A Director's Guide to Administering Companies in New Zealand

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The Legal Framework for Administering Companies

The Companies Act and the company constitution

Since 1 July 1997 all companies in New Zealand have been governed by the Companies Act 1993. This Act is the core legislation dealing with the incorporation, operation and liquidation of companies.

Companies can, if they wish, rely solely on the Act's provisions to provide rules for their governance and administration. However, companies with more specialised requirements can tailor their rules and procedures to their particular circumstances by adopting a constitution.

Do we need a constitution?

Under the Companies Act, a company may have a constitution, but is not required to. A constitution is optional because the Act provides a set of rules that govern all companies registered in New Zealand that don't have constitutions.

The Act contains a set of core requirements that apply to all companies and that cannot be varied or overridden by any constitution. For example, all companies must have at least one director, and he or she must be a natural person.

However, the Act allows a constitution to modify or override many other provisions in the Act dealing with the rights, powers and duties of companies, directors and shareholders. These “presumptive provisions” apply to all companies unless the constitution states otherwise. Other provisions in the Act - “optional provisions” - operate only if they are explicitly adopted by a constitution.

A company registered under the Companies Act may therefore choose to have a constitution to:

- override or modify presumptive provisions
- adopt optional provisions, or
- deal with issues the Act is silent on.

Common constitutional provisions

These are some provisions commonly included in constitutions:

- provisions modifying the rules in the Act for appointing directors, to ensure that certain shareholders have the power to appoint or remove one or more directors;
- provisions allowing the company to insure and indemnify its directors;
- provisions inserting pre-emptive rights - for example, the constitution can provide that current shareholders have the first right to buy shares sold by other shareholders.

PART 1 - DIRECTORS

Directors and Management

The board and its powers

A company’s business and affairs must be managed by or under the supervision of the company’s board of directors.

The board has all the powers necessary for managing and supervising the company’s business and affairs, unless the constitution restricts these powers.

The board of directors manages the company on behalf of its shareholders, often through delegation of day to day management to professional management (i.e. employees).

If a company has only one director, that director is considered to be “the board”. If a company has more than one director, then “the board” is those directors who together meet the required quorum and act as a board of directors. A quorum is normally a majority of directors, but this can be changed in a company’s constitution.

Who is a “director”?

Under the Companies Act, the term “director” means anyone who occupies the position of director, whether or not they have the formal title of “director”.

This means that someone may be considered to be a director if they can tell the board what it should do, or if they exercise powers on the board's behalf, have been delegated duties by the board, or exercise powers or duties with the board's approval, even if they have not been formally appointed. A "director" also includes someone who can instruct an individual director to act in a certain way.

People who are considered to be directors under that extended definition might include:

- shareholders who nominate directors to the board and then instruct them to protect their interests;
- company executives whose advice the board routinely follows;
- lawyers and accountants whose involvement in the company extends to more than just giving professional advice;
- executives, employees or consultants to whom the board has delegated responsibility.

Appointment and removal of directors

Directors are appointed and removed by a simple majority of shareholders. A director must be a natural person, not a body corporate.

A company's constitution can modify these "presumptive" rules. For example, the constitution can require more than a simple

majority for the appointment and removal of directors, or give one or more shareholders or groups of shareholders the right to appoint and remove directors.

Number of directors

A company must have at least one director. There is no maximum number.

Share qualifications

There is no requirement in the Companies Act for a director to hold shares in the company. However, a constitution can require this.

Directors Duties

The law imposes duties on directors. Two key duties are:

- A duty to act in good faith and in the best interests of the company; and

- A duty of care, diligence and skill.

The duty to act in good faith and in the best interests of the company is subjective: the director must genuinely believe that he or she is making the right decision for the company.

A director must exercise the same level of care, diligence and skill that a reasonable director would exercise in similar circumstances. Circumstances to consider are the nature of the

company, the nature of the decision, and the position of the director and the responsibilities which he or she has undertaken.

The Companies Act also imposes other more specific duties on directors, including:

- A duty to comply with relevant legislation and the company's constitution (if it has one);

- A duty not to cause, allow, or agree to the company carrying on of the business of the company in a manner likely to create a substantial risk of serious loss to creditors, commonly referred to as a duty to avoid trading recklessly; and

- A duty to incur obligations only if he or she reasonably believes at the time that the company will be able to meet those obligations.

Breaches of Directors' Duties

Breaches of directors' duties can give rise to a right to damages or compensation. The director may be required to restore the losses suffered by the company as a result of his or her breach, to the extent that those losses were reasonably caused by the breach. A director that breaches the duty to avoid trading recklessly may be liable to the company's creditors.

