To: Ministry of Business, Innovation and Employment

On: the Exposure Draft: Incorporated Societies Bill

27 June 2016

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INTRODUCTION

1. This submission is from SUE BARKER CHARITIES LAW, PO Box 3065, Wellington 6140.

2. We have no objection to information in this submission being released. If you would like to contact us our details are:

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ABOUT SBCL

3. Sue Barker Charities Law is a boutique law firm in Wellington specialising in charities law and public tax law. The firm has been assisting a number of incorporated societies review their constitution in light of the proposed new legislation governing incorporated societies.

BACKGROUND

4. We welcome the initiative to update the Incorporated Societies Act 1908. The Exposure Draft is a significant improvement on the current legislation. We also appreciate the opportunities provided for consultation.

SUMMARY OF MAIN ISSUES

5. Our submission addresses the following issues:

(a) retaining the Registrar's ability to permit a society to incorporate under a name that is similar to a company's name, where that company *consents* to the similar name;

(b) permitting societies proposing to incorporate to *reserve* a name in a manner similar to section 22 of the Companies Act 1993.

(c) the Law Commission recommendation that a mandatory use provision, equivalent to section 25 of the Companies Act, be included;

(d) whether the financial gain prohibition precludes the distribution of surplus assets on the winding up of a society to members that are themselves not-for-profit entities;

(e) whether the definition of "not-for-profit" entity in clause 24(4) precludes sporting organisations that are constituted as trusts;

(f) extending the compliance cost reduction measures for incorporated societies that are also registered charities to the requirement to notify amendments to constitutions;

(g) aligning the factors that disqualify persons from being officers of an incorporated society with those that disqualify persons from being officers of registered charities;

(h) whether employees or former employees who are or have been officers of the society may be provided for in connection with the society ceasing to carry on the whole or part of its activities;

(i) whether the legislation should require officers of incorporated societies to meet a particular level of skill;

(j) whether the legislation should clarify that officers of incorporated societies are entitled to rely on financial data;

(k) that the minimum number of members for a society to incorporate and remain incorporated should be further reduced to 5, consistently with the requirements for charitable societies incorporated under the Charitable Trusts Act 1957;

(l) the process for establishing which entities registered under the Charitable Trusts Act will be required to transition to the new Incorporated Societies' legislation;

(m) a transition period of 4 years is likely to be too long from a practical perspective; and

(n) some suggested amendments to the standard provisions annexed to the Consultation Document.

6. We expand on these points below.

7. In this submission the following abbreviations are used:

Charitable Trusts Act: Charitable Trusts Act 1957

Charities Act: Charities Act 2005

Charities regulator*:* previously the Charities Commission, and now the Department of Internal Affairs – Charities Services and the Charities Registration Board

Companies Act*:* Companies Act 1993

Consultation Document: means the document entitled *Exposure Draft: Incorporated Societies Bill including consultation on Agricultural and Pastoral Societies legislation Request for Submissions,* issued with the Exposure Draft on 10 November 2015

Exposure Draft: means the Exposure Draft Incorporated Societies Bill released for consultation on 10 November 2015

Law Commission report: Report of the Law Commission NZLC R129 *A New Act for Incorporated Societies* June 2013.

Clause 10(1)(iii) - Proposed name of society

Issue

8. Incorporated societies should be able to have a name that is similar to a company's name, where that company has consented, as is the case under the current legislation. In addition, consideration should be given to allowing incorporated society names to be reserved in a manner similar to companies.

Submission

9. Under clause 10(1), the Registrar must refuse to incorporate a society for certain name-related reasons. The 4 reasons listed in clause 10(1)(a) have been modelled on section 22(2) of the Companies Act (Consultation Document, paragraph 22).

Removal of discretion for names similar to companies

10. Under proposed clause 10(1)(ii), the Registrar of Incorporated Societies *must* refuse to incorporate a society under a name if the name is identical, or near identical, to the name of any company carrying on business in New Zealand (whether incorporated in New Zealand or not), or other body corporate established or registered in New Zealand.

11. There does not appear to be any discretion under proposed clause 10(1)(ii) for the Registrar to permit such a registration where the company or body corporate has consented to the similar name.

12. In practical terms, this means that if there was a New Zealand company called **X,** and a not-for-profit entity known internationally as **X** that wanted to establish a New Zealand presence under the name **X NZ**, the international not-for-profit entity would not be able to incorporate a society in New Zealand with that name, even with the consent of **X**. Also, if a New Zealand company or body corporate wanted to create an incorporated society with a similar name, the Registrar would be required to refuse the name. This poses practical problems in terms of brand continuity.

