorised that community shares represents an alternate form of social investment that could be made available to organisations working in Muslim communities in the UK.

In 2021, Co-operatives UK and Amanah Advisors successfully applied to the Connect Fund under their Equality and Diversity programme for funding to explore this concept further. The Connect Fund is managed by Barrow Cadbury Trust in partnership with Access – The Foundation for Social Investment.

As part of the project, detailed analysis of the community shares model and Co-operatives UK Model Rules have been undertaken and revised models developed and approved by the Financial Conduct Authority to enable Shariah Compliant Community Share Offers to work in principle. This guidance and associated materials are an outcome from this work, detailing the provisions required within the model to ensure Shariah compliance and where the model would be applicable.

Overview of the guidance

This guidance is designed for practitioners and advisers working with groups in Muslim communities in the UK who are interested in using the community shares model to raise finance and take collective or community ownership of businesses and assets.

This detailed registration guidance is designed to sit alongside the new Shariah compliant model rules for a Community Benefit Society and a Multi-stakeholder Co-operative Society which have been registered by Co-operatives UK as a Sponsoring Body.

There is a model description sheet for each society model, a full breakdown of any rules which have been amended to be made Shariah compliant with notes on any subsequent considerations for the business or governance model.

Any questions on this guidance should be directed to isla.mcculloch@uk.coop.

¹ There are creative examples of Shariah compliant social investment options, but these sit outside the mainstream.

Shariah Compliant Co-operative and Community Benefit Society Model Description Sheets

Co-operatives UK Multi-stakeholder Co-operative Society (Shariah Compliant Model)

<p>General description</p>	<p>A Multi-stakeholder co-operative registered under the Co-operative and Community Benefit Societies Act 2014 (CCBSA 2014) as a <i>bona fide cooperative</i>.</p> <p>This model will be suitable for an organisation which is owned and controlled democratically by a variety of stakeholders, that wish to work together to achieve their shared interests. Multistakeholder co-operatives may engage in any trading activity as long as this is Shariah Compliant. For the full list of compliant trading activities see the detailed registration guidance below.</p> <p>The model allows for members to invest in the co-operative through the purchase of shares but no interest can be paid on those shares.</p> <p>Any investor members will be eligible for a dividend payment based on an equitable distribution of surplus, this cannot be based on a percentage of the original capital invested and not necessarily linked to their transactions with the co-operative society.</p>
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<p>Key constitutional features</p>	<ul style="list-style-type: none"> • This model includes options to enable a choice of membership categories based on their role in the co-operative. • One member, one vote. • The co-operative's governing body is called "the Board of Directors". • Directors are elected annually by and from the membership.
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	<ul style="list-style-type: none"> • This model provides options to include a <i>common ownership</i> or <i>co-ownership</i> dissolution clause.
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<p>Details of provisions in model</p>	<ul style="list-style-type: none"> • Membership Any individual or organisation which supports the objectives of the co-operative and who meets the membership criteria chosen from the options listed in the model may apply for membership. Acceptance is at the discretion of the Board. As a multi-stakeholder model, the society can choose different categories of members: e.g. investor members, community members, worker members etc. This can be decided at the point of registration. This model can still be used with one category of membership. • Share Capital. Individuals can join as members by purchasing a £1 share in the co-operative. This nominal share is a membership share and is donated back to the society and cancelled when a member leaves. From a Shariah perspective, this is treated as a one off membership fee, not as a share. These terms must be agreed between the society and the member at the point of application. • Share offer. The society may choose to raise capital through an offer of shares. Members may choose to purchase additional shares in the co-operative up to the statutory limit (currently £100,000 per member). Members that are societies can invest more than the £100,000 limit. Members can normally withdraw their share capital by giving 3 months' notice, but the Board has the power to suspend this right if the co-operative needs to maintain its capital for a particular period, or does not have sufficient trading reserves to fund capital withdrawals. The shares can be reduced in value in line with the Society's Rules but cannot increase in value. Interest cannot be paid on these shares. • Directors must be aged 18 years or over. This may be changed on request. • Officers. Directors elect from amongst their own number a chairperson and Secretary, and any other officers they wish. • Profits. Additional shares are governed by the rules of Musharakah, therefore the profit distribution should not be based on transactions with the co-op or be a percentage of capital invested but should be distributed equitably amongst the members. Some or all of the profits may be retained within the co-operative as a
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	<p>general reserve, or members may decide to make payments for social or charitable purposes that are also Shariah compliant.</p> <ul style="list-style-type: none"> • Disputes between members are to be referred to an independent arbitrator for a ruling. <p>A co-ownership dissolution clause is preferred to be aligned with Shariah compliance but the common ownership dissolution clause is also compliant with consent from the members.</p> <p>Co-ownership dissolution clause. If the co-operative is wound up when solvent, its remaining assets may be distributed amongst all those who have been members of the co-operative during the preceding six years, in proportion to each person's contribution to the business of the co-operative.</p> <p>Common ownership dissolution clause. If the co-operative should be wound up by its members when solvent, then the members cannot share out its remaining assets amongst themselves. Any such assets must be passed on to other organisation(s) whose purpose is to promote and support the co-operative movement and common ownership enterprises.</p> <p>Members of a common ownership co-operative are thus not beneficial owners of the business in the normal sense; rather they are stewards of the co-operative, looking after it on behalf of past and future members as well as themselves. For Shariah compliance, the members must agree up front to distribute and donate any residual assets.</p>
Tax relief	<ul style="list-style-type: none"> • Tax relief may be available for individual investors who have invested shares in the society. Eligibility for tax relief will be dependent on the business model of the society and tax position of the investor member as usual. There are no Shariah related issues with using tax relief to incentivise investment.