Acting in the best interest of a parent company

A director's obligation to act in the best interests of the company has been a frequent source of conflict for directors who sit on the

boards of both a holding company and its subsidiary. A particular decision may not be in the best interests of a subsidiary when considered in isolation, though it may be in the best interests of the group of companies. The most common example is where a subsidiary is asked to provide a guarantee for a debt of the parent company.

Directors of wholly owned subsidiaries are permitted to do things that are in the best interests of the parent company, though not in the best interests of the subsidiary, provided the subsidiary's constitution allows this. The same applies to subsidiary companies that are not wholly owned if the subsidiary's constitution allows this and the other shareholders have agreed in advance.

Joint venture companies

A director of a company carrying out a joint venture between the shareholders may do things that are in the best interests of one or more of its shareholders, though not in the best interests of the joint venture company, if the constitution of the company explicitly permits this.

The company secretary

The Companies Act does not require a company to have a secretary. However, in practice a company will need someone to carry out the duties of a company secretary, whether they formally have the position of secretary or whether they act as a delegate of the board.

Interested Directors

Directors must act in the company's best interests. If a director has an interest in one of the company's transactions, the director may face a conflict of interest.

Meaning of "interested"

A director will be interested in a transaction to which the company is a party if the director:

- is a party to the transaction;
- will or may benefit financially from the transaction;
- has a material financial interest in another party to the transaction;
- is a director, officer or trustee of another body that is a party to the transaction or that will or may benefit financially from it, if that other body is not part of a wholly owned group of companies;
- is the parent, child or spouse, or the civil union or de facto partner, of a person who is a party to the transaction or who will or may benefit financially from it, or
- otherwise has a material interest in the transaction, whether direct or indirect.

A director is not considered to be interested in a transaction in situations where the company grants security for its obligations to a party who is unconnected to the director and the director has given some form of guarantee in support of those obligations.

Disclosure by directors

Directors must maintain an “interests register”. This records matters which may give rise to a conflict of interest for directors:

- contracts in which directors are interested;
- directors’ interests in other companies;
- directors’ share dealings;
- directors’ use of company information, and
- directors’ remuneration and other benefits.

Directors can give a general notice disclosing their interest in any transactions that the company might enter into with people or companies named by the director in the notice.

If a director has not given a general notice, or a transaction arises that isn’t covered by the general notice, they must disclose their interest as soon as they become aware of the transaction that creates the conflict.

The disclosure must state the nature and value of the interest, or the extent of the interest if the value can’t be quantified.

Directors do not have to disclose their interests to the board if the interest arises from:

- being paid for their services as a director;
- compensation for loss of office;
- the company making a loan to them or guaranteeing their debts;
- the company indemnifying or insuring them for liabilities they may incur on the company's behalf, or
- a transaction between the company and the director entered into in the ordinary course of business and on usual terms and conditions.

Restrictions on an interested director

The Companies Act allows interested directors to attend meetings of the board that address the transaction in which they are interested. Interested directors can:

- be counted as part of the quorum;
- vote on matters relating to the transaction;
- sign documents relating to the transaction on the company's behalf; and
- do anything else in their capacity as directors in relation to the transaction.

The constitution can modify or exclude those powers.

Avoiding the transaction

If a company enters a transaction in which a director is interested and the director hasn't disclosed his or her interest, it may be open to the company to avoid the transaction if the company doesn't receive fair value. If a company does receive fair value from a transaction in which a director is interested, the transaction cannot be upset.

If a company avoids a transaction, this does not affect "downstream" (subsequent) transactions. An avoided transaction does not affect the title or interest of a person who has acquired the property from someone other than the company, has given valuable consideration for it, and wasn't aware of the circumstances under which the property was acquired from the company.

Use of company information by directors

A director can disclose, use or act on information that they obtain through their position with the company only in the following situations:

- when they do so for the company's own purposes;
- when the law requires it;
- when they disclose information to a person whose interests the director represents, unless the board does not allow this;

- when they disclose information to a person from whom the director takes instructions and whose name the director has recorded in the interests register, unless the board does not allow this; or

- when the board has allowed the director to disclose, use or act on the information after the director has given written notice to the board, and the company will not be prejudiced.

Directors buying or selling shares

The Companies Act imposes obligations on directors who buy or sell shares in their companies. These obligations extend also to the people who have bought shares from, or sold shares to, the director.

Immediately after directors have bought or sold shares, they must disclose to the board:

- the number and class the shares bought or sold;

- the nature of their interest in those shares;

- the price paid or received; and

- the date on which the shares were bought or sold.

The price for which a director bought or sold shares must fairly reflect all information that is known to the director (whether or not it is known to the other party) or publicly available at the time. If a director has bought shares for less than the fair value, he or she will be liable to the seller for the difference. If a director sells

shares for more than their fair value, he or she will be liable to the buyer for the difference.