13. This situation would also contrast with section 11(1) of the current Incorporated Societies Act 1908, which allows an incorporated society to have a name that is identical or almost identical to a company or other body corporate *where that company or other body corporate has given consent* to the similar name.

14. The current discretion for the Registrar to permit a name similar to a company where the company has consented should be continued under the proposed new legislation.

Permitting name reservation

15. In addition, a society proposing to incorporate should be able to reserve a name in a similar manner to companies.

16. Proposed clause 10(1)(iii) of the Exposure Draft requires that the Registrar of Incorporated Societies must refuse to incorporate a society under a name if the name is identical, or near identical, to a name reserved under the *Companies* Act

1993. This clause draws on section 20 of the Companies Act, which prevents the Registrar of Companies from registering a company unless its name has first been reserved.

17. It is not possible to reserve names under the current or proposed Incorporated Societies' legislation. However, there are circumstances when such an ability would be useful in today's fast-paced environment. We do not see any benefit in forcing incorporated societies to reserve a name before seeking incorporation. However, consideration should be given to *permitting* a society proposing to incorporate to reserve a name in a similar manner to section 22 of the Companies Act.

Recommendation

18. We recommend that:

(i) Clause 10(1)(a)(ii) is amended by inserting the following words after the words "New Zealand":

", except where that other society, company or body corporate signifies its consent in such manner as the Registrar requires"

(ii) Consideration be given to permitting names to be reserved under the Incorporated Societies Act.

Suggested new clause 10A - Use of incorporated society name

Issue

19. Consideration should be given to the Law Commission recommendation that a mandatory use provision, equivalent to section 25 of the Companies Act, be included in the proposed new incorporated societies' legislation.

Submission

20. Section 25 of the Companies Act 1993 requires that a company clearly state its name in every written communication or document creating a legal obligation. At paragraph 7.74 of its report, the Law Commission recommended that a similar "mandatory use" provision be included in the new incorporated societies' bill: "As with shareholders, members of incorporated societies have limited liability. It is important that this is signalled to third parties entering into legal obligations with the society."[1]

21. A mandatory use provision has not been included in the exposure draft bill. However, there is no discussion in the commentary as to whether this omission was intentional or otherwise.

Recommendation

22. We recommend that a new clause 10A is inserted to require that an incorporated society clearly state its name in every written communication or document creating a legal obligation, in a similar manner to section 25 of the Companies Act 1993.

[1] http://www.lawcom.govt.nz/sites/default/files/projectAvailableFormats/NZLC%20R129.pdf, paragraph 7.74.

Clauses 21-22 - Financial gain prohibition

Issue

23. The Exposure Draft should clarify that the prohibition on financial gain does not prevent an incorporated society from distributing surplus assets on winding up to members that are themselves not-for-profit entities.

Submission

24. The Exposure Draft proposes to make it very clear that incorporated societies must not be carried on for the financial gain of *any* of its members (clauses 3(a), 8, 21, 22, 24(2), 68, 106-108, 158(1)(e) and 161(2)). In particular, clause 21(2) provides that an officer of a society would commit an offence, punishable by a fine of up to $50,000, if the society is carried on for the financial gain of any of its members with the officer's authority, permission or consent.

25. Under clause 22(1)(a) and (2), a society must be treated as being carried on for the financial gain of any of its members if it distributes, or may distribute, *any gain or other financial benefit to any of its members* (whether in money or in kind).

What if a society is comprised of members that are not-for-profit entities?

26. However, it is common for the members of an incorporated society to include not-for-profit entities. It does not seem inconsistent with the principle of the financial gain prohibition for surplus assets of such an incorporated society to be able to be distributed to such not-for-profit members on dissolution. In fact, it would seem odd if this were not possible, given that clause 24(1)(m) requires such distributions to remain within the not-for-profit sector. It also does not seem appropriate that a not-for-profit entity should be prohibited from receiving a distribution on dissolution of an incorporated society merely because it was a member of the society.

27. Although clause 22(3) provides for some exclusions from the financial gain prohibition, none of these exclusions provide comfort that a distribution could be made to a not-for-profit member on winding up, without risking the commission of an offence.

