

5. DUTIES AND LIABILITIES

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Introduction

One of the main goals of the Crown Entities Act is to clarify the roles of the board and the responsible Minister.¹⁸⁰ The Act does this by setting out the accountabilities of each party and, in particular, the duties which members owe in relation to their role. These duties are discussed below.

The chapter also covers protections from liability that members, office holders, and employees of statutory entities are given by the Act. The chapter does not cover the obligations of board members and employees under codes of conduct issued under the State Sector Act 1988. These obligations are addressed in chapter 6.

Accountability of boards of statutory entities

Under section 26 of the Crown Entities Act, board members of statutory entities are accountable to the entity's responsible Minister for performing their duties as members. This is analogous with directors of a company, who are accountable to the company's shareholders for the management of the company.

Duties of board members of statutory entities

The common law

Before the passage of the Companies Act 1993, it was not the practice to set out in statute detailed duties of, and restrictions on, directors of bodies corporate. However, the common law imposed a number of limitations of this kind on such directors, stemming from their role as agents of the body corporate.

The classic statement of the fiduciary duty of company directors is in *Aberdeen Rail. Co v Blaikie Brothers*,¹⁸¹ where Lord Cranworth LC stated:¹⁸²

The directors are a body to whom is delegated the duty of managing the general affairs of the company. A corporate body can only act by agents, and it is of course, the duty of those agents so to act as best to promote the interests of the corporation whose affairs they are conducting. Such an agent has duties to discharge of a fiduciary nature towards his principal, and it is a rule of universal application that no one having such duties to discharge shall be allowed to enter into engagements in which he has or can have a personal interest conflicting or which possibly may conflict

¹⁸⁰ This is reflected in section 3(b) Crown Entities Act.

¹⁸¹ (1854) 1 MACQ 461(HL), [1843-60] All ER 249.

¹⁸² Above n 181, 471 (and All ER 252).

with the interests of those whom he is bound to protect. So strictly is this principle adhered to that no question is allowed to be raised as to the fairness or unfairness of a contract so entered into.

The fiduciary duty of directors meant that they were required to account to the corporation for any profit that they made by the use of their powers, even in the absence of fraud or bad faith. Nor were directors permitted to take any secret benefit from their office, whether it be a “commission; bribe; gift ...; secret profits on contracts; or otherwise”.¹⁸³

Fiduciary duties also required directors “to act in good faith, in the interests of the company, to exercise the powers conferred on them for a proper purpose, to exercise reasonable care and skill in the performance of their duties, and to avoid any conflict of interests between their own interests and those of the company”.¹⁸⁴

Further, at common law directors had a duty not to exceed their power:¹⁸⁵

[D]irectors must not do any act which is ultra vires the company or illegal nor without proper sanction, act beyond their own powers including acting without good faith. If they do and the company suffers loss in consequence, the company can recover the amount of its loss from the directors without having to show negligence or dishonesty. Misfeasance also “includes actions within the [directors’] powers which cause loss to the Company and which are not done for its benefit”.¹⁸⁶

The Crown Entities Act duties

The Crown Entities Act sets out a mix of individual duties, based largely on the common law duties described above, as amended by the Companies Act 1993; and public duties, which reflect the position of statutory entities as an integral part of executive government. The two types of duties vary as to –

- whether they are owed by the board as a whole, or by each member individually;
- who they are owed to; and
- what the sanction for breach is.

Like the Companies Act 1993, the intention appears to be to codify the duties of board members.¹⁸⁷

¹⁸³ *Morison’s Company Law* (4th ed) vol 2, (Butterworths, Dec 1992), para 17.44.

¹⁸⁴ Andrew Beck “Company Transactions” in *Morison’s Company & Securities Law* (LexisNexis NZ Ltd, loose leaf, 2004), para 24.1.

¹⁸⁵ Above n 183, para 17.39 (original footnotes removed).

¹⁸⁶ This duty is a particular instance of the fiduciary relationship of directors to the company, in that being trustees of their powers they are liable for misfeasance and breach of trust in the exercise of their powers.

¹⁸⁷ Although see dicta of Heath J in *Benton v Priore* [2003] 1 NZLR 564, para 46.

Importantly, while the Act specifically envisages that some statutory entity boards will contain elected members, it does not differentiate between such members in terms of duties or accountabilities. Members elected or appointed by stakeholders do not have duties in law to those persons, but are in the same position as those appointed by the entity's responsible Minister.¹⁸⁸

One other feature of the Act is that corporations sole may owe duties to themselves. Or put more accurately, corporate status enables the Act to make a conceptual split between the office holder as an individual and the office as a legal entity to enable duties to be owed by the first mentioned to the second mentioned - even a collective duty.