These rules do not apply to companies that are public issuers. Those companies are covered by the insider trading provisions of the Securities Markets Act 1988, which apply to all people with inside information.

Disclosure in annual report

In each annual report, directors are required to provide details of all disclosures given by directors to the board. This includes disclosures of:

- interests in transactions;
- use of company information;
- share dealings; and
- remuneration and other benefits that they have received.

Directors' certificates

Director's certificates are required for the following:

- an issue of new shares;
- insurance of directors or company officers against liability;
- establishing that the solvency test has been met, whenever that test applies;

- repurchasing, redeeming or financing the purchase of the company's own shares; and

- any amalgamation with other companies.

These certificates have two purposes: first, to concentrate the directors' minds on the decision or action in question; second, to provide a "paper trail" if directors are accused of breaching their obligations by shareholders or a liquidator.

The Act sets out the essential contents for each certificate, but doesn't require them to have any particular form. Directors may sign different copies of the same certificate.

Directors’ Indemnities and Insurance

Indemnity

If its constitution permits it, a company can indemnify its directors and employees to reimburse them for costs they incur in defending legal proceedings brought against them for activities carried out as a director or employee. This includes criminal proceedings. The indemnity can be given only if the director or employee has won the case or been acquitted, or if the proceedings were discontinued.

If authorised by its constitution, a company can also indemnify a director or employee for any liability to third parties, or for costs incurred in defending or settling a claim that relates to that liability. However, directors can’t be indemnified if they committed a criminal act or breached their duty to act in good faith and in the company’s best interests. Similarly, employees can’t be indemnified if they breached a fiduciary duty to the company.

Insurance

In addition to those indemnities, a company can, if the constitution permits it, take out insurance for the benefit of a director or employee covering civil liability for any acts carried out as a director or employee and covering certain costs relating to defending or settling any claims. Directors who vote in favour of the insurance policy must certify that, in their opinion, the cost of the insurance is fair to the company.

Disclosure in annual report

Indemnities or insurance policies must be disclosed in the company’s interests register and in the annual report to shareholders.

Directors' Meetings

The rules for board meetings are set out in the Third Schedule of the Companies Act, and are explained below.

These rules apply unless they are explicitly modified or excluded by the constitution.

Chairperson

The chairperson is elected by the directors. He or she does not have a casting vote.

Notice of meetings

Two days' notice of meetings must be given to every director who is in New Zealand. The notice must set out the date, time and place of the meeting and the matters to be discussed. Directors who are not in New Zealand are not entitled to be notified about meetings.

Holding of meetings

Board meetings may be held at the place, date and time appointed for the meeting, or by teleconference or video conference.

Quorum

The quorum for board meetings is a majority of the directors.

Voting

Each director has one vote.

A director who was present at a meeting is presumed to have voted in favour of a resolution unless he or she explicitly dissented from or voted against the resolution at the meeting. A director who neither abstains nor votes against the resolution will therefore be considered to have voted for it.

Resolutions in writing in lieu of meeting

Instead of passing a resolution at a meeting, the board can pass a resolution in writing by having it signed by all directors who are entitled to receive notice of board meetings. Resolutions in writing may be made up of a number of identical documents (including facsimile copies), each signed or assented to by one or more directors.

PART 2 - SHARES

Shares

Types of shares

Subject to any restrictions in its constitution, the types of shares a company can issue are unlimited. It can issue shares that:

- are redeemable;
- confer preferential rights to distributions of capital or income;
- confer special, limited or conditional voting rights; or
- have no voting rights.

Issue of shares must be "pro rata"

Unless the company's constitution provides otherwise, any new issue of shares must be offered to existing shareholders in proportion to their current shareholding. This allows shareholders to maintain their existing proportional voting and distribution rights. The constitution can allow new shares to be issued other than pro rata to existing shareholders.

No “authorised” or “nominal” capital

There is no limit on the number of shares a company can issue, unless the constitution imposes a limit. Artificial limitations of “authorised” and “nominal” capital no longer exist: companies can issue new shares without first having to increase their capital or having to ensure they have adequate authorised but unissued capital.

“Fair”, not “par” value

Further, shares are not issued at an arbitrary “par” value. Instead they must be issued for a consideration that is fair and reasonable to the company and its existing shareholders; this will fluctuate with the company’s fortunes.

This allows companies to continue to issue shares even if their value has dropped below the original issue price. It also means that company boards should consider the interests of existing shareholders before deciding the price at which to issue shares.

Procedure for issuing shares

Before a board issues shares, it must consider and decide the following matters:

- The price to be paid for the shares and the terms on which they will be issued.
- The reasonable present cash value of the consideration being offered (if the shares are not being bought with cash),

which cannot be less than the amount to be credited for the issue of the shares.

