

INCORPORATED SOCIETIES- NEW DRAFT LEGISLATION WHAT DOES IT MEAN?

UPDATE DECEMBER 2015

Summary

Timing

- The process has begun to replace the 107 year old Incorporated Societies Act
- The time frame is lengthy. Intended introduction to Parliament 2017 with a likely four year transition period
- Plenty of opportunity for feedback – 30 June 2016 for [submissions](#) plus a subsequent Select Committee phase

Key changes proposed

- Basic duties for “committee members” more akin to directors' obligations under the Companies Act 1993, that will be expressly set out in the new legislation
- More specificity around managing conflicts of interest
- Dispute process to be built into constitutions
- Must have a constitution not just “rules”

Key information

Work is underway to replace the Incorporated Societies Act 1908 (the **Act**) with a new piece of legislation to update the law relating to incorporated societies. As many clubs and other sporting organisations are structured as incorporated societies this will be relevant to a large number of sporting bodies in the community.

The changes are still a considerable period away – in November officials released an exposure draft of a new Incorporated Societies Bill (the **Exposure Draft**) that would replace the Act. The Exposure Draft has been released to provide an opportunity for public comment, and the public have until **30 June 2016** to make [submissions](#). At this stage it is intended that a bill will be introduced to Parliament in **2017**. The public will have a second opportunity to make submissions during the select committee process after the bill has been introduced. Once the bill is enacted and comes into force incorporated societies will have a period of up to four years to make changes to their constitutions as required.

The three key messages that we would like to identify for sporting bodies are:

- the changes will give certainty to incorporated societies and their members and enhance protections, and so the Exposure Draft does provide benefits for incorporated societies;
- the law-making process that the Government intends to follow will provide an opportunity for incorporated societies to have their input, either directly or through representative bodies; and
- the length of time before the Exposure Draft is finalised and introduced to Parliament, and in turn before current incorporated societies have to transition to the new requirements, is sufficient to

- enable incorporated societies to, consider how they may be impacted, take advice if necessary and make a measured transition to the new requirements.

In this update we provide some background to the Exposure Draft, and summarise key features of the proposals.

Background - why is the law going to change?

The Law Commission's Report

The Law Commission reviewed the Act and published a report, *A New Act for Incorporated Societies*, in 2013. The Commission saw the role of the Act in providing incorporated societies as having been "*world leading and innovative*", and hence saw its report as representing "*the evolution of this beneficial vehicle, rather than revolution*".

The Commission identified a number of concerns in their report, including a lack of clear guidance for incorporated societies and their members on matters such as governance and resolving disputes. It was also noted that in many cases people were elected to responsible positions within incorporated societies without having a clear understanding of the responsibilities that are involved, and that the current legislation and the constitutions adopted by incorporated societies often provided limited help for external advisers. For example, while the officers of incorporated societies have responsibilities that are similar to those of directors of companies, the Act does not specify these duties directly, unlike the Companies Act 1993, and incorporated societies and their advisers have to look to case law. Similarly the Act is silent on important issues such as conflicts of interest and potential personal liability for an incorporated society's officers. These were identified as the type of problems that could be alleviated with new legislation.

The three main principles that the Commission recognised as important to incorporated societies, and which the Exposure Draft reiterates, are:

- incorporated societies are organisations run by their members, coming together to achieve a common purpose;
- incorporated societies should not distribute profits or financial benefits to their members; and
- incorporated societies should be self-governing and independent of government.

We consider that these principles are vital to the standing of sports organisations that are structured as incorporated societies, and the Commission's recognition of them is very helpful.

The main recommendations that the Commission made, in order to improve on the status quo, were:

- replacing the Act with new legislation;
- setting out a transition period for societies incorporated under the Act to change over to the new requirements;
- specifying a basic set of duties for committee members, using the duties of company directors as a starting point;
- providing a procedure for dealing with financial conflicts of interest;
- requiring incorporated societies to include dispute resolution provisions in their constitutions; and
- providing a model constitution for incorporated societies to use instead of preparing their own.

The Government's response to the Law Commission report

The Government responded to the Commission's report in December 2013, agreeing with all but one of the Commission's recommendations (the outlier was a question relating to Agricultural & Pastoral societies, and so was not relevant to the concerns of sporting bodies). Officials prepared the Exposure Draft to give effect to the recommendations.

The Exposure Draft is certainly a longer document than the Act – 102 pages compared to 29 – but is intended to provide assistance to incorporated societies and their members by setting out more detailed provisions to give more certainty about matters.

How is the Exposure Draft structured?