28. For example, clause 22(3)(b) provides that a society is not being carried on for the financial gain of any of its members merely because it will or may "pay a not-for-profit member for matters that are incidental to the purposes of the society". Clause 23(3)(g) provides that a society is not being carried on for the financial gain of any of its members merely because it will or may "provide a member with incidental benefits (for example, trophies, prizes or discounts on products or services) in accordance with the purposes of the society".

29. However, it is not clear that a distribution of surplus assets to a not-for-profit member on winding up would constitute either a payment for matters that are "incidental to the purposes of the

society", or the provision of "incidental benefits" in accordance with the purposes of the society.

30. If the intention is that distributions may be made to not-for-profit entities who happen to be members of a society on dissolution of the society, it would be helpful if this point was made more clearly in the legislation.

Recommendation

31. We recommend that:

    Clause 22(3) is amended by deleting the full stop in paragraph (g), replacing it with a semi-colon, and inserting a new paragraph (h) as follows:

    "(h) distribute surplus assets on a liquidation of the society, or the removal of the society from the register, to a member where that member is itself a not-for-profit entity."

Clause 24(4) - Definition of "not-for-profit entity"

Issue

32. The definition of "not-for-profit entity" in clause 24(4) of the Exposure Draft may inadvertently exclude sporting organisations that are structured as trusts. It should also retain the word "charitable", as not all charities are registered under the Charities Act.

Submission

33. Clause 24(4) of the Exposure Draft proposes to define "not-for-profit entity" to mean any incorporated society (paragraph (a)), any registered charity (paragraph (b)), and any:

> "society, institution, association, organisation, or trust that is not carried on for the private benefit of an individual, and whose funds are applied entirely or mainly for benevolent, philanthropic, cultural or **public** purposes in New Zealand" (paragraph (c)) [Emphasis added].

Donee status definition

34. Paragraph (c) of this definition is similar to the definition used in section LD 3(2)(a) of the Income Tax Act 2007 for "donee status". Donee status is a key tax privilege that enables donors to claim tax credits or deductions for their donations to organisations that meet the definition. Section LD 3(2)(a) uses the following wording:

> "a society, institution, association, organisation, or trust that is not carried on for the private pecuniary profit of an individual, and whose funds are applied wholly or mainly to **charitable**, benevolent, philanthropic, or cultural purposes within New Zealand"

35. A key difference in wording between section LD 3(2)(a) and clause 24(4)(c) is the replacement of the word "charitable" with the word "public". However, this definition may nevertheless have unintended consequences.

Not all charities are registered

36. For example, it seems understandable that the word "charitable" should be excluded from clause 24(4)(c), given that registered charities are specifically included in clause 24(4)(b). However, not all charities in New Zealand are registered under the Charities Act 2005: New Zealand charities are not required to be registered in order to operate and collect funds from the public. The effect of excluding the word "charitable" from clause 24(4)(c) is that many *bona fide* charities, that are not structured as incorporated societies and for whatever reason may have chosen not to be registered, may not fall within the definition.

37. It would therefore be helpful to include the word "charitable" in clause 24(4)(c), to make it clear that charities are eligible for distributions from incorporated societies, even if they are not registered under the Charities Act.

38. Including the word "charitable" in section 24(4)(c) would also

assist with maintaining consistency with the section LD 3 definition. Section LD 3 does not require a charity to be registered in order to be eligible for donee status.

39. Another unintended consequence is that clause 24(4)(c), as currently worded, would likely exclude many *bona fide* not-for-profit sporting organisations, even if the word "charitable" is added.

Sporting purposes not considered charitable

40. It is currently very difficult for sporting organisations to gain or maintain registered charitable status. The charities regulator's approach to the definition of charitable purpose is very controversial in many areas, including in relation to sport.[2] Although there are understood to be some 1,800 sporting organisations listed on the charities register, the charities regulator appears to be systematically working its way through and deregistering them. See, for example, the charities regulator's decision to deregister the New Zealand Rowing Association Incorporated (Decision No D2015-3, 11 September 2015),[3] even though no wrongdoing was involved, simply because the charities regulator had controversially changed its mind regarding its interpretation of the definition of charitable purpose. Other sporting organisations similarly affected include Swimming New Zealand Incorporated,[4] New Zealand Cricket and Table Tennis New Zealand, to name only a few.[5] The net result is that it is currently extremely difficult for many sporting organisations, even those that are well-run and providing significant benefit to the community, to gain or maintain registered charitable status. Unless and until the charities regulator's interpretation is successfully challenged by a sporting organisation through the Courts, this appears destined to be the approach that the charities regulator will take.

