

6. FACT SHEET ON COMPANIES AND OTHER LEGAL FORMS



This fact sheet deals with the law relating to companies in the Companies Act 1993. It provides information about the liability of companies and company directors, and also deals with companies that have charitable status. This fact sheet also includes information about industrial and provident societies and Māori land trusts.

COMPANIES

Introduction

The main Act governing companies is the Companies Act 1993. The Act limits the activities of companies and the rules that companies can adopt for themselves (their constitution).

A company must have a name, one or more shares, one or more shareholders, and one or more directors. A person cannot be a company director if they are under 18, are an undischarged bankrupt, have certain convictions, or are stopped by the Court or Registrar of Companies from being a director in accordance with the Act.

Effect of incorporation under the Companies Act

Once incorporated, a company is considered to be a body corporate under the name of the company. This means that it takes on a separate legal identity distinct from its shareholders and directors. Until it is liquidated, the company enjoys a continuing existence that does not depend in any way on changes in its shareholders or directors.

Limited liability

Unless their constitutions state otherwise, companies are limited liability entities. This means the shareholders are not personally liable for any contract, debt or other obligation the company makes or incurs beyond the value of their shareholding, unless they give personal guarantees.

Directors are personally liable if they have breached their duties and obligations or have given personal guarantees.

Registration and incorporation of a company

Requirements for incorporation

The Companies Act sets up a statutory regime for the incorporation of a company. For a company to be incorporated, it must have:

- a company name
- one or more shares
- one or more shareholders
- one or more directors.

A company may adopt a constitution to regulate its operations on or after it is incorporated, but this is not a requirement of incorporation (because companies automatically have the powers set out in the Companies Act).

Applications for registration and incorporation

Once these requirements for incorporation are satisfied, the applicant must apply to the Registrar of Companies to reserve the company name. The applicant should then complete, sign and submit an application for registration. This application must state:

- the full name and address of each applicant
- the full name and address of each director and shareholder
- the number of shares to be issued to each shareholder
- the company's registered office and address for service.

The application must include the following documents:

- The consent of every person named as a director recorded in the appropriate form and signed by that person.
- A certificate demonstrating that the person named as a director is not disqualified from being a director (where the Companies Office forms are used the Consent and Certificate of a director are incorporated into the one form).
- The consent of every person named as a shareholder, and their number and class of shares, recorded in the appropriate form and signed by the shareholder.
- Any proposed constitution for the company.

When the completed application has been received, the Registrar will register the application and issue a certificate of incorporation.

Governance of companies

Constitutions

While it is not necessary for a company to have a constitution, it is almost always desirable for a company to have a specially drafted constitution that

meets the company's particular needs. A constitution will have no effect if it contravenes the Companies Act 1993.

A company can adopt a new constitution, or alter or revoke its current one, only by a special resolution passed by 75 per cent of shareholders entitled to vote. The company's board must notify the Registrar of Companies within 10 working days of this resolution and deliver a copy of the constitution to the Registrar of Companies.

Annual meetings and special meetings

A company must hold an annual meeting of shareholders within 18 months after it is incorporated. Annual meetings must be held not more than six months after the company's balance date and not more than 15 months after the previous annual meeting. A special meeting of shareholders may be called at any time by the board or by a person authorised by the constitution.

Notice of a shareholders' meeting must be sent to all people who are entitled to attend, including the auditor if one is appointed, at least 10 working days before the meeting.

Directors' responsibilities and delegation

The board of directors is responsible for the day-to-day management of the company, but subject to the restrictions contained in the Companies Act and the constitution. Directors may delegate their powers to individuals or committees. However, they remain responsible for these duties and must ensure there is some system of monitoring to ensure that the delegated duties are carried out correctly.

Statutory duties of directors

Directors must:

- act in good faith and in the company's best interests at all times
- exercise their powers for a proper purpose
- exercise the care, diligence and skill that a reasonable director would exercise in the circumstances, taking into account the nature of the company, the decision and the nature of the responsibilities
- record the basis on which important decisions are made and retain supporting information on which the decisions are based – this will help the director establish that their decisions were reasonable if a question of compliance arises.