The Exposure Draft is divided on a part by part basis, with Part 1 containing preliminary matters such as interpretation and commencement provisions. The other parts of the Exposure Draft are as follows:

- Part 2 – establishing an incorporated society;
- Part 3 – operating an incorporated society;
- Part 4 – enforcement;
- Part 5 – structural changes such as amalgamations, liquidations, and deregistrations of incorporated societies; and
- Part 6 – other matters such as the Registrar.

The Exposure Draft also contains Schedules setting out matters such as the transition of existing incorporated societies to the new legislation. We discuss each of these below in turn.

Part 2 - Changes to establishing an incorporated society

The Exposure Draft makes limited changes to the requirements for establishing an incorporated society, with the two most important being:

- the reduction in the number of required members from 15 to 10; and
- the replacement of "pecuniary gain" with "financial gain" – but the existing test is carried over – a society may incorporate for "any lawful purpose other than financial gain".

Other than these key changes, Part 2 largely carries over provisions from the existing law.

Part 3 - Changes to the operation of an incorporated society

Part 3 of the Exposure Draft represents the most important part of the proposed new legislation, as it sets out the day to day rules that will govern how incorporated societies operate. We set out some of the key changes that the Exposure Draft makes to the operation of incorporated societies below.

Constitutions

Probably the most important single change that the Exposure Draft sets out is to replace the current requirement in the Act for an incorporated society to have rules providing for certain matters with a new requirement to adopt a constitution.

In our view the requirement for incorporated societies to prepare a constitution will be the single most important feature of the transition process. In many cases incorporated societies will be able to adapt

existing provisions from their rules. There are, however, two main new matters that are dealt with in the Exposure Draft's requirements for a constitution:

- incorporated societies must put in their constitutions procedures for resolving disputes between members, and between members and the society, including procedures for investigating and dealing with member grievances and complaints concerning the misconduct or discipline of members; and
- incorporated societies must nominate a not-for-profit entity or class of not-for-profit entities to which any surplus assets should be distributed on the liquidation or deregistration of the society.

In addition to these requirements for a constitution, the Exposure Draft also provides for standard constitution provisions to be specified. This is a point of difference from the Law Commission's recommendations, as the Commission had favoured providing a standalone model constitution. Officials have instead opted in the Exposure Draft for a number of standard provisions for a constitution to be prepared, so that individual societies can pick those that would be applicable to them. We expect that these standard form provisions should substantially assist incorporated societies in transitioning to the new legislation.

Officers and committees

The Exposure Draft requires every incorporated society to have a committee with at least three members, and with one of those members being designated a "contact officer" whom the Registrar can contact when needed. The committee will be responsible for the management of the affairs of the incorporated society, in a comparable manner to the board of a company.

In addition to this collective responsibility the members of the committee, together with any other officers designated in an incorporated society's constitution, will have individual duties similar to those of directors of a company under the Companies Act 1993. Officers will also be made subject to rules requiring them to disclose conflicts of interest and refrain from voting when conflicted.

We expect that existing structures within incorporated societies, with set roles such as presidents, secretaries, treasurers, and so on will be able to be carried over to the new requirements set out in the Exposure Draft.

The main issues that we see arising, if the legislation is enacted in its current form, are:

- the need for committees and officers to consider their new obligations;
- the need to seek training and refer to guidance materials for incorporated societies in relation to the new duties and obligations for committees and officers; and
- whether incorporated societies would wish to arrange provide indemnities for their committees and officers, as expressly provided for in the Exposure Draft.

The new proposals highlight the need for officers to understand their obligations. Case law indicates that the standard outlined in the Companies Act already applies within Incorporated Societies, to a large extent, but the Exposure Draft is intended to set down these obligations in a single source,. We consider that it will be important for incorporated societies to have sound governance frameworks in place in order to prevent talented people being deterred from serving on sports boards and committees.

Part 4 - Enforcement provisions

At present the Act is silent on enforcement proceedings in the Courts. The Law Commission noted that in practice a mix of legal remedies have been adopted, with the main ones being contract law; judicial review; and seeking a declaratory judgment under the Declaratory Judgments Act 1908. These all have disadvantages, and are expensive and difficult for all parties involved.

The Law Commission has proposed a two tiered approach to dealing with the general problem of resolving disputes. As noted above in Part 3 all incorporated societies will have to adopt dispute resolution procedures. This should hopefully deal with a high proportion of disputes within incorporated societies.

Where the dispute resolution does not succeed, however, Part 4 of the Exposure Draft is concerned with creating a civil enforcement regime for incorporated societies. This would mean a society, one of its members, or a former member (for a limited period after leaving the society) could apply for Court orders. Under these provisions a Court could make orders to:

- enforce a society's constitution or bylaws;
- declare and enforce an officer's duties if an officer is in breach of those duties; or
- rule that a society has conducted its affairs in a manner that is, or is likely to be, oppressive, unfairly discriminatory, or unfairly prejudicial to one or more members.