Duty to disclose before appointment

The duties of a potential board member in fact start before appointment, with a requirement in section 31 of the Act to disclose to the responsible Minister of the statutory entity the nature and extent (including monetary value, if quantifiable) of all interests that the person has at that time, or is likely to have, in matters relating to the entity. However, in recognition of how difficult such disclosure may be in relation to some statutory entities, the Act does not make disqualification for failure to comply with this requirement automatic. Rather, the board must notify the responsible Minister of a failure to comply with section 31(1) as soon as practicable after becoming aware of the failure.¹⁸⁹ The Minister may then remove the member if the breach meets the requisite standard for the type of entity, and the Minister considers such removal appropriate.

Collective duties of board members of a statutory entity

The collective duties of the board of a statutory entity are essentially its public duties. Consistent with the clear accountability regime set out in the Act, and the principles of Ministerial responsibility, collective duties are owed to the entity's responsible Minister.

Statutory entities have four collective duties, as discussed below.

(1) Entity must act consistently with objectives, functions, statement of intent, and output agreement

Section 49 of the Act provides that:

The board of a statutory entity must ensure that the entity acts in a manner consistent with its objectives, functions, current statement of intent, and output agreement (if any) under Part 4.

This duty aims to ensure that the entity is managed, and its functions are performed, in accordance with both its Act (passed by Parliament) and its accountability documents, (which have been approved by the responsible Minister).

¹⁸⁸ See discussion in *Collinge v Kyd*, (HC Ak, CIV 2004-404-4828, 15 September 2004) in relation to the position of an elected trustee.

¹⁸⁹ Section 31(2) Crown Entities Act

(2) Functions must be performed efficiently, effectively and consistently with spirit of service to the public

Under section 50:

The board of a statutory entity must ensure that the statutory entity performs its functions efficiently and effectively and in a manner consistent with the spirit of service to the public.

The Controller and Auditor-General noted in the mid-nineties that: “As public bodies, Crown entities have an obligation to conduct their activities in an open and ethical manner, and to play a responsible role in the community as a corporate citizen.”¹⁹⁰ This is reflected in the duty above. The duty would prevent, for example, the entity’s interests prevailing over those of the wider community.

(3) Entity must act in a financially responsible manner

Section 51 of the Act provides that:

The board of a statutory entity must ensure that the entity operates in a financially responsible manner and, for this purpose, that it—

- (a) prudently manages its assets and liabilities; and
- (b) endeavours to ensure –
 - (i) its long-term financial viability; and
 - (ii) that it acts as a successful going concern.

This duty is unique to statutory entities, although it owes its genesis to section 5 of the Crown Research Institutes Act 1992. Unlike the duties to avoid reckless trading and relating to obligations in sections 135 and 136 of the Companies Act 1993,¹⁹¹ which require directors to avoid certain conduct, the duty requires positive action in relation to the finances of a statutory entity.

Reflecting the fact that many Crown entities obtain their revenue from the Crown, the focus of the duty is on prudent management of the entity’s capital assets. The duty also reflects an expectation that the statutory entity will break even.

¹⁹⁰ *Report of the Controller and Auditor-General on Governance Issues in Crown Entities*, November 1996, para 421.

¹⁹¹ Those sections provide that a director must not agree, cause or allow, the business of the company to be carried on in a manner likely to create substantial risk of serious loss to creditors, and that a director must not agree to the company incurring an obligation unless he or she believes on reasonable grounds that the company will be able to perform the obligation when it is required to do so.

(4) Subsidiaries and other interests

Under section 52 of the Act:

The board of a statutory entity must ensure that the entity complies with sections 96 to 101.

Sections 96 to 101 set out the Act's regime for use of subsidiaries and other associates. For board members of statutory entities which do not use subsidiaries or hold other interests that fall within section 100, the duty will have no application.

Sections 96, 100 and 101 set out the processes for acquiring subsidiaries and other interests. Commentary on these sections appears in chapter 4. A particular issue which is covered in that commentary, is the restriction on the acquisition being "for the purposes of carrying out the entities functions".

Sections 97 to 99 cover the other duties in relation to control of subsidiaries.

Oversight of Crown entity subsidiaries

Section 97 provides that a parent Crown entity must ensure "to the extent of its powers" that each of its Crown entity subsidiaries:

- (a) does not do anything that the parent itself does not have the power to do; and
- (b) acts consistently with the parent's objectives and current statement of intent (to the extent they relate to the subsidiary); and
- (c) exercises its powers only for the purpose of performing, or assisting the parent to perform, the parent's functions; and
- (d) does not contravene [the] Act or the entity's Act (if any) to the extent it relates to a subsidiary; and
- (e) complies with a direction given to the parent (to the extent that it relates to the subsidiary);
- (f) does not pay directors of the subsidiary any compensation or other payment or benefit on any basis for ceasing for any reason to hold office; and
- (g) does not perform any of the parent's statutorily independent functions; and
- (h) has a constitution and that constitution contains a statement to the effect that the company is a Crown entity for the purposes of [the] Act; and

- (i) complies with the statutory requirements as to employees that apply to the parent;¹⁹² and
- (j) does not have a member of Parliament as a member.