Technical data	<ul style="list-style-type: none"> • <i>Relevant legislation:</i> Co-operative and Community Benefit Societies Act 2014 • <i>Registered by:</i> the Financial Conduct Authority • <i>Corporate status:</i> a corporate body with limited liability for members. • <i>Charitable status:</i> this model would not qualify for charitable status.
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Co-operatives UK Community Benefit Society (Shariah Compliant Model)

<p>General description</p>	<p>A community organisation registered under the Co-operative and Community Benefit Societies Act 2014 as a Community Benefit Society.</p> <p>The Shariah Compliant Community Benefit Society model cannot offer interest on shares and cannot distribute dividends. This should be considered more applicable for a society where collective, community ownership of an asset or business is the primary motivation for the community share offer.</p> <p>The successful running of the business for community benefit would be the incentive for investment rather than any financial return on investment. This could be a community multi-purpose hub type facility, learning centre, creative space or retail outlet. The society must take consideration of the Shariah compliant trading activities as below when registering. The community which the society intends to benefit will commonly be a geographically defined community, but it may instead be a community of interest.</p> <p><i>Co-operatives UK also has a Charitable Community Benefit Society model which may be more applicable depending on the activities being proposed. The Shariah compliant amends made to the CBS model are transferable to the Charitable model if required.</i></p>
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<p>Key constitutional features</p>	<ul style="list-style-type: none"> • Open membership. • One member, one vote. • The society's governing body is called "the Board of Directors". • Directors are elected annually by and from the membership. • Profits and any residual assets cannot be distributed amongst the members.
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<p>Details of provisions in model</p>	<ul style="list-style-type: none"> • Membership. Any individual or organisation which supports the objectives of the society may apply for membership. Acceptance is at the discretion of the Board.
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	<ul style="list-style-type: none"> • Share Capital. Individuals can join as members by purchasing a £1 share in the co-operative. This nominal share is a membership share and is donated back to the society and cancelled when a member leaves. From a Shariah perspective, this is treated as a one off membership fee, not as a share. These terms must be agreed between the society and the member at the point of application. • Share offer. The society may choose to raise capital through an offer of shares. Members may choose to purchase additional shares in the co-operative up to the statutory limit (currently £100,000 per member). Members that are societies can invest more than the £100,000 limit. Members can normally withdraw their share capital by giving 3 months’ notice, but the Board has the power to suspend this right if the co-operative needs to maintain its capital for a particular period, or does not have sufficient trading reserves to fund capital withdrawals. The shares can be reduced in value in line with the Society’s Rules but cannot increase in value. Interest cannot be paid on these shares. • Interest may not be paid on shares in this Shariah Compliant model. • Directors must be aged 18 years or over. This may be changed on request. <p>Charitable model: no employee of the society may serve on the Board.</p> <ul style="list-style-type: none"> • Officers. Directors elect from amongst their own number a chairperson and Secretary, and any other officers they wish. • Disputes between members are to be referred to an independent arbitrator for a ruling. • Dissolution <p>The model provides for 2 options for dissolution:</p> <p>Asset Lock</p> <p>The model provides an option for the inclusion of an asset lock. An asset lock places certain restrictions on the distribution of the society’s profits to the members as well as restrictions on the distribution (or dividing) assets of the society to (or between) members on winding up of the society, for example, by providing that the assets must be passed to a charity or another asset locked body.</p>
<p>Tax relief</p>	<ul style="list-style-type: none"> • Tax relief may be available for individual investors who have invested shares in the society. Eligibility for tax relief will be dependent on the business model of the society and tax position of the investor member as usual. There are no Shariah Compliant issues with using tax relief to incentivise investment.