41. This means that a sporting organisation is unlikely to fall within paragraph (b) of the definition of "not-for-profit entity" in clause 24(4). This in turn means that a sporting organisations that is not structured as an incorporated society (clause 24(4)(a)), would need to fall within paragraph (c) of the definition proposed in clause 24(4).

Sporting purposes may not be considered

42. However, sporting purposes have traditionally not been considered to be "benevolent, philanthropic, or cultural" either. The Inland Revenue Department consistently refuses to

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[2] See for example the discussion in *Is Sport charitable any more?* Maria Clarke, New Zealand Law Society, 10 April 2015: https://www.lawsociety.org.nz/lawtalk/issue-862/is-sport-charitable-any-more

[3] https://www.charities.govt.nz/charities-in-new-zealand/legal-decisions/view-the-decisions/view/new-zealand-rowing-association-incorporated

[4] https://www.charities.govt.nz/charities-in-new-zealand/legal-decisions/view-the-decisions/view/swimming-new-zealand-incorporated

[5] See Bevan Hurley, *Charity Knockback for Churches, Knights and huskies,* Stuff National, 19 June 2016: http://www.stuff.co.nz/national/81136703/charity-knockback-for-churches-knights-and-huskies.

benevolent, philanthropic or cultural

consider sporting organisations, that are not structured as charities, to be eligible for donee status under section LD 3(2)(a), despite the importance of sport to the culture of New Zealand society. Again, the Inland Revenue Department's interpretation is arguable. However, unless and until it is successfully challenged by a sporting organisation through the Courts, it appears destined to be the approach that the Inland Revenue Department will take.

Sporting purposes may not be "public" either

43. It is also not clear that sporting purposes would fall within the category of "public" purposes either, particularly if registered charitable status has been denied. This means that a sporting entity that is not structured as an incorporated society (paragraph (a)), and that has not been able to gain registered charitable status, due to controversial interpretations by the charities regulator (paragraph (b)), may not fall within the definition of "not-for-profit" entity in clause 24(4) of the Exposure Draft at all.

Some sporting organisations considered worthy of support are structured as trusts

44. In this context, it should be noted that section CW 46 of the Income Tax Act 2007 provides a specific income tax exemption for "clubs, societies or associations" established mainly to promote an amateur game or sport. Section CW 46 was amended in 2014 by supplementary order paper to include the words "or trustee or trustees of a trust". The stated reason was "to ensure that trusts can take advantage of the exemption for bodies promoting amateur games and sports".[6] There is doubt as to whether this amendment was necessary given that charitable trusts that are incorporated under the Charitable Trusts Act 1957 are bodies corporate by definition (under section 13 of that Act), and therefore fall within the concept of "society or association" for the purposes of section CW 46. They were therefore arguably able to take advantage of the exemption even if there was no specific reference to trusts. However, the amendment does make it clear that sporting organisations that are constituted as trusts, but that are not incorporated under the Charitable Trusts Act, are eligible to take advantage of the income tax exemption in section CW 46.

Not-for-profit sporting entities should fall within the definition

45. It is therefore clear that some sporting organisations that are considered worthy of support by the Government are structured as trusts. It does not seem reasonable that the question of whether a sporting organisation falls within the definition of "not-for-profit entity" in clause 24(4)(c) should turn on whether the organisation is structured as an incorporated society or as a trust. It should be clarified that sporting organisations do fall within the definition of not-for-profit entity, and are therefore eligible to receive distributions from incorporated societies on

[6] Taxation (Annual Rates, Employee Allowances, and Remedial Matters) Bill in 2014, SOP No 455 29 May 2014.

winding up, even if they are not themselves structured as an incorporated society.

Recommendation

46. We recommend that:

Clause 24(4)(c) is amended by inserting the words "**charitable, sporting,**" after the word "cultural,"

Clause 27 – Society may amend constitution

Issue

47. Societies that are also registered charities should be required to file notice of amendments to their constitution with the charities regulator only.

Submission

48. Clause 27(4) of the Exposure Draft requires a society to ensure that a copy of an amendment of its constitution is given to the Registrar of Incorporated Societies within 20 working days after the amendment is approved at the general meeting.