Under section 98, a parent statutory Crown entity must also ensure “to the extent of its powers” that each of its Crown entity subsidiaries:

- (a) performs its functions efficiently and effectively and in a manner consistent with the spirit of service to the public; and
- (b) pays remuneration to members of the subsidiary only at a rate and of a kind determined by the parent in accordance with the fees framework or after consulting with the responsible Minister; and
- (c) complies with any requirements as to chief executives set out in section 117 in the same way as the parent must do [].

Where a Crown entity subsidiary is jointly owned by two or more Crown entities, section 99 provides that the responsible Ministers of the parents must agree on the restrictions and obligations that the parents must abide by.

“To the extent of its powers”

The extent of the parent’s powers to meet the requirements of sections 97 and 98 will depend to a large measure on the level of its control of the Crown entity subsidiary. If the parent controls 75% or more of the votes attached to the shares, it will have extensive powers to control the subsidiary through its constitution.¹⁹³

In such case, it might be prudent if the Crown entity subsidiary’s constitution contained not only a statement to the effect that the company is a Crown entity for the purposes of the Act,¹⁹⁴ but also provisions:

- mirroring any restrictions on natural person powers that may apply to the parent;¹⁹⁵
- requiring the subsidiary to act consistently with the parent’s objectives and current statement of intent (so far as they cover the subsidiary);¹⁹⁶

¹⁹² In fact, most obligations and restrictions imposed on the parent are also imposed on Crown entity subsidiaries directly (eg. the “good employer” obligation in section 118, and the superannuation scheme provisions in ss 84-84B State Sector Act 1988. Codes of conduct under section 57 State Sector Act may also be expressed as applying directly to Crown entity subsidiaries.) However, section 97(i) may require monitoring of compliance of these provisions, as well as provisions that apply to the parent and not the subsidiary.

¹⁹³ Constitutions may only be adopted or amended by a special resolution (section 32 Companies Act 1993).

¹⁹⁴ Section 97(h) Crown Entities Act.

¹⁹⁵ Section 97(a) Crown Entities Act. Note, this need not include reference to the restrictions on financial powers in sections 160 to 164, or on bank accounts in section 158, as Crown entity subsidiaries are caught by those provisions directly. Nor does it appear that references to restrictions on indemnities and insurance will be necessary as the restrictions in section 164 of the Companies Act are stricter than those in sections 122 and 123 of the Crown Entities Act.

- restricting the business that can be conducted by the company to one that performs or assists the parent to perform one or more of its functions;¹⁹⁷
- providing that the subsidiary must comply with a Ministerial or whole of government direction to the parent (to the extent it is relevant to the subsidiary);¹⁹⁸
- restricting payments to directors of the subsidiary, both in terms of directors' fees and compensation;¹⁹⁹
- providing that the subsidiary must comply with any requirements as to employees or the chief executive that apply to the parent.²⁰⁰

The requirement that a parent must ensure that the subsidiary exercises its powers only “for the purpose of performing, or assisting the parent to perform, the parent’s functions,” would also seem to necessitate a provision in the constitution under section 131(2) or (3) of the Companies Act 1993, permitting the subsidiary’s directors to act in a manner which they believe to be the best interests of the “holding company” (ie. the parent statutory Crown entity), even though it may not be in the best interests of the subsidiary.

The members of the parent board must also ensure that they can meet the duty to ensure the subsidiary performs its functions efficiently and effectively and in a manner consistent with the spirit of service to the public,²⁰¹ perhaps by a monitoring power reserved to the shareholder in the constitution.

Where a statutory entity has a controlling interest in a Crown entity subsidiary but does not have sufficient control to change its constitution, then “the extent of its powers” in regard to the matters in sections 97 and 98 may be rather more limited.²⁰² However, the board of a statutory entity should consider, before taking the interest, how it can best meet the requirements, and thus its duty.²⁰³

It is worth noting that the tight controls which are required by Crown entities of their Crown entity subsidiaries, may make a minority shareholding in such a Crown entity undesirable to third parties. Close attention will no doubt be given to the provisions when third parties are considering the possibility of joint venture arrangements with Crown entities.

¹⁹⁶ Section 97(b) Crown Entities Act.

¹⁹⁷ Section 97(c) Crown Entities Act.

¹⁹⁸ Section 97(e) Crown Entities Act.

¹⁹⁹ Sections 97(f) and 98(b) Crown Entities Act. Without such a provision, the board would be entitled to set its own fees and compensation under section 161 Companies Act 1993.