Technical data	<ul style="list-style-type: none"> • <i>Governing statute:</i> Co-operative and Community Benefit Societies Act 2014 • <i>Registered by:</i> the Financial Conduct Authority • <i>Corporate status:</i> a corporate body with limited liability for members. • <i>Charitable status:</i> the charitable version of this model should prove suitable for the negotiation of "exempt charity" status with HMRC, provided its objectives and activities are charitable in law.
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Rules which have been amended to ensure Shariah Compliance

As a matter of course, we would expect these areas to be covered in the share offer document and business plan to ensure transparency on all aspects relating to Shariah compliance across all the documents.

A lot of the amends made apply across the Community Benefit Society and Multi-stakeholder Co-operative model so have not been separated out here to avoid duplication. Where there is a distinction, that has been indicated.

Objects

Objects and business activities must be aligned with Shariah principles. The business **cannot be** of the following nature. If there are any questions, further clarification must be sought.

- Alcohol dealers such as brewers, distillers, wineries, packagers, wholesalers, transporters, sellers including pubs, bars etc.
- Companies engaged in conventional interest-based financial services and conventional insurance companies
- Gambling platforms such as Lottery and casino operations, online gambling, gambling software developers, betting companies, gambling machine manufacturers, gambling promoters and marketers.
- Pork dealers such as Retailers, manufacturers and distributors of food products containing pork. Restaurants selling pork items. Business activities which involve breeding, rearing, slaughtering, processing, packaging pork products are considered non-compliant.
- Pornography and offensive content. Producers, promoters and marketers, publishers of all types of adult entertainment, explicit content etc. Businesses producing, printing, distributing or

marketing pornographic material are considered nonpermissible for investment. This could be over any media i.e. print, visual or audio. Content which is abusive/offensive is also considered non-permissible.

- Tobacco companies. Producers, processors, packagers, retailers of tobacco products. Businesses involved in growing, processing, packing, marketing and retailing of tobacco products are considered non-permissible. Companies involved in doing research on behalf of tobacco companies or funded by them are considered non-permissible too.
- Advertising of non-compliant products and services. Advertisers of pork, alcohol, gambling, tobacco and all other non-Islamic activities
- Producers, distributors, and broadcasters of music, movies, television shows, and musical radio shows

Borrowing

The Act requires a society's rules to reference borrowing but any borrowing must be done on Shariah compliant terms. This should be considered as part of the overall capital requirements of the society at an early stage as it may impact the decision to register using the Shariah compliant model.

Any borrowing must be Shariah compliant. The Rules stipulate that the rate of interest on any borrowing must not exceed 0% and the lender must not receive any conditional benefit. If the society is considering Shariah compliant borrowing as part of the capital raise, then they should work with relevant, certified lenders on this.

Investment of funds

Any investments made by the Society must be Shariah compliant in their own right. It is not unusual for societies who share their objects or aspirations in terms of community benefit. Care should already be undertaken in this instance that the investment enables the society to fulfil its own objects.

Additional considerations to ensure any investment is Shariah Compliant are as follows:

1. Underlying asset classes are Shariah compliant.
2. The contracts used in the investment are Shariah compliant.
3. There should be no use of derivatives.
4. The investment should not leverage.
5. The company should have a business activity and service which is Shariah compliant. A business should not be of the following:

- a. Companies in the financial services industry that are involved in interest-based lending and/or distribution of interest-based products. This includes financial intermediaries such as conventional banks, conventional insurance, interest-based lending (excluding windows operating in compliance with Shariah principles).
- b. Manufacturing or distribution of alcohol and tobacco;
- c. Companies operating in betting and gambling operations like casinos or manufactures and providers of slot/gambling machines;
- d. The production, packaging, processing, or any other activity related to pork and nonhalal food and beverages;
- e. Shariah non-compliant entertainment and illicit adult industries

Financials of the company Investments shall not be made in companies with the following financial ratios:

- a. Total Conventional debt (interest bearing) divided by the Total Asset of the company that is equal to or greater than 30%;
- b. The sum of cash plus interest-bearing securities divided by the Total Asset is equal to or greater than 30%; and
- c. Non-permissible income equal to or greater than 5% of total revenues.

Membership categories

While it is possible (and necessary for the multistakeholder model) to have different categories of membership, it is important that all members are treated equitably.