49. By contrast, clauses 84(b) and 85(3) provide that the requirements for societies to file financial statements and annual returns with the Registrar of Incorporated Societies do not apply to charitable entities. These are compliance cost reduction measures that permit incorporated societies that are also registered charities to file their financial statements and annual returns with only one regulator (the charities regulator). Part 1 of Schedule 3 of the Exposure Draft proposes to amend section 42(3) of the Charities Act to facilitate information sharing between the charities regulator and the Registrar of Incorporated Societies regarding the particulars of charities' annual returns.

50. Section 40(1)(e) of the Charities Act requires all registered charities to notify changes to their constituting document to the charities regulator within 3 months of the effective date of the change. In practice, we have noticed that many incorporated societies that are also registered charities are inadvertently notifying only one regulator of changes to their constitutions.

51. Given section 40(1)(e), and the practical problems arising from counter-intuitive requirements to notify 2 regulators, the process of amending constitutions should be streamlined in a similar manner to the process for filing financial statements and annual returns, so that incorporated societies that are also registered charities are required to file details of amendments to their constitutions with only one regulator. For consistency, this regulator should be the charities regulator, who should also be required to liaise with the Registrar of Incorporated Societies regarding on-notification of amendments to constitutions.

Recommendation

52. We recommend that:

(i) Clause 27 is amended by inserting the following words: "This paragraph does not apply to a charitable entity."

(ii) The charities regulator and the Registrar of Incorporated Societies be required to liaise to establish mechanisms by which amendments to the constitutions of incorporated societies which are notified to the charities regulator are automatically on-notified to the Registrar of Incorporated Societies.

Clause 39(2) - Qualifications of officers

Issue

53. The factors that would disqualify a person from being an officer of an incorporated society in clause 39(2)(e) and (f) should align with the factors that disqualify a person from being an officer of a registered charity in section 16 of the Charities Act.

Submission

54. Clause 39(2) of the Exposure Draft proposes to list a number of circumstances that would disqualify a person from being appointed or holding office as an officer of an incorporated society.

55. The disqualifying circumstances listed in clause 39(2) generally align with the circumstances that would disqualify a person from being an officer of a registered charity under section 16(2) of the Charities Act (as proposed to be amended by Part 1 of Schedule 3 of the Exposure Draft, and the Charities Amendment Bill 2016 which is currently before Parliament). However, there are 5 exceptions where clause 39 includes a disqualifying factor that is not included, or proposed to be included, in section 16:

    Clause 39(e) - a person who has been convicted of any of the following and has been sentenced for the offence within the last 7 years:

    (i) an offence under subpart 6 of part 4 of the Exposure Draft (which relates to offences under the proposed new Incorporated Societies' legislation);

    (iv) an offence in a country other than New Zealand that is substantially similar to: an offence under subpart 6 of part 4 of the Exposure Draft, a crime involving dishonesty, or a tax evasion offence;

    (v) a money laundering offence, or an offence relating to the financing of terrorism, whether in New Zealand or elsewhere

    and

    Clause 39(f) - a person subject to:

    (ii) An order under section 108 of the Credit Contracts and Consumer Finance Act 2003; or

    (iii) A confiscation order under the Proceeds of Crime Act 1991.

Persons disqualified from being officers of incorporated societies may be officers of registered charities?

56. In other words, the offences listed in clause 39(e)(i), (iv) and (v) and 39(f)(ii) and (iii) of the Exposure Draft would disqualify a person from being an officer of an incorporated society, but not from being an officer of a registered charity. It seems counter-intuitive that the requirements for being an officer of a registered charity should be less restrictive than the requirements for being an officer of an incorporated society.

57. As discussed above, section 16 of the Charities Act is proposed to be amended by the Charities Amendment Bill 2016, which is currently before the Government Administration Select

Committee, to preclude a person convicted of a tax evasion offence under section 143B of the Tax Administration Act 1994, and sentenced for that offence within the last 7 years, from being an officer of a registered charity. However, the Charities Amendment Bill does not propose to include the other 5 matters listed above within section 16.

Review of the Charities Act urgently needed

58. It is desirable that there be consistency between the disqualifying factors in section 16 of the Charities Act, and clause 39 of the Exposure Draft. However, we accept that including the above 5 factors in section 16 of the Charities Act is a policy change that should not be made without proper consultation. This reinforces the need for a post-implementation review of the Charities Act, which was agreed to by Cabinet in 2010, but then controversially cancelled by the Government in November 2012, without consultation. The post-implementation review of the Charities Act needs to be undertaken as a matter of urgency.

