Hui E! Submission:

MBIE Proposals to replace the Incorporated Societies Act

Introduction

Hui E! was set up in 2014/15 with wide support from the sector, with clear purposes: to strengthen, connect and promote the sector as a whole. Although Hui E! is relatively new its lead staff have many years of experience working in, leading and mentoring community organisations, especially incorporated societies.

Hui E! acknowledges the shortcomings of the current 1908 Act, and generally supports the recommendations of the Law Commission in its 2013 Report *A New Act for Incorporated Societies.*

Hui E!'s experience coincides with that quoted from the Auckland District Law Society:
"In our experience, members generally want to do their best for their society, are happy to follow rules, and would welcome greater certainty both in terms of internal processes and rights of recourse outside the society"

Hui E!'s submission is based partly on input gathered during the series of consultation seminars during February – May 2016, but also on the experience and interactions of its governance and staff, with very many organisations across this very diverse sector, over many years.

Registration and Regulation

Hui E! is concerned that some aspects of the proposed Bill substantially alter the relationship between incorporated societies and government, possibly without conscious intention but also, whether or not it is deliberate, unilaterally acting when the relationship is supposed to be one of partnership.

In recent years the role of the Registrar of Incorporated Societies has been benign, with only minimal demand placed on societies on terms of annual reporting to the Registrar. This is appropriate, given the UN resolutions which lay out the independence, rights and freedoms of civil society organisations.

Several aspects of the Draft Bill indicate an assumption on the part of government, and MBIE, that incorporated societies are not independent, and that government is somehow free to impose greater regulation, and a greater compliance burden, at will. Why is this?

Internationally there is significant awareness that the global Financial Action Task Force (FATF), set up in 2004 as a response to the September 2001 terrorist attacks in the US, created a set of ***International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation*** with 8 key recommendations for participating governments, of which New Zealand is one.

As noted by the UN Special Rapporteur, FATF Recommendation 8 has badly undermined the relationship and the level of trust between governments and civil society.

Recommendation 8, under the heading *Terrorist Financing and Financing of Proliferation,* appears to have been taken on board by the New Zealand Government:

> N**on-profit organisations**
> Countries should review the adequacy of laws and regulations that relate to entities that can be abused for the financing of terrorism. Non-profit organisations are particularly vulnerable, and countries should ensure that they cannot be misused:
> (a) by terrorist organisations posing as legitimate entities;
> (b) to exploit legitimate entities as conduits for terrorist financing, including for the purpose of escaping asset-freezing measures; and
> (c) to conceal or obscure the clandestine diversion of funds intended for legitimate purposes to terrorist organisations.

This has driven government policy-setting and greater regulation of organisations in many countries, and has been shown to have significant negative consequences for social cohesion and social capital. It changed the psychology of governments and thus their attitude to independent civil society organisations, providing a rationale for a shift from benign registration regimes to active regulation.

Ironically while the NZ government and MBIE are proposing replacement of the 1908 Incorporated Societies Act with something that imposes greater regulation and compliance, the FATF has acknowledged the negative effects of Recommendation 8, and committed to revise it. Submissions on the revision closed on 30 April 2016.

See the submission to that review from Maina Kiai, UN Special Rapporteur, to FATF

> **SPECIAL RAPPORTEUR CALLS ON FATF TO CONSIDER CIVIL SOCIETY'S ROLE IN COUNTERTERRORISM**
> The United Nations Special Rapporteur on the rights to freedom of peaceful assembly and of association, Maina Kiai, called on the Financial Action Task Force (FATF) to improve its cooperation with civil society and consider the sector's valuable contribution to the fight against terrorism. He commended FATF on its decision to revise its controversial Recommendation 8 (R8), which requires FATF member states to ensure that nonprofits are not used to fund terrorism. In recent years, oppressive governments have used R8 to crack down on dissent. He said that 'the approach to countering terrorist activity needs to shift from regarding NPOs as part of the problem, to embracing them as integral to the solution'.
> See here for the full statement, issued 18 April 2016.

There is a significant contrast between the New Zealand move to impose greater regulation and compliance, and the UN Rapporteur's call for governments to instead embrace 'non-profit organisations' as integral of the solution.