An important implication of this is that **Pioneer Offers** or any further offers of investment that offer different terms and conditions to investment would not be considered Shariah compliant.

Membership subscription

All references to and the option for membership subscriptions have been removed as this was creating unnecessary complications relating to termination of membership to keep it Shariah compliant and is very rarely used by societies issuing community shares.

Termination of Membership

Reference to any annual subscription has been removed here and should not be included. Dealing with share capital when membership is terminated is detailed below.

Expulsion from Membership

This is revised wording of the clause and is more comprehensive. We have added caveats that the grounds for expulsion but be fair, reasonable and Shariah compliant. If there is any doubt on this, advice should be sought at the time.

Dealing with share capital when membership ends

We have removed option 1 from our model (members only hold one share) as the purpose of these rules is to enable community share offers therefore we are not providing for an option where members only hold one share.

The one non-withdrawable share (normally a nominal value of £1) should be agreed to be **donated** back to the society and then cancelled before returning the value of any remaining shares to the member. The understanding of it as being donated and consented to as a process is important. This needs to be in the share offer documentation as members need to agree to this at the point of investment/becoming members.

Share capital

We have removed the option for members holding one share as the intention behind these models are to enable Shariah compliant community shares so the default option would always be members holding more than one share.

If the society has suspended withdrawal of shares and the nominal value of the shares cannot be immediately returned to the member, additional consideration needs to be given to the terms agreed between the society and the member to resolve this situation. If the share is converted to loan stock to be repaid within three years, no interest can be charged on that loan.

The Share Offer Document needs be clear that the managing of share capital in the event of a member ceasing to be a member.

Transferable shares

We have deleted reference to transferable shares as the intention of these models is to enable Shariah compliant community shares – community shares defined as withdrawable but non-transferable share capital.

Loan stock

Any loan stock issued must also be Shariah compliant. For simplicity and the avoidance of doubt, any reference to loan 'stock' has been removed and has just been referred to as a 'loan' on Shariah compliant terms.

Reduction in share value

For clarity, any impairment or reduction of the share value cannot be arbitrary. It must be based on a professional business valuation and reflect the actual value of the society. This section has been reworded for clarity.

Power and Duties of the Board of Directors

An additional Board responsibility has been added: “To ensure that all activities and practices of the Society are conducted in a Shariah compliant manner”.

Societies are advised to consider annual ‘Shariah compliant’ checks or audit of some description.

Payment of interest on share capital

It is not considered Shariah Compliant for interest to be paid on share capital. Any financial return cannot be predetermined or a percentage of capital provided.

A Community Benefit Society looking to raise Shariah compliant community shares would have to do so at 0% conferring community ownership but with no financial return for members.

If the offer is eligible for tax relief this could act as a useful financial incentive in this scenario. There are no restrictions on utilising tax reliefs from a Shariah compliance perspective.

Reference to interest payments have been removed throughout the model, with the exception of the asset lock which is statutory wording but understood in reference to the 0% rate.

Application of profits

For clarity, any trading surpluses generated in a society are considered profits. The application of these profits towards a general reserve for the continuation and development of the Society is Shariah Compliant.

The application of these profits towards payments to other organisations to further the social and community purposes of the Society must also be mindful of Shariah Compliance of activities as outlined in the objects section above.

Profits may be distributed to members in the Multi-stakeholder Co-operative model. According to the rules of Musharakah, the profit distribution should not be based on transactions with the co-op or be a percentage of capital invested but should be distributed equitably amongst the members.

The intentions surrounding this equitable distribution should be communicated clearly in the Share Offer Document and Business Plan.

Asset lock (CBS)

It is recommended that if using the Community Benefit Society model, a group should adopt the statutory asset lock. As the wording cannot be changed, it's been confirmed it is okay to leave in 'or interest on such capital' with the understanding that it cannot be above 0% as per earlier rules.

The Share Offer Document and potentially Application Form need to be explicit that members agree to the distribution of residual assets as described but will still have recourse to their shareholding.

Dissolution clause (Co-operative)

If using the Multi-stakeholder Co-operative Model, there remain two options: the Common Ownership clause or Co-ownership clause. It is recommended that the **Co-ownership clause**, which allows residual assets to be distributed to members, be adopted as it is the best fit from a Shariah Compliance perspective. The Common Ownership clause would still be compliant as is similar to the CBS statutory asset lock and requires the same approach as above to ensure that members agree at the point of investment to the wider distribution of the society's residual assets.

Untraced members

Transparency on this approach has been raised as pertinent to ensure Shariah compliance of the Rules.