Recommendation

59. We recommend that:

(i) the post-implementation review of the Charities Act, that was originally promised in 2005 and agreed to in 2010, but unilaterally and controversially cancelled in 2012, now be undertaken as a matter of urgency; and

(ii) the issue of alignment of factors that would disqualify a person from being an officer of an incorporated society, and factors that would disqualify a person from being an officer of a registered charity, be considered as part of that review.

Clause 48 – Duty of officers to act in good faith and in best interests of society

Issue

60. Officers of societies that are ceasing operations should be permitted to make provision for employees who are or may have been officers of the society.

Submission

61. Clause 48(2) of the Exposure draft proposes that the duty of an officer to act in the best interests of the society may be modified when the society is ceasing to carry on the whole or part of its activities. In that context, an officer may make provision for the benefit of employees or former employees of the society, and their dependants. However, under clause 48(3) an officer may not make such provision for an employee or former employee who "is or was an officer of the society".

62. The words in inverted commas are taken from section 132(2) of the Companies Act 1993. However, they seem less appropriate in the context of incorporated societies, where it is common for the lines between governance and management to be blurred out of necessity. To be unable to make provision for an employee in the context of a society ceasing its operations simply because that person may be, or may at some time in the past have been, an officer of the society would disincentivise people from becoming officers of an incorporated society.

Recommendation

63. We recommend that:

    Clause 48(3) is amended by deleting the words ", but does not include an employee or a former employee who is or was an officer of the society"

Clause 51 - Officer's duty of care

Issue

64. Inconsistent threshold required compared to other law.

Submission

65. Clauses 48 to 55 propose to codify the duties of officers of incorporated societies as they might be described if a court were to comprehensively list them (Consultation Document, paragraph 75). Clause 51 of the Exposure Draft requires an officer to exercise the "care and diligence" that a reasonable person would exercise in the same circumstances.

66. By contrast, section 137 of the Companies Act, on which clause 51 is based, requires a director of a company to exercise the care, diligence *and skill* that a reasonable director would exercise in the same circumstances.

67. The omission of the word "skill" from clause 51 is deliberate. The Law Commission considered that, even where people taking on governance roles in societies are volunteers, and the objectives of a society are of a social nature, it is reasonable that those running the society meet an objective test of diligence and care. However, unlike care and diligence, which are concerned with the manner in which people go about their roles, skill is a measure of competence. Officers of societies may be chosen for reasons other than their management competence. Many are elected or appointed because they have the confidence and support of the membership based on a broader set of considerations. Many also take on roles because it is their turn, or because no one else is willing or available. In such circumstances, the Law Commission considered it was reasonable to expect people to be reasonably careful and diligent when undertaking activities for the society, but that it may not be reasonable to find them wanting because they do not have the necessary competence to undertake the role to a reasonable standard.[7]

68. In principle, we support the application of a standard in the Exposure Draft that it is reasonable for officers of incorporated societies to be expected to meet. However, we are concerned that the common law may continue to require the officers of incorporated societies to meet a standard of skill, even if the legislation does not. If that is the case, little would be gained by omitting the word "skill" from the legislation.

69. We are also concerned about the message that the omission of the word "skill" might send to those taking on the role of an officer of an incorporated society. We anticipate that the concerns of the Law Commission set out above may be able to be accommodated within the word "reasonable" in clause 51.

[7] Law Commission *Incorporated Societies'* Report, page 77.

70. On balance, we consider the word "skill" needs to be retained in clause 51.

Recommendation

71. We recommend that:

    Clause 51 is amended to remove the words "care and diligence" and replace them with the words "care, diligence and skill".

Clause 54 – Use of information and advice

Issue

72. It should be clear that officers of incorporated societies may rely on financial data in exercising their powers and performing their duties as an officer.

Submission

73. Clause 44 of the Exposure draft proposes that officers of incorporated societies may rely on "reports, statements, and other information prepared or supplied, and on professional or expert advice given", in exercising powers or performing duties as an officer.

74. The words in inverted commas are taken from section 138 of the Companies Act 1993. However, they omit the words "and financial data". We accept that these words would arguably fall within the concept of "other information" prepared or supplied, and/or professional or expert advice. We also accept that incorporated societies exist "for purpose" rather than "for profit". However, given the requirement in clause 83 for incorporated societies to prepare financial statements that comply with financial reporting standards prepared by the External Reporting Board, financial data seems an important criterion for officers of incorporated societies to be able to rely on. Certainly, there does not appear to be any reason for these words to be omitted.