Open Government Partnership

Also relevant are the provisions of the Open Government Partnership publication ***Guide to Opening Government*** chapter entitled ***An Enabling Environment for Civil Society Organizations.*** New Zealand committed to the Open Government Partnership (OGP) in October 2014. The "Partnership" of the title is between government and civil society, and the chapter referred to lays out illustrative commitments necessary for building that partnership.

The illustrative commitments are categorised as Initial, Intermediate, Advanced and Innovative, and some New Zealand established practice is certainly in the "Innovative" category. However, back in the "Intermediate" grouping, under "Provide safeguards against undue supervision of CSOs" (CSOs are civil society organisations) we see the recommendations:

> *2. CSOs are allowed to make decisions and determine their governance structures and leaders, without government interference through law or practice. Any governance requirements prescribed by law are made proportional to the size and scope of different types of organizations.*
>
> *3. Reporting requirements are made proportional to the size and scope of different types of CSOs and are not more burdensome than for other legal entities. Mechanisms for online reporting are considered in order to lessen administrative burdens.*

Since New Zealand is officially committed to OGP, via a formal Letter of Commitment from Prime Minister Key in 2014, these recommendations need to be included in any consideration of a possible change to the relationship.

Some proposals in the Draft Bill do not meet the recommendations above, and thus need to be reconsidered. Points where Hui E! believes this to be the case are identified in our Response to particular proposals, below.

Hui E! Response to the Proposals

What we like:

Hui E! supports many parts of the proposed Bill, as listed below. However we have significant reservations in some areas:

1. The **core principles** established by the Law Commission and confirmed here;
   - Societies are private bodies that are operated by their members
   - Societies should not distribute profits or financial benefits to members
   - Societies should be free from inappropriate government interference

2. The 4th principle described by MBIE in the presentation to the consultation seminars:
   - Societies' governance should be based on Trust and Integrity

3. That an incorporated society is a separate legal entity that operates for purposes other than the financial gain of its members

4. That a society continues in existence unaffected by the comings and goings of its members or office holders
   - A Society is a body corporate, from the date on its incorporation certificate

- It has perpetual succession
- It has the capacity, rights, powers and privileges of a legal person
- It continues in existence until it is removed from the register

5. The principle of incorporation - that a society can enter into contracts and hold assets in its own name
   - It has full capacity to undertake any activity, do any act, or enter into any transaction, But
   - It must not break the general law
   - What it does will be limited to the powers etc. that are in its constitution

6. Members of a society are not personally liable for any obligation or liability that the society incurs in its own name
   - A member is not liable for an obligation of the society by reason only of being a member, but
   - A member who is also a committee or governance group member has the responsibilities that come with a governance role

7. Societies should not distribute profits or financial benefits to members.
   - A society must not be carried out for the financial benefit of its members
   - No profit-sharing, no ownership by members in the form of shares or stock, or disposable interest

8. The availability of legislated "safe harbours" - to
   - Engage in trade
   - Pay a member for matters incidental to the purposes of the society
   - Reimburse a member for expenses related to the purpose of the society
   - Provide benefits to members or the public, e.g. scholarships
   - Pay a salary or wages or other payments for service, at a market rate or below
   - Provide a member with incidental benefits, e.g. prizes, trophies, discounts on services

9. The clarity around financial gain and what can be done if a Society fails to meet the criteria

10. We support the reduction from 15 in the number of members a society must have to register, and the requirement to maintain at least that number. The draft proposes 10, however internationally the Open Government Partnership, to which NZ is committed, recommends in the ***Guide to Opening Government*** chapter on ***An Enabling Environment for Civil Society Organizations,*** that the number of founders needed to register an organisation should be no more than 2 or 3 natural and/or legal persons.

Hui E! Recommends 5 members would be more appropriate, balancing the need to demonstrate the community basis of the organisation with the rather arbitrary existing 15 and the similarly arbitrary proposal of 10 members.

11. The proposal that the minimum age for officers of a society be reduced from 18 to 16 years – there are some great rangatahi groups and rangatahi should be part of their governance.

12. The emphasis that officers' responsibility in decision-making is to the society. It is clear from case law and from the "legal person" status of societies that officers owe their duties to the society, but there is a widespread misunderstanding.