- Whether the terms of issue are fair and reasonable to the company and to all existing shareholders.

Directors who vote in favour of the share issue must sign a certificate confirming those matters, and send a copy of it to the Registrar of Companies within 10 working days.

The same procedure applies when a company issues convertible notes and options.

A company does not have to comply with this procedure if it issues shareholders with fully paid shares from company reserves pro-rata, or consolidates or divides existing shares.

Transferring shares

Under the Companies Act, shares are freely transferable unless the constitution says otherwise. If shareholders want the right to have shares offered to existing shareholders before they're offered for sale to third parties ("pre-emptive rights"), this right will need to be specified in the company's constitution.

Contracts for the issue of shares

A contract with a company in which it agrees to issue shares, options or convertible notes will be an illegal contract, unless the directors have the power to issue the shares and the board has complied with the statutory procedure for issuing shares (see above).

Evidence of ownership of shares

A company must maintain a share register. Being entered on the register as a shareholder is "prima facie" evidence of ownership of the shares (which means it is conclusive evidence if no other evidence is offered to contradict it). The shares are considered to be issued when the shareholder is registered on the share register.

Share certificates are no longer issued as a matter of course: a company must issue a certificate only if a shareholder applies for one. Share certificates are not evidence of a shareholder's ownership of shares. However, if share certificates have been issued, they must accompany any transfer of the shares.

Dividends, Distributions and Discounts

Distributions and the solvency test

Before any distribution (including a dividend) can be made to shareholders, the board must be satisfied that the company will meet the solvency test after the distribution. The directors who vote in favour of the distribution must sign a certificate stating that they believe the company will meet the solvency test and giving their reasons.

The distribution can't be made if, after it is authorised but before it is paid, circumstances change so that the board has reason to believe that the company won't meet the solvency test - for example, if the company has resolved to pay a dividend to shareholders but, before it does so, a major debtor goes into liquidation. In that case, the directors would have to re-evaluate whether the solvency test would be met.

Shareholders may bypass the need for the board resolutions and director's certificates (but **not** the need to meet the solvency test itself) by passing a unanimous resolution (see "Unanimous Assent Agreements" below).

Paying dividends

Companies must pay any dividends equally to all shareholders of the class of shares entitled to receive the dividends, unless the value of the dividend is in proportion to the amount paid-up on the shares.

If shares are issued to shareholders in the place of a dividend, they must be offered to all shareholders of the class that are entitled to receive dividends, in the same proportion.

Reduction in liability is a distribution

If a shareholder's liability to the company is reduced because of an alteration to the constitution or through the company buying its own shares or redeeming shares, the reduction in liability is considered to be a distribution from the company to the shareholder.

Recovering distributions

A company can recover distributions paid to shareholders if the solvency test was not met immediately after the distribution was made. However, the company cannot recover the distribution if:

- the shareholder received it in good faith and wasn't aware that the company would not meet the solvency test; and
- the shareholder altered his or her financial position and has relied on the distribution; and
- it would be unfair to the shareholder for the company to recover all or part of the distribution.

Directors who sign the solvency certificate or who do not try to stop a distribution when the company should not have made it may be personally liable to the company for any amount that cannot be recovered from the shareholders.

In deciding whether a shareholder or director should repay dividends, the courts will consider whether a smaller distribution would have met the solvency test. If it would have met the test, the courts will limit the amount the company can recover to the difference between the smaller distribution and the actual distribution.

Discounts

A company can give shareholders a discount for goods or services bought from the company if the board has decided that the discount:

- is fair and reasonable to the company and its shareholders; and
- is available to all shareholders on the same terms.

"Entitled persons" can implement a discount scheme without the board resolutions if they unanimously resolve to do so (see "Unanimous Assent Agreements" below). A discount scheme must stop operating if the company does not meet the solvency test.

Repurchases and Redemption of Shares

A company may buy back its own shares if:

- the constitution permits this; and
- the company can pass the solvency test before and after the purchase.

There are additional requirements if:

- the shares are listed on the stock exchange and shareholders are notified only after the purchase is completed; or
- the purchase is not made pro rata from all shareholders.

Three methods of buying back shares

A company can buy its own shares in one of three ways:

- by offering to buy a proportion of the shares held by all the shareholders, so that the shareholders' proportional voting and distribution rights are unaffected;
- by buying the shares from one or more shareholders, if all shareholders have given written consent; or
- by buying the shares through a registered stock exchange and notifying shareholders, either before or after the event.

Authorising the purchase

Before a company can buy its own shares, the board must pass a resolution stating:

- that the purchase is in the company's best interests;
- that the price and terms of the offer are fair and reasonable; and
- that all information necessary for assessing the offer is available to the shareholders.