Directors must not:

- act or agree to the company acting in a manner that contravenes the Companies Act or the company's constitution
- incur or cause the company to incur obligations that the company can't meet or that would create serious loss to the company's creditors
- make use of or disclose any confidential information relating to the company.

Directors' interests and disclosure requirements

A director must disclose to the board and shareholders if he or she:

- has an interest in a contract or other transaction and may or will obtain a material financial benefit from the transaction
- is a director, officer or trustee of another entity that is a party to a transaction, or that will or may receive a material financial benefit from the transaction
- is a parent, child or spouse of a person who is a party to a transaction, or who will or may receive a material financial benefit from the transaction
- is otherwise materially interested in a transaction, directly or indirectly.

The interests of a director must also be registered in the company's interests register, as well as being disclosed to the board and shareholders.

Reckless trading and incurring obligations

A director of a company must not:

- agree to, cause or allow the company's business to be carried out in a way that is likely to create a substantial risk of serious loss to the company's creditors
- agree to the company incurring an obligation unless the director believes on reasonable grounds that the company will be able to perform it.

Similarly, the Fair Trading Act 1986 prohibits people in trade from engaging in misleading or deceptive conduct in general. The issue is not whether the director or trader intends to mislead or deceive – it is whether their actions did or could mislead or deceive.

See Fact sheet 14: Trading and other activities.

Director's certificates

These are written statements of opinion endorsed and signed by directors. A director should never sign a director's certificate without first carefully reviewing what it says, as he or she will be exposed to potential civil and criminal penalties if:

- he or she signs a director's certificate without holding the opinion expressed in it
- he or she does not sign a director's certificate when required to do so.

Remuneration of the board

The Companies Act provides for the board of a company to authorise the remuneration of its directors. If the company has a constitution, then this may affect remuneration for the board. The board must be satisfied that the remuneration is fair to the company, and a certificate to this effect must be signed by those directors who voted in favour of the remuneration.

If the remuneration is deemed to contravene the Companies Act, then the director and former directors who received the remuneration will be personally liable to the company for that amount.

Indemnity and insurance

The Companies Act 1993 allows a company to indemnify and effect insurance for directors and employees only if the company's constitution permits it.

The constitution may authorise the following indemnities:

- Indemnity from costs in criminal cases in which the director or employee is not convicted
- Indemnity from civil liability (but not liability arising from a breach of a director's duty to act in the company's best interests, or an employee's fiduciary duties to the company or a related company)
- Indemnity from costs in civil cases in which judgment is given for the director or employee

The constitution may authorise the company to give effect to the following types of insurance for directors or employees:

- Insurance against costs in criminal cases in which the director or employee is not convicted (the case must relate to the person's conduct in their capacity as director or employee)
- Insurance against any civil liability or costs

Accounts

A company must prepare financial statements that comply with the Financial Reporting Act 1993, within five months of its balance date. "Balance date" means 31 March or any other date that the directors adopt as the balance date.

The Financial Reporting Act generally requires a statement of financial position (balance sheet) and a statement of financial performance (income and expenditure statement). Sometimes a company may be required to include a statement of cash flows in its Financial Statements. A company is required to keep records of its Financial Statements for five years. Some companies must also file their financial statements with the Registrar of Companies.

Records and registers

A company is generally required to keep a number of records at its registered office, including, for example, its constitution and minutes of all meetings and resolutions of shareholders, directors and committee members over the past seven years.

A company's interests register must record details of the directors' interests including remuneration, benefits and share dealings.

Annual reports

A company must prepare an annual report each year within five months of its balance date. The annual report and annual financial statements must be sent to all shareholders at least 20 working days before the annual meeting is to be held. An annual report must contain:

- completed and signed financial statements
- group financial statements (if applicable)
- an auditor's report, if the company is required to be audited
- additional mandatory information which must be included unless the company specifically resolves otherwise.

Annual returns

A company must file an annual return with the Registrar of Companies every year, except for the calendar year in which the company is registered. An annual return must be dated and submitted by a director, or by a lawyer or chartered accountant who is authorised to submit it.

A company may file its annual return either by filling out the annual return and sending it into the Companies Office with the correct filing fee or

alternatively, the annual return may be submitted online at the Companies Office website free of charge.