13. The simpler procedure for the amalgamation of two or more societies.

14. That constitutions will be required to contain rules setting out the composition, roles and functions of the committee, that there is clarity around Officers Duties, and that these are very much based on the Companies Act. However, there is **no mention of Sub-Committees** in this context. Very many Incorporated Societies have them, but they can be a significant cause of strife.

Hui E recommends the addition of a provision that where a society has the capacity in its constitution to form one or more sub-groups of the main elected governance group, (a Finance Sub-Committee is the most common) there must also be provisions requiring the sub-group to report back to the main body. The 'how' of the reporting should be up to the society.
One of the most common complaints we hear is that people feel disempowered by the actions of a subcommittee – "I'm an elected officer so I'm legally responsible, but they make all the decisions and I get no say."

15. The proposals around indemnification of officers, members or employees, including the identification of areas where an officer cannot be indemnified

16. The proposals around disqualification of officers, including the opportunity to seek a waiver. This has worked appropriately in relation to registered charities.

17. The grounds on which a Court may make orders against an officer or former officer, including enforcing a duty and compensating the society

18. Re **Conflict of Interest** we agree that some provision is necessary – to define what it is, what should be done to ensure members and officers are aware when it arises, and what should be done to prevent it affecting decision-making in inappropriate ways. However we are not convinced that the proposed requirements are appropriate – they would be onerous for small societies.

Hui E recommends that the proposed requirements be simplified.

19. What a constitution must contain; we support the clarity of the list, but would make one change.
Hui E recommends that item *g. Committee's composition, roles and functions*, be extended to include a mention of sub-committees as described in point 14 above.

20. The decision to provide "standard clauses" rather than a model constitution, recognising:
    - the diversity of the sector, and
    - the principle that civil society organisations are created to meet the needs and aspirations of communities, and writing a constitution is an opportunity for the people involved to consider and to document what those are.

21. The long introduction period, with a series of **transition dates** that give everyone the chance to do what is needed.

22. We support the logic re Audit or Review in clauses 106 – 109 of the Call for Submissions, which limits the number of organisations required to undertake audit or review.

Hui E! recommends however that consideration be given to requiring audit or review in societies that are in Tier 1 or Tier 2 of the XRB Standards, if they have **Donee Status with IRD**, and thus an increased level of public interest.

Other areas we strongly question

1. Clauses 83 and 84: The proposed requirement that all Incorporated Societies meet the same accounting and reporting standards as registered charities

- This is an unnecessary compliance burden for very small societies – Members should be able to decide what reporting they need, and Government should accept that. See the 3 core principles that are supposed to guide the legislation, and in particular;
    - *Societies are private bodies that are operated by their members*
    - *Societies should be free from inappropriate government interference*

- If the members of a society are content with the current level of accountability and financial information they receive from their treasurer, where is the need for government to require a higher level of reporting?

- Charities get a significant tax benefit, as do their donors – what's in it for incorporated societies? Why would government impose the same level of compliance as registered charities on a large number of relatively small organisations, when there is no accompanying benefit?

- Hui E! has been contacted by Community Trusts who are concerned about the proposal. They make grants to a range of small local and regional organisations, they get to know the organisation, and they gather reports on what has been achieved as a result of the grant. If the Community Trusts are happy with the reports they receive, and the organisation's members are happy with the level of accountability within their organisation, where is the need for central government to get involved and require something different?

- See Recommendation 3 from the Open Government Partnership, above: "Reporting requirements are made proportional to the size and scope of different types of CSOs and are not more burdensome than for other legal entities." The proposal does not meet this standard;

- The proposal undermines the independent basis of civil society organisations by creating a disincentive to formation of societies. It is not clear whether this is deliberate or unintended, but it will have an effect – not simply because of the perceived work involved but on principle – people volunteer in communities so that they can achieve something for their community, not so that they can write reports for government;

- The proposal undermines an internationally recognised and valued principle of NZ's legislation – the ease of establishment and maintenance of a community-based legal entity. NZ has a role-model, and exemplar – why sabotage that?