Recommendation

75. We recommend that:

    Clause 54(1) is amended by inserting the words "financial data," after the word "statements,"

Clause 66 – Requirement to have at least 10 members

Issue

76. The required minimum number of members should be reduced to 5.

Submission

77. Clause 66(1) of the Exposure draft proposes that a society must continue to have at least 10 members.

78. The minimum number of members required for a society to incorporated is and has always been arbitrary. We support the initiative to reduce the minimum member requirement from 15. We also support the intention to clarify that the minimum member requirement be required to be complied with at all times. However, we recommend that the minimum number be reduced further to a number below 10.

79. It is becoming increasingly difficult for incorporated societies to attract and maintain members. This may be a function of a faster-paced world in which people are eschewing annual general meetings and the like for the immediacy of social media. Allowing a lower minimum number requirement would allow an incorporated society to continue to exist, and to continue to access the benefits of incorporation, even with a smaller number of members. A minimum number of 5 is clearly appropriate for incorporated societies, as it is consistent with the minimum number of members already required for a charitable society to incorporate under the Charitable Trusts Act (section 8(3) of that Act). It is not uncommon, nor inherently undesirable, for all members of an incorporated society to be members of its governing body.

80. If the proposal to reduce the minimum number of members to 5 is accepted, the ability of bodies corporate to be counted as 3 members should be consequentially removed.

Recommendation

81. We recommend that:

(i) Clause 66 is amended by deleting the number "10" where it appears in the heading and in subsection (1) and replacing it in both cases with the number "5".

(ii) Clause 8(1) is similarly amended by deleting the number "10" and replacing it with the number "5".

(iii) Clause 13 (*Body corporate treated as equivalent to 3 members)* is deleted.

Schedule 1 Part 1 – Process for existing societies to become societies under this Act

Issue

82. A process needs to be established for ascertaining which entities registered under the Charitable Trusts Act are in fact charitable societies that will need to transition to the new regime.

Submission

83. Schedule 1 Part 1 of the Exposure Draft sets out the process by which existing societies incorporated as a board under the Charitable Trusts Act 1957 will transition to become societies incorporated under the new Incorporated Societies' Act.

84. Entities incorporated under the Charitable Trusts Act are currently included on the register of charitable trusts maintained at the Companies Office. This register does not distinguish between charitable trusts, the trustees of which are incorporated as a board under section 7 of the Charitable Trusts Act, and charitable societies incorporated as a board under section 8 of the Charitable Trusts Act. All entities incorporated under the Charitable Trusts Act are recorded on the register of charitable trusts as "charitable trusts".

It may not be clear whether an entity incorporated under the Charitable Trusts Act is a trust or a society

85. In practice, we have noticed a number of entities incorporated under the Charitable Trusts Act have been conducting themselves as charitable trusts even though they are in fact charitable societies. The reference on the Companies Office register to their being a "charitable trust" may have contributed to this confusion.

86. Where the entity was established prior to the introduction of the electronic register, there may be considerable uncertainty as to whether they are a charitable trust, or a charitable society. Of course, only charitable societies are required to the new Incorporated Societies' legislation. Incorporated charitable trust boards will be able to remain on the register of charitable trusts and governed by the Charitable Trusts Act.

87. This means that all entities incorporated under the Charitable Trusts Act will need to be individually considered to ascertain whether they are in fact a charitable trust, able to remain on the register of charitable trusts, or a charitable society required to transition to the new legislation. We understand that there are several thousand entities listed on the register of charitable trusts, and that several thousand of these may in fact be charitable societies. Some such entities may need assistance to ascertain whether they are required to transition.

Recommendation

88. We recommend that:

(i) A process is established for ascertaining which entities listed on the register of charitable trusts are in fact charitable societies required to transition to the new regime; and

(ii) Resource be committed to communicating with, and assisting, entities incorporated under the Charitable Trusts Act to ascertain whether they are required to transition to the new regime.

Schedule 1 Part 1 clause 3 – Interpretation

Issue

89. The proposed transition period is likely to be too long.

Submission

90. The definition of "second transition date" in clause 3 of Part 1 of Schedule 1 of the Exposure Draft sets out a transition period of 4 years following enactment of the new legislation.

91. While we understand the reasons behind a transition period of this length, we are concerned that such a transition period may be too long from a practical perspective.