The resolution authorising the repurchase must set out in full the directors' reasons for approving it. The directors who voted for the resolution must also sign a certificate stating that the three conditions above are met. If it becomes apparent that one or more of the conditions may not be met, the board must not proceed with its offer.

The offer to repurchase shares may also allow the company to buy more shares from one shareholder if another shareholder does not accept the offer in full.

Contracts to purchase

Contracts entered into by a company for the purchase of its own shares are enforceable against the company, unless the company would fail the solvency test because of the repurchase. It's up to the company to prove it would fail the solvency test.

After the shares are acquired

Shares bought by the company are usually deemed to be cancelled immediately afterwards. This means that a company cannot hold shares in itself, nor can it act as an intermediary in acquiring its own shares. Shares held as treasury stock are an exception (see below).

Share buy-backs do not prevent a company from issuing further new shares in accordance with its constitution or the Companies Act.

Tax consequences

Directors should consider the income tax consequences of the company repurchasing its own shares. In particular, the dividend provisions in the Income Tax Act 2004 provide for share repurchase transactions to be taxed.

Broadly, when amounts distributed to shareholders fall below specified thresholds (called the “brightline test”), the distributions are taxable in full in the hands of shareholders as dividends; they may, however, have imputation credits attached. When distributions on repurchase exceed those thresholds, the distributions will be deducted from the subscribed capital of the company (to the extent it is available) and returned, free of tax, to the shareholders who sold the shares. If the amount distributed is greater than the company’s subscribed capital, that excess will be taxable, but may have imputation credits attached.

Special rules apply to those shareholders who trade in shares. Where distributions exceed the thresholds or are on-market,

“trader shareholders” are in effect taxed on any gain, and may deduct any loss on sale.

Treasury stock

“Treasury stock” are shares that are temporarily retained by the company after a buy-back, instead of being cancelled. A company may repurchase and retain up to 5% of its shares rather than cancel them, if its constitution permits this.

Voting and distribution rights attached to shares are suspended while those shares held as treasury stock.

If the company sells treasury stock within one year after the buy-back, the repurchase and subsequent sale is treated for tax purposes in the same way as the acquisition and disposal of any other shares, rather than as a distribution of company reserves.

Redemption of shares

Although in strict legal terms redeemable shares are “equity”, they are a hybrid form of equity securities in that they have the characteristics of a debt instrument. For that reason, though in principle the redemption of shares is little different to a company repurchasing its own shares, the Companies Act contains specific provisions dealing with redeemable shares and their redemption.

Companies must not redeem their own shares unless the board believes:

- that the redemption is in the company’s best interests;

- that the redemption price is fair and reasonable; and

- that the solvency test will be met immediately after the redemption.

Directors who vote for the redemption must explain fully their reasons for doing so in the resolution, and must sign a certificate stating that the solvency test will be met. The solvency test must be met even if the shares are redeemable at the shareholders' option.

The board resolutions, opinions and certificates (but not the need to meet the solvency test itself) can be avoided if "entitled persons" unanimously resolve to redeem the shares (see "Unanimous Assent Agreements" below).

Financial assistance for purchase of shares

Companies can provide financial assistance for the purchase of their own shares if:

- the solvency test is met;

- the total amount of assistance is not more than 5% of shareholders' funds (unless the shareholders unanimously agree to a higher percentage);

- the company receives fair value for the assistance; and

- the board has approved the financial assistance and given its reasons for doing so, and the directors voting in favour have signed certificates stating that the assistance is in the

company’s best interest and should be given and that the terms are fair and reasonable.

The factors the board must consider before giving financial assistance, and the resolutions and certificates the directors must sign, are similar to those required when the company makes a distribution to its shareholders or buys its own shares.

The company must be able to satisfy the solvency test immediately after it gives the financial assistance. However, the solvency test is here more rigorous than the usual test. The company cannot include in its assets the value of loans made to assist in the purchase of its shares, whereas it must include any liabilities it may have incurred to provide the assistance. This has the effect of reducing net assets.

The Solvency Test

When does the solvency test apply?

A company must satisfy the solvency test before it:

- pays dividends or other distributions to shareholders (this includes transfers of property and the incurring of a debt or obligation for a shareholder's benefit);
- operates discount schemes for shareholders;
- guarantees shareholders' obligations;
- redeems or repurchases the company's own shares;
- gives financial assistance for the purchase of the company's own shares;
- amalgamates; or
- buys shares in accordance with minority shareholders' buy-out rights.

The solvency test does not have to be satisfied before the company pays salaries, bonuses or other remuneration to shareholders as employees or officers of the company.