The Exposure Draft does provide for a limited power for the Registrar to apply for such orders, but subject to express public interest requirements – these include the principles mentioned above of self-government of incorporated societies and freedom from government intervention; the potential deterrent effect of a particular proceeding; and whether the proposed proceeding is an efficient and effective use of the Registrar's resources.

In addition to these civil provisions the Exposure Draft also proposes the creation of a number of criminal offence, and an infringement offence regime for minor administrative breaches. The new criminal offences follow those recommended by the Law Commission, and include: the dishonest use of a position; making false or misleading statements in documents required under the legislation; and falsification of records.

The use of an infringement offence regime has become more common with recent legislation, and in this case would enable the Registrar to serve incorporated societies with infringement notices for breaches of minor provisions (for example, the failure to register an annual return) and impose an infringement fee of up to \$1,000.

As with the additional duties imposed on committees and officers these new enforcement provisions may be of concern for some officers or potential officers. We consider, however, that it will be important to note that in many cases the dispute resolution provisions would enable disputes to be settled without the risk of litigation. Turning to the criminal law provisions, the adoption of an enforcement regime may lead to the Registrar being more stringent in enforcing minor provisions. Incorporated societies may wish to ensure their record keeping and administrative processes are fully up to date to minimise the risk of infringement notices.

Part 5 - Amalgamation, liquidation and other processes

Part 5 is concerned with the "end of life" processes for incorporated societies, and the means by which incorporated societies might be removed from the Register.

In the case of liquidation the Law Commission found that the Act's liquidation provisions worked well, and these have largely been carried over to the Exposure Draft. In the event of liquidation (or removal from the register), however, the Exposure Draft provides that any surplus cannot be distributed to members, but must instead be distributed to a nominated not-for-profit entity.

In other areas the Exposure Draft moves incorporated companies closer to company law. Part 5 introduces an amalgamation regime, similar to that of companies, and directly cross-references provisions for compromises and voluntary administration.

Part 6 - Register provisions

Part 6 of the Exposure Draft is mostly concerned with carrying over the provisions for the Register of Incorporated Societies, and ensuring that the public has access to relevant information. As such the proposals will have limited impact for incorporated societies.

Transitioning existing incorporated societies

Schedule 1 of the Exposure Draft sets out provisions that will apply to existing societies incorporated under the Act. These societies will need to transition to the new requirements, and do so by a fixed transition date, that will be not less than two years after the date when the new legislation is brought into force. There are some limited exemptions to this general principle, most importantly the contents of constitutions and the qualifications of a society's officers – these will be subject to an extended transition date, four years after the legislation is brought into force.

The rules of an incorporated society will become its constitution on that designated transition date, and so societies will need to review and amend those rules to ensure compliance with the new requirements.

What happens next?

The Exposure Draft has been released so that the public, and especially incorporated societies, would have an opportunity to review the proposed legislation and offer comments. In addition officials are considering hosting a series of seminars in the main centres during 2016 to give stakeholders further opportunities to make submissions. Sport New Zealand will keep partners informed about feedback opportunities

Once interested persons have had an opportunity to make their views heard, officials expect that a revised version of the Bill will be introduced to Parliament in 2017.

What should sporting bodies do?

We recommend that sporting bodies which are incorporated societies should take the opportunity to review the Exposure Draft in light of the summary in this update, and consider whether there are any matters that they may want to make a submission to officials on. We emphasise, however, that there will be further opportunities for sporting bodies to comment and a considerable period of time in which do so.

We recommend that incorporated societies do not commit themselves to any action at this early stage. The Exposure Draft is likely to change before it is introduced to Parliament, and may change further as it

goes through the legislative process. The proposed schedule for implementing the legislation will give an appropriate period of time to make the necessary changes (and any additional changes that incorporated societies may wish to make as part of a "tidy-up" process), and members' time spent or expenses incurred before matters have settled may be wasted.

Incorporated societies should instead take this opportunity to review the Exposure Draft and consider whether there are aspects of the proposed legislation that they wish to comment on. If there are then we suggest that you should also consider a combined submission through the relevant industry forum.

Find out more

The Ministry of Business, Innovation, and Employment's website page on incorporated societies:

<http://www.mbie.govt.nz/info-services/business/business-law/incorporated-societies>

this page has a number of resources, including the Exposure Draft itself, a request for submissions, and the Government's response to the Law Commission's report

The Law Commission's website page on incorporated societies:

<http://www.lawcom.govt.nz/our-projects/incorporated-societies-act-1908>

this page contains links to the Law Commission's report A New Act for Incorporated Societies and earlier work on incorporated societies