- The proposal actually increases risk of misappropriation of funds – a group that decides to not register or to cease registration, because of the need to provide reports to government,

will have trouble opening a bank account due to the Anti Money-Laundering legislation. As a result, funds will be kept in a personal account or kept as cash in a drawer somewhere, increasing the risks of misappropriation or loss, as well as strife about its handling;

- Realistically, groups will avoid reporting to government not because they have anything to hide, but because of lack of skills and confidence at filling government forms. In this the proposal can be seen as discriminatory. Tangata whenua, Pacifica, immigrant and refugee groups may want to organise and register a society but may also have language difficulties, may lack experience with the assumed accounting practice, and may also have had previous experiences where any contacts with government have been negative or catastrophic;

- Many small societies come together around a shared activity or aspiration – reporting to government is not on their radar at all, and registration is one step in their growth towards a significant contribution in NZ society. They should be encouraged and valued for their potential e.g. IHC grew from a small local parents' support group;

- Many societies may stay small, but we should not discourage them by imposing needless requirements. Small societies can always choose to report according to the standard but that decision belongs to the members, not to government;

- Given the difficulties DIA Charities Services are having in establishing consistent reporting according to the standard, from registered charities who have a significant incentive to report, it makes no sense to impose the same requirements on a whole lot more who lack the incentive;

- There is evidence registered charities are already making up the numbers they are required to provide to DIA Charities Services, because they have not gathered the necessary data over the past year. MBIE should be aware this is a result of Charities Services focusing on the end of each organisation's financial year as the date they need to start thinking about reporting according to the standard. Charities Services may attempt to address this 'construction' of data over the coming years, but societies are now realising how little resource Charities Services has to be able to check, and the practice will likely become cemented in over the next 6 months.

- Given this, the law is an ass if it imposes a greater reporting requirement on an additional 15,500 societies (that are not registered charities) but has no plan and no resources allocated to education or monitoring the quality, or even reading the reports. If MBIE intends to simply tick a box that a report has been received we would be better to stick with the existing regime, where societies report in the form chosen by their members.

- There is a rationale for government gathering annual accounts, and this was confirmed by the Law Commission in its review (6.167-6.172). As the Commission noted this has particular value for societies that are not good at keeping consistent records, especially when there is a change of Treasurer.

- There is also an argument that the above rationale is patronising - it is certainly inappropriate for government and MBIE to use this as a reason for increased regulation. Hui

E! has some feedback that it is the responsibility of organisations to keep their own records, and if they fail to do so that is their problem, not a reason for government to be involved.

In summary, given that:

- There is no demonstrable benefit in a scheme where government requires societies to produce more detailed reports but has no intention of reading them;

- A ready-made regime for reporting by registered charities exists;

- That regime recognises the need to scale reporting requirements according to the size of organisation and to a realistic assessment of risk to the public;

- The draft Bill acknowledges that in relation to audit at least, there is significantly less public interest and thus less need for public accountability for small incorporated societies;

- There is much lower public interest in the finances of incorporated societies compared to registered charities;

Hui E! recommends:

- Incorporated societies that sit within the parameters of Tier 4 in the XRB standards be exempt from having to report according to the standard, but should continue to provide the registrar with financial reports in the form chosen by their members and approved at an annual general meeting;

- Incorporated societies in Tiers 1, 2, and 3 should report according to the XRB standard, as the level of donor and grant funding is likely greater, creating a greater public interest;

- Incorporated societies that have Donee Status should report according to the standard, including if they are in Tier 4, as they receive a tax benefit and therefore have accountability beyond their members.

2. Appeals

The Draft Bill proposes that appeals from decisions of the Registrar have to go to the High Court within 15 days, although this can be extended by the Court if the organisation applies.

This is unreasonable – it may be deliberately difficult, with the intention of discouraging appeals, but whether or not it is deliberate it offends the spirit of the Open Government Partnership to which NZ has committed.

- Hui E! recognises, from the experience of our supporting organisations with the former Charities Commission and more recently DIA Charities Services, this is a prohibitively expensive process, almost impossible for most organisations;

- It's extremely difficult for a volunteer-based community organisation to gather material, get advice, meet, decide to lodge an appeal and lodge it within 15 days. Societies typically have volunteer governance group members who reside at a distance from each other and who only gather monthly or quarterly;

- The proposal means organisations effectively have the stress and cost of going to court twice – to get an extension and then get the actual appeal heard.

Hui E! Recommends:

- That more time be allowed for an organisation to process the decision to seek a formal review of a decision – at least 3 months.
- That a lower level review process be included in the legislation, before going to the High Court.

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