The requirements of the solvency test

The basic solvency test has two requirements:

- the company must be able to pay its debts as they become due in the normal course of business; and

- the value of the company's assets must be greater than the value of its liabilities (including contingent liabilities such as guarantees).

In deciding whether the company's assets exceed its liabilities, the directors must consider the company's most recent financial statements and all other circumstances that affect or may affect the value of its assets and liabilities. They may rely on valuations of assets or estimates of liabilities that are reasonable in the circumstances.

PART 3 - SHAREHOLDERS

Shareholders' Resolutions

When shareholder approval is necessary

The approval of shareholders is necessary for:

- a change to the company's constitution
- the appointment or removal of directors (unless the constitution modifies the director appointment powers)
- amalgamation, liquidation or a major transaction.

The constitution may also require that certain other matters must be decided by shareholders instead of by the directors - for example, the payment of dividends or giving authority to borrow.

"Special resolutions"

Resolutions dealing with fundamental matters normally require "special resolutions" - that is, the support of 75% of shareholders. The constitution can require an even higher percentage.

Companies that may wish to increase the percentage are likely to be those with working shareholders who see themselves as partners in the company's business and who believe that all major decisions should be unanimous. The disadvantage is that a shareholder can cause a deadlock even if he or she has only a small shareholding.

Unanimous Assent Agreements

"Entitled persons", acting unanimously, can authorise the company to do certain things that would normally be authorised by the board. In effect, if all entitled persons agree, a range of things can be done without having to comply with most of the normal limitations and procedural requirements.

Who is an "entitled person"?

The term "entitled person" means:

- a shareholder; and
- a person who has been given the rights and powers of a shareholder.

For example, a company's creditors may require, as a condition of a loan, that the constitution grant them certain rights and powers of shareholders, such as the power to call a shareholder's meeting. In that case, the creditor will be an "entitled person".

Often, in a small company the shareholders make up all of the "entitled persons".

What actions can entitled persons authorise?

"Entitled persons" can unanimously agree for the company to do the following:

- Authorise a dividend;
- Approve a discount scheme;
- Acquire the company's own shares;
- Give financial assistance for buyers of the company's own shares;
- Authorise directors' remuneration, loans, guarantees and compensation for loss of office;
- Issue shares; and
- Enter into a transaction with an interested director.

Solvency test must be satisfied

Although all entitled persons may agree to authorise an action, the directors cannot implement it unless they are satisfied that the company will pass the solvency test after the event, and have completed a certificate to that effect.

Shareholder Meetings

There are two types of shareholder meetings: annual meetings and special meetings. As described in this section, many of the rules described below for calling and holding shareholder meetings may be modified by a company's constitution.

Annual meetings

Except for the first annual meeting, which may be held up to 18 months after a company is registered, annual meetings must be held:

- not later than six months after the company's balance date, and
- not later than 15 months after the last annual meeting.

The board is responsible for calling the meeting, and the company must hold the meeting on the day for which it is called. Once the meeting has been called, the directors cannot postpone it.

A company can do away with an annual meeting if everything that is required to be done at that meeting is done by way of written resolution of shareholders (see resolutions in lieu of meeting below).

Disclosure to shareholders of the company's accounts is made through the annual report. Before each meeting, a company must send to shareholders either:

- a copy of its annual report; or
- a notice that tells shareholders how to access an electronic copy of the report and explains to them that they may request a hard copy of the report from the company.

Shareholders cannot waive the right to receive both the annual report and the notice.

Special meetings

All shareholder meetings other than the annual meeting are known as "special meetings". Special meetings are called by the board of directors, or by any person that the constitution authorises to call them. Any business that may be properly dealt with by the shareholders may be considered at a special meeting, if notice has been given (see "Notice of Shareholders' Meetings" below).

Shareholder requests for special meetings

The Act provides that shareholders may request a special meeting. The shareholders requesting the meeting must together have shares carrying at least 5% of the voting rights that may be exercised on the issue.

The request must be in writing. It doesn't have to be signed, but this is preferable. The request should also state the reason for the meeting so that proper notice can be given.

When directors receive a request for a special meeting, they must call the meeting. The Act doesn't specify a time limit, but the directors would have to act within a reasonable time.

Notice of shareholder meetings

Ten working days' notice of meetings must be given to all shareholders, directors and auditors. The notice must state:

- the nature of the business to be transacted, in enough detail to allow a shareholder to form a reasoned judgment about it, and
- the text of any resolution to be submitted to the meeting.

However, the Act does not clearly state that only the business included in the notice may be discussed or voted on at shareholder meetings.

It's advisable for the constitution to specify that business at an annual general meeting shall be:

- the consideration of the annual accounts and annual report,
- the election of directors to replace any who are retiring, and
- the appointment of auditors and the setting of their remuneration,

- any business notified in the notice of meeting, and

- any business of which written notice is given to the board prior to commencement of the meeting.