There are reporting requirements for companies that register for charitable status with the Charities Commission.

See *Fact sheet 7: Charities Commission*.

There may also be reporting requirements required of charitable companies as a result of the review of the Financial Reporting Act 1993.

Dividends and classes of shares

A dividend is a distribution made by the company to shareholders in proportion to the particular shareholder's shareholding. The board of a company authorises the payment of dividends and can do so only once the company has satisfied the solvency test as set out in the Companies Act.

Alternatively, a dividend can be authorised by the shareholders if all shareholders (and everyone to whom the constitution gives the rights and powers of shareholders) agree to this.

The Companies Act permits different classes of shares to be issued, and these classes may have different rights, privileges, limitations and conditions attached to them. The shares in each individual class will have identical rights, privileges, limitations and conditions.

If there is more than one class of shares in a company, the ordinary shares will be those with the fundamental rights, privileges, limitations and conditions attached to them.

Other classes may involve what are known as "preferential shares". These are shares that entitle the holder to a dividend payment or repayment of capital ahead of shareholders of ordinary shares in the company.

Transactions with other people and organisations

Entering into contracts

A company may enter into a contract with another person or entity. The appropriate method for contracting will depend on the legal requirements for entering into the particular kind of contract.

See *Fact sheet 18: Contracts*.

"Major transactions"

The Companies Act prohibits companies from entering into a "major transaction" unless it is approved by a

special resolution of the shareholders, or unless the transaction depends on getting that approval.

A "major transaction" is:

- an acquisition or disposition of assets, the value of which is greater than half of the value of the company's assets before the acquisition or disposition
- a transaction that has, or is likely to have, the effect of the company incurring obligations or liabilities, the value of which is greater than half of the value of the company's assets before the transaction. For example, any loan or other agreement to provide financial accommodation will be a major transaction if it is more than half of the value of the company's assets, even if the borrower is not obliged to fully draw the loan.
- a transaction that will result in the company acquiring rights or interests, the value of which is greater than half of the value of the company's assets before the transaction.

Charitable status

A company will be taxed on profits unless it is approved as having charitable status. Inland Revenue will accept a company as charitable if all the shareholders are themselves charitable entities and accepted as such by Inland Revenue, with appropriate restrictions incorporated into the company constitution.

Registration with the Charities Commission is required for any organisation to be tax-exempt, but the final decision on tax exemption is still be made by Inland Revenue.

See *Fact sheet 7: Charities Commission and Fact sheet 8: Taxation*.

Liquidation and receivership

Liquidation of a company is when it ceases to trade or becomes bankrupt. The company's assets are sold and the proceeds are paid to the company's creditors in accordance with what the company owes them and the priorities between those creditors themselves. Any surplus money will be distributed proportionately among the shareholders. A company may be put into liquidation voluntarily or by the Court. Liquidation begins when a liquidator is appointed.

Voluntary liquidation

A liquidator can be appointed either by a special resolution of the shareholders entitled to vote on the matter, or by the company's board when something occurs that is provided for in the company's constitution.

Compulsory liquidation by the High Court

Alternatively, the High Court may appoint a liquidator when it has received an application from the company, a director, a shareholder or other entitled person, a creditor of the company, or the Registrar of Companies.

Consequences of liquidation

Once a company has been put into liquidation, the control and custody of its assets vest in the liquidator. The directors remain in office, but have only the powers specified in the Companies Act. As a result of the liquidation, there are restrictions on activities within the company. For example:

- no shares may be transferred
- no changes may be made to shareholder rights or liabilities
- shareholders may not exercise any powers they may have under the company's constitution or the Act, unless those powers are exercised for the purposes of the liquidation
- the company's constitution may not be altered.

Receivership

A company is placed in receivership when a receiver is appointed. A "receiver" is a person appointed by a creditor of the company or the Court to investigate the affairs of a company that is in financial difficulty. A receiver can be appointed by or on behalf of a secured creditor to take control of, and protect, the assets or property over which the security has been granted. Debentures creating a security over the company's property often confer a right on a debenture holder to appoint a receiver. The Courts may also appoint receivers under the Judicature Act 1908.