92. Turnover of officers of incorporated societies can be high. Many constitutions set terms for officers of 3 years, or even less. Terms of 1 year are reasonably common. If the proposed legislation is introduced in 2017, enacted in 2018, and does not come fully into force until 2022, there may be a very high turnover of incorporated society governance within the intervening 5 year period. This may lead to a corresponding gap in continuity of institutional knowledge.

93. The net effect of the second transition date is that all officers must be qualified, and the constitution of the society must comply with the requirements of the new legislation (clauses 7 and 12(1) of Part 1 of Schedule 1). In addition, the Registrar may declare that a non-compliant society must be treated as having adopted the standard provisions (clause 13(2) of Part 1 of Schedule 1).

94. As noted in paragraph 48 of the Consultation Document, most societies will already have constitutions that comply with 11 of the 13 requirements in clause 24 of the Exposure Draft. The 2 expected exceptions are the requirements for a disputes resolution clause, and for nominating one or more not-for-profit entities to which any surplus assets should be distributed on the winding up of the society. We do not believe 4 years are needed to meet these requirements.

The experience of the charities register is not likely to be replicated in this case

95. In this context, we note that the difficulties that were experienced in the initial phases of the charities register, following its opening in February 2007, are unlikely to be replicated in the context of the register of incorporated societies. Registration as a charitable entity under the Charities Act requires that the charities regulator be "satisfied" that an entity's purposes are "charitable". What constitutes a charitable purpose can be a notoriously difficult question on which reasonable minds can and do often differ. For example, of the 9 Judges that considered the issue of charitable purpose in the Crown Forestry Rental Trust case, 5 considered the income in question was derived in trust for charitable purposes, but 4 did not, for 2 very different reasons: see *Latimer v Commissioner*

of Inland Revenue [2004] 3 NZLR 157 (PC), [2002] 3 NZLR 195 (CA), [2002] 1 NZLR 535 (HC).

96. By comparison, whether a society qualifies for incorporation under the Incorporated Societies' legislation can be expected to be a simple "tick-the-box" exercise similar to the process required for incorporating companies under the Companies Act. We do not believe such a long transition period is needed.

Recommendation

97. We recommend that:

(i) The definition of "**first transition date**" in clause 3 of Part 1 of Schedule 1 is amended by deleting the words "2 years" and replacing them with the words "1 year".

(ii) The definition of "**second transition date**" in clause 3 of Part 1 of Schedule 1 is amended by deleting the words "4 years" and replacing them with the words "2 years".

Standard Provision 1 – How a person becomes a member of the society

Issue

98. The issue of fees should be addressed in the standard provisions.

Submission

99. Standard provision 1.2 sets out a standard provision for how an applicant becomes a member of a society. It does not make any reference to any requirement to pay membership fees.

100. The Law Commission noted that not all societies impose fees, but considered that if a society wishes to set fees or subscriptions, it must provide a rule for how that will be done (*Law Commission report,* paragraph 7.87). There are a number of educative provisions in the Exposure Draft. It may be helpful to draw attention to the issue of fees in the standard provisions.

Recommendation

101. We recommend that:

Standard provision 1.2 is amended by inserting an additional paragraph (c) as follows:

(c) pay the required membership fee (if any).

Standard Provision 9 – Arrangements and requirements for general meetings

Issue

102. The standard provision needs to be consistent with the underlying legislation.

Submission

103. Standard provision 9.5(b)(iii) provides that the business of the annual general meeting must include the presentation of a summary of any disclosures or the types of disclosures of conflicts of interest made by "committee members" since the last annual general meeting.

104. By contrast, clause 57 of the Exposure Draft imposes a duty of disclosure on "officers" of the incorporated society. "Officer" is defined in clause 36 more widely than simply committee members.

105. The standard provision should be consistent with the underlying legislation.

Recommendation

106. We recommend that:

Standard provision 9.5(b)(iii) is amended by deleting the words "committee members" and replacing them with the word "officers".

Standard Provisions – typographical errors

Recommendation

107. In case it's helpful, we also noticed the following typographical errors in the standard provisions attached to the Consultation Document:

(a) In standard provision 5.14, the word "be" should be "been";

(b) In standard provision 9.9(a), the word "appoint" should be "appointed";

(c) In standard provision 9.13(a), the word "committee" should be "meeting"; and

(d) In standard provision 9.13(b)(ii), the word "is" should be "in".