The constitution should provide that the business of special general meetings shall be restricted to the items given in the notice of meeting.

Inserting these provisions in the constitution will limit the risk of any "ambush" at shareholder meetings, because they will allow resolutions to be ruled out of order if prior notice of them has not been given.

Methods of holding meetings

Shareholder meetings must be held at the place, date and time appointed for them. Unless the constitution provides otherwise, they can also be held by teleconference or video-conference.

Quorum

The quorum for a shareholder meeting consists of shareholders or their proxies who together can exercise more than 50% of the voting power of the company. This can be amended in the constitution to require, for example, that a set number of shareholders must be present or that representatives of certain shareholders must be present.

Votes

Votes can be cast by voice or by a show of hands, except when a poll is required. A poll is necessary if one has been requested by:

- at least five shareholders who have the right to vote at the meeting;
- shareholders representing 10% or more of the total voting rights of the company;
- shareholders holding voting shares on which the total paid-up capital is at least 10% of the total paid-up capital on all voting shares issued by the company; or
- the chairperson.

Unless the constitution states otherwise, the chairperson of a shareholder meeting does not have a casting vote.

Proxies

Proxies must be produced before the start of the meeting, although the constitution may require proxies to be produced by a specified time, which can't be earlier than 48 hours before the start of the meeting. Proxy notices must state whether the appointment is for a particular meeting or for a specific period of time.

Corporations can appoint representatives to act on their behalf in the same way as a proxy might. These appointments can be for as long as the corporation wishes.

Postal votes

The constitution may permit shareholders to cast postal votes. The procedure for postal votes is set out in the Companies Act (Schedule 1, clause 7).

Shareholders' proposals

Shareholders who want to raise matters for discussion or put resolutions before a shareholders' meeting can do so by giving written notice to the board.

If the board receives the notice at least 20 working days before the last day by which notice of the shareholders' meeting must be given, the notice must be circulated at the company's cost. If the notice is received less than 20 working days and five or more working days before that date, it must be sent to shareholders, but at the expense of the shareholders giving the notice. If it is received less than five working days before that date, the board may circulate the notice if this is practicable, at the expense of the shareholders giving the notice.

The shareholders giving the notice have the right to include a statement of up to 1,000 words in support of their proposal. The board does not have to circulate statements it considers to be defamatory, frivolous or vexatious.

Resolutions in lieu of meetings

Resolutions in writing signed by at least 75% of the shareholders (or any higher percentage specified by the constitution) who together hold 75% or more of the voting rights on the question are as valid as if passed at a meeting of those shareholders. This means written resolutions must be signed by 75% of shareholders both by number of shareholders and number of votes.

Management review by shareholders

At a meeting of shareholders, the chairperson must allow a reasonable opportunity for shareholders to question, discuss or comment on the management of the company. The constitution cannot restrict or remove this shareholder right.

Shareholders may pass a resolution relating to the management of the company, but the resolution is not binding on the company. The constitution can modify this rule to allow resolutions of that type to be binding.

Shareholders' Rights

The Companies Act contains provisions that protect minority shareholders, such as "buy-out rights" and the right to inspect company documents.

Minority buy-out rights

If a special resolution of shareholders is passed to approve certain transactions, dissenting minorities can require the company to buy their shares at a fair and reasonable price - this is called a "minority buy-out right".

Minority buy-out rights may be exercised if one of the following company transactions is approved:

- a change to the constitution to impose or remove a restriction on the company's activities;
- the sale of more than half the company's assets or the purchase of assets equal in value to half the company's existing assets (referred to as a "major transaction"- see "Major Transactions" below);
- an amalgamation of the company with other companies;
- changes to the rights, privileges, limitations or conditions attaching to a share;

- changes affecting the pre-emptive rights of shareholders that apply to an issue of shares;
- changes to the procedures the company must follow before it amends shareholder rights; and
- the issuing of further shares ranking equally with or in priority to existing shares, unless the constitution specifically permits the shares to be issued, or the shares are issued in accordance with pre-emptive rights.

Effects of the obligation to buy back

Directors, executives and advisers will need to bear in mind the buy-out rights of dissident minorities. Minority shareholders may directly affect the company's ability to carry out the relevant kinds of transactions, even if the proposals are supported by 75% or more of the shareholders (that is, by a special resolution), because the company will need to find cash to buy the shares of the dissenting minorities if it can't find a third party to acquire them.