OTHER LEGAL FORMS

Industrial and provident societies

There are relatively few industrial and provident societies registered today. They were more common in the 1970s when co-operative organisations were popular.

However, the industrial provident society remains a sound and workable structure. They are suitable for groups wanting to work together co-operatively and make a profit that may be paid out to members. Industrial and provident societies share many features with incorporated societies, but must use a name that ends with the words "Society Limited" or "Co-operative Society Limited".

There are six key characteristics of an industrial and provident society:

- It has a minimum of seven members, with members joining and leaving according to the rules.
- The society is a separate legal entity from its members and can enter into contracts in its own name. No member of the society can have personal rights or interests in any of the society's assets.
- Voting is on the basis of one person, one vote.
- The society is a genuine co-operative, working to benefit the community in some way.
- The society has a formal registered set of rules.
- Tax is paid on profits after wages and business expenses. Levies, subscriptions and the first \$1,000 of income may be tax-exempt if certain conditions are met, such as the society having no power to make distributions to members.

Although it is only stated indirectly in the Industrial and Provident Societies Act 1908, a society must have at least seven shares (references in the Act to "members" are effectively references to shareholders). There are limitations on transferring shares: they may only be of a nominal value (for example, \$1.00) and no member may hold or have an interest in more than \$4,000 in shares. Annual audited accounts and an annual return are required by the Companies Office.

Māori land trusts

There are five different types of trusts as set out in Te Ture Whenua Māori Act 1993/Māori Land Act 1993:

- Pūtea trust
- Whānau trust
- Ahu whenua trust
- Whenua tōpū trust
- Kai tiaki trust

Whānau and pūtea trusts are the types most

frequently used. Each trust has a different purpose and different rules. Detailed information on these trusts is available from Māori Land Court offices.

There are several key characteristics to Māori land trusts:

- Only the owners of Māori land or their trustees can set up a trust.
- The primary goal of a trust is to retain Māori land in Māori ownership.
- Trusts are set up under a trust deed and must be registered with the Māori Land Court.
- Trustees make all the decisions.
- Trusts may make profits.
- Establishing a trust over the land may prevent individual ownership of the land and therefore further fragmentation.
- Trusts can include shares in a corporation.

RESOURCES

Fact sheets

Fact sheet 7: Charities Commission

Fact sheet 8: Taxation

Fact sheet 14: Trading and other activities

Fact sheet 18: Contracts

Websites

www.biz.org.nz

This portal provides access to all sorts of business-related websites and is intended to make it easier for organisations to run their business.

www.charities.govt.nz

The Charities Commission is responsible for registering charities from 2007 onwards.

www.community.net.nz

The “How-to Guides” section has a community development resource kit covering all aspects of establishing and running an organisation.

www.companies.govt.nz

The New Zealand Companies Office’s website provides general advice and guidance on companies and has a business update letter, forms and fees.

www.dia.govt.nz

The Department of Internal Affairs has information about administering lottery grants and community grants schemes.

www.ird.govt.nz

Inland Revenue’s website has information on not-for-profit groups. Download a copy of the brochure *Smart business – An introductory guide for businesses and non-profit organisations* (IR320).

www.justice.govt.nz/maorilandcourt

The Ministry of Justice website offers guidance on Māori Land Trusts and duties of trustees.

www.lawaccess.lsa.govt.nz

This website offers a catalogue of law-related information resources, with over 140 New Zealand organisations listing their resources on the site.

www.lsa.govt.nz

The Legal Services Agency has information on community law centres throughout New Zealand.

www.nzco-ops.org.nz

This website provides information on industrial and provident societies.

www.societies.govt.nz

Societies and Trusts Online provides an information library with forms and fact sheets. It enables incorporated societies to maintain organisational details and provides access to a register of incorporated societies and charitable trusts.

www.tpk.govt.nz

Te Puni Kōkiri’s website has information on effective governance.

Publications

Von Dadelszen, M – *Law of Societies in New Zealand* (2000, Wellington, Butterworths)

Von Dadelszen, M – *Members’ Meetings in New Zealand*, 2nd ed (2004, Wellington, LexisNexis)

