

# Memorandum

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To: The Institute of Directors  
in New Zealand Inc.

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## **FUTURE DIRECTORS INITIATIVE – STATUS OF FUTURE DIRECTORS**

### **Introduction and Summary**

- 1 Under the Future Directors initiative, individuals will be appointed as observers (called "future directors") of the board of directors of certain companies for a term of one year to gain corporate governance experience.
- 2 We have been asked to confirm that "future directors" should not be treated as directors in a legal sense, which we do below. As a result, participants in the initiative should not be exposed to the potential liabilities which the law personalises to company directors. Participants in listed companies may however be treated as 'officers' for share trading disclosure purposes. In any event it would be prudent for companies to arrange insurance for them as 'officers', and 'future directors' should be required to agree to follow company charters, policies, codes and procedures.

### **Definition of a director**

- 3 The Companies Act 1993 (the *Act*) contains an inclusive definition of "director" that is wider than people who are formally appointed as directors in accordance with the Act and the company's constitution.
- 4 As outlined further below, it covers both:
  - 4.1 a person who is formally appointed as a director; and
  - 4.2 a person who, although not formally appointed as a director, is treated as a director due to certain factors, such as discharging directorial responsibilities, having director powers reserved to them under the constitution or influencing a director or the board.

- 5 The definition aims to capture people who have a real influence on the company's corporate affairs. The focus is on the functions discharged by the individual and not their title. The definition of "director" is included in full in the schedule to this note.

### ***Is the 'future director' a director in the legal sense ?***

- 6 Future directors are not formally appointed in the sense of a shareholder resolution or board appointment to fill a casual vacancy. The appointment is simply a contractual arrangement between the company and the participant (recorded in the letter of appointment).

- Does the future director fall under the extended definition of director?**
- 7 As noted above, the definition of director extends beyond those persons formally appointed as a director. The Act provides that a director includes a person:
- 7.1 “occupying the position of director of the company by whatever name called” (section 126(1)(a));
  - 7.2 in accordance with whose directions or instructions a person referred to in paragraph 7.1, or the board, may be required or is accustomed to act (sections 126(1)(b)(i) and (ii));
  - 7.3 who exercises or who is entitled to exercise or who controls or who is entitled to control the exercise of powers which, apart from the constitution of the company, would fall to be exercised by the board (section 126(1)(b)(iii));
  - 7.4 to whom a power or duty of the board has been directly delegated by the board with that person’s consent or acquiescence, or who exercises the power or duty with the consent or acquiescence of the board (section 126(1)(c)); and/or
  - 7.5 in accordance with whose directions or instructions a person referred to above may be required or is accustomed to act in respect of his or her duties and powers as a director (section 126(1)(d)).
- 8 For some of the above categories, the relevant person is only treated as a director for certain specified purposes only (generally for the director duties regime and the prohibition sanctions).
- 9 Although each of the categories differs slightly, the essential point is that the person must be carrying out director functions or must be directing/instructing those who do.
- 10 We also note that the case law indicates that a relatively substantial level of involvement is required. For example, in *Buzzle Operations Pty Ltd (In Liq) v Apple Computer Australia Pty Ltd* a creditor of a financially distressed company which imposed conditions on that company’s commercial dealings was not treated as a director, on the basis that this was not a sufficient level of influence given that the formal directors of the company were still free to exercise independent judgement to decide whether any course of action was in the company’s best interests.
- 11 We consider that future directors should not fall within the above categories. That is primarily because:
- 11.1 Future directors have no voting rights and do not form part of the quorum of a board meeting;
  - 11.2 The role of future director is limited to observation and participation – future directors are mentees;

11.3 The letter of appointment confirms that future directors are not a position of instruction or corporate control; and

11.4 As a matter of fact, we understand that the board will not act under instructions from a future director and will exercise its own independent discretion on all decisions.

**Insurance and indemnities**

12 Given the nature of the companies likely to participate in the Future Directors Initiative, we expect that they would all hold directors' and officers' liability insurance policies for the benefit of directors.

13 To cover the unlikely event that future directors were considered to be actual directors of the company, we recommend that the companies arrange for their insurance brokers to specifically confirm cover would be available to the future directors as company 'officers' for the purposes of the insurance cover.

**Compliance with company policies**

14 The letter of appointment makes it clear that future directors should comply with listed company securities dealing policies. It would also be prudent to require future directors to file with NZX 'officer disclosure notices' should they be permitted to trade listed security interests.

15 More generally, as the letter of appointment contemplates, future directors should agree to follow company charters, policies, codes and procedures that would ordinarily apply to board members, and observe strict confidentiality of information which comes to their knowledge through observing and participating in board discussions.



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**SCHEDULE: EXTENDED DEFINITION OF 'DIRECTOR'**

**126 Meaning of director**

- (1) In this Act, **director**, in relation to a company, includes –
- (a) a person occupying the position of director of the company by whatever name called; and
  - (b) for the purposes of sections 131 to 141, 145 to 149, 298, 299, 301, 383, 385, 386A to 386F, and clause 3(4)(b) of Schedule 7 –
    - (i) a person in accordance with whose directions or instructions a person referred to in paragraph (a) may be required or is accustomed to act; and
    - (ii) a person in accordance with whose directions or instructions the board of the company may be required or is accustomed to act; and
    - (iii) a person who exercises or who is entitled to exercise or who controls or who is entitled to control the exercise of powers which, apart from the constitution of the company, would fall to be exercised by the board; and
  - (c) for the purposes of sections 131 to 149, 298, 299, 301, 383, 385 386A to 386F, and clause 3(4)(b) of Schedule 7, a person to whom a power or duty of the board has been directly delegated by the board with that person's consent or acquiescence, or who exercises the power or duty with the consent or acquiescence of the board; and
  - (d) for the purposes of sections 145 to 149, and clause 3(4)(b) of Schedule 7, a person in accordance with whose directions or instructions a person referred to in paragraphs (a) to (c) may be required or is accustomed to act in respect of his or her duties and powers as a director.
- (1A) In this Act, **director**, in relation to a company, does not include a receiver.
- (2) If the constitution of a company confers a power on shareholders which would otherwise fall to be exercised by the board, any shareholder who exercises that power or who takes part in deciding whether to exercise that power is deemed, in relation to the exercise of the power or any consideration concerning its exercise, to be a director for the purposes of sections 131 to 138.
- (3) If the constitution of a company requires a director or the board to exercise or refrain from exercising a power in accordance with a decision or direction of shareholders, any shareholder who takes part in –
- (a) the making of any decision that the power should or should not be exercised; or
  - (b) the making of any decision whether to give a direction,
- as the case may be, is deemed, in relation to making any such decision, to be a director for the purposes of sections 131 to 138.
- (4) Paragraphs (b) to (d) of subsection (1) do not include a person to the extent that the person acts only in a professional capacity.