The only situation in which the company does not have to buy back the shares is where the company would fail to meet the solvency test immediately after the shares are repurchased and the company applies to the court for an exemption. The court will grant an exemption if:

- the purchase of the shares would be disproportionately damaging to the company;

- the company cannot reasonably be required to finance the purchase of its shares; or

- it would not be just and equitable to require the company to proceed with the purchase of the shares.

A risk in applying for a court exemption is that the court can also make any other order it thinks is appropriate. For example, it could require the company to take a particular action, to pay compensation, or to be wound up (liquidated).

Major transactions

The Companies Act also imposes restrictions on companies entering into "major transactions". A company can enter into a major transaction only if the transaction is approved by a special resolution of shareholders. So, if the transaction is not approved by 75% of shareholders (or any higher percentage specified by the constitution), then the board cannot enter into it.

What is a "major transaction"?

A major transaction is an agreement that will result in:

- the company acquiring assets valued at more than half the value of the company's assets before the transaction;

- the company disposing of more than half of its assets; or

- any transaction in which the company is likely to acquire rights or interests or incur obligations or liabilities that are

more than half the value of the company's assets before the transaction.

When a company enters into contracts on matters that would trigger minority buy-out rights, it would be advisable to have the contracts made conditional on no more than a specified percentage of minorities exercising their buy-out rights. In this way, the company can quantify the cost of having to buy out minorities as part of the overall transaction cost.

Shareholder right to inspect company records

The company must keep the following records available for inspection by any shareholder on request:

- minutes of all meetings and resolutions of shareholders;
- copies of written communications to all shareholders, including annual reports, financial statements and group financial statements for the last 10 years;
- certificates given by directors under the Companies Act; and
- entries in the interests register.

In addition, a shareholder may at any time make a written request to the company for information held by the company. The company must provide the information within 10 working days.

If the company refuses to supply the information, it must give reasons for this. Three situations are specified in the Act as justifying a refusal, and these give general guidance to the board as to when they might properly refuse to disclose information. The three situations are where:

- disclosing the information would, or would be likely to, prejudice the company's commercial position;
- disclosing the information would, or would be likely to, prejudice the commercial position of any other person, whether or not that person supplied the information to the company; or
- the request for the information is frivolous or vexatious.

A shareholder or creditor can also apply to the court for an order to inspect the company's records or other documents, and to make copies of them or take extracts.

PART 4 - ADMINISTRATION

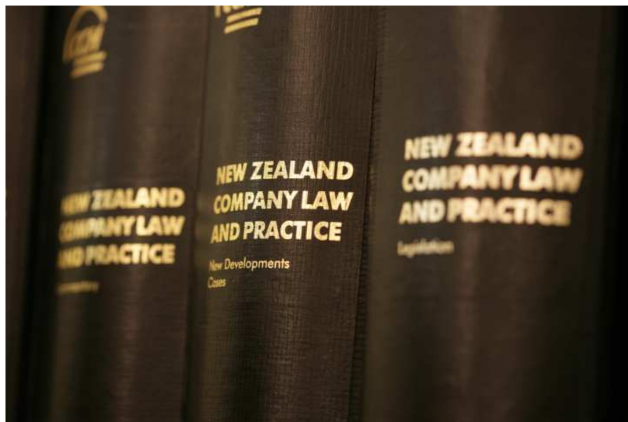
Company Records

A company must keep the following documents at its registered office:

- the constitution;
- minutes of all meetings and resolutions of shareholders from the last seven years;
- the interests register;
- minutes of all meetings and resolutions of directors and directors' committees from the last seven years;
- certificates given by directors under the Companies Act during the last seven years;
- the full names and addresses of the current directors;
- copies of all written communications to all shareholders or all holders of the same class of shares during the last seven years, including annual reports;
- copies of all financial statements and group financial statements for the company's last seven completed accounting periods;

- the accounting records for the company's last seven completed accounting periods; and
- the share register.

A company's records must be kept in a written form or in a form that is reasonably accessible and convertible into a written form. It's the board's responsibility to make sure that adequate measures are taken to prevent and detect any falsification of the company's records.



Entering into Contracts

Documents must be executed by or under the authority of a company's board of directors in one of the following ways.

Arrangements required to be by deed

Deeds may be signed on behalf of the company under the company's name by:

- two or more directors, in which case no witnessing is necessary;
- one director, if there is only one director, in which case his or her signature must be witnessed;
- one director or other person or class of people, whose signature or signatures must be witnessed, if the constitution explicitly permits this, or
- one or more people with powers of attorney from the company.

Arrangements required to be in writing

Arrangements that are legally required to be in writing, such as agreements relating to land, may be entered into in writing by a person who has the company's express or implied authority to do so.

Arrangements not required to be in writing

Obligations that are not legally required to be in writing may be entered into on the company’s behalf in writing or orally by a person acting with the company’s express or implied authority.

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