²⁰⁰ Sections 97(i) and 98(c) Crown Entities Act.

²⁰¹ Section 98(a) Crown Entities Act.

²⁰² In this case, the parent might not have power even to get the constitution altered to provide that the subsidiary is a Crown entity subsidiary. However, whether or not this statement is made in the constitution, the subsidiary will fall within that definition and will be caught, for example, by the restrictions on exercise of financial powers in the Crown Entities Act.

²⁰³ For example, through a shareholders’ agreement.

Deemed director status

The level of control required of subsidiaries also appears to make it inevitable that parent Crown entities will become “deemed directors” of their Crown entity subsidiaries under section 126 of the Companies Act 1993, and that they may therefore be required, among other things, to meet the directors’ duties in sections 131 to 138 of the Companies Act 1993 when exercising their powers in relation to their subsidiaries.²⁰⁴

While these requirements may not necessarily be onerous, particularly in relation to wholly owned subsidiaries, they could potentially cause tension and should be borne in mind during dealings between a parent Crown entity and its subsidiary.

Individual duties of board members of a statutory entity

The Crown Entities Act sets out five individual duties of board members of statutory entities, which in the main reflect the common law duties of directors and agents, although some have been updated to reflect the Companies Act 1993 codification of directors’ duties.

Unlike the Companies Act, which makes the equivalent duties of company directors owed to the company alone, individual duties in the Act are owed to both the entity and the responsible Minister.

(1) Duty to act in accordance with Act

Section 53 provides that:

A member of a statutory entity must not contravene, or cause the contravention of, or agree to the entity contravening, this Act or the entity's Act.

This duty codifies the common law duty not to do an act which is ultra vires or illegal. There is a similar duty in section 134 of the Companies Act 1993.

²⁰⁴ Under section 126 of the Companies Act 1993 the definition of a “director” extends to those in accordance with whose directions or instructions a director of a company may be required or is accustomed to act; and a person in accordance with whose directions or instructions the board of the company may be required or is accustomed to act. Further, “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 [the directors’ duties in] sections 131 to 138 of this Act”.

Similarly, under section 126(3), if the constitution 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 the making of any decision that the power should or should not be exercised; or the making of any decision whether to give a direction, is deemed, in relation to making any such decision, to be a director for the purposes of sections 131 to 138..

(2) Duty to act with honesty and integrity

Under section 54:

A member of a statutory entity must, when acting as a member, act with honesty and integrity.

This duty and the following duty are consistent with the fiduciary duty of board members to the entity. It appears likely that a member who breached the duty by acting without honesty and integrity would also breach the duty of good faith below.

(3) Duty of good faith

Section 55 provides that:

A member of a statutory entity must, when acting as a member, act in good faith and not pursue his or her own interests at the expense of the entity's interests.

The first limb of this duty – the duty to act in good faith is an essential element of the common law fiduciary duty of a director. A good faith requirement is essentially one of proper motive. It appears that the Courts will generally assume that acts are done in good faith.²⁰⁵

The second limb of the duty amends the common law duty that a director must act in what the director believes to be the best interests of the company (now encapsulated in section 131(1) of the Companies Act 1993). The Crown Entities Act does not require a board member to act in the best interests of the entity; but only that he or she does not place his or her own interests above the entity's interest. This no doubt reflects the fact that the board as a whole has public duties under sections 49 to 52. Complying with a duty to act in the entity's best interests, might at times otherwise put board members in a situation of conflict with their collective duties.

(4) Duty to act with reasonable care, diligence and skill

Section 56 of the Act provides that:

A member of a statutory entity must, when acting as a member, exercise the care, diligence, and skill that a reasonable person would exercise in the same circumstances, taking into account (without limitation)-

- (a) the nature of the statutory entity; and
- (b) the nature of the action; and

²⁰⁵ Beck, above n 184, para 24.9, (which means that a person alleging otherwise will be required to prove it).

- (c) the position of the member and the nature of the responsibilities undertaken by him or her.

This duty echoes section 137 of the Companies Act, which raised the former low and subjective threshold for negligence of company directors at common law to an objective standard.

(5) Duty as to confidential information

Under section 57 of the Act:

- (1) A member of a statutory entity who has information in his or her capacity as a member that would not otherwise be available to him or her must not disclose that information to any person, or make use of, or act on, that information, except-
 - (a) in the performance of the entity's functions; or
 - (b) as required or permitted by law; or
 - (c) in accordance with subsection (2); or
 - (d) in complying with the requirements for members to disclose interests.
- (2) A member may disclose, make use of, or act on the information if-
 - (a) the member is first authorised to do so by the board or, in the case of a corporation sole, by the responsible Minister; and
 - (b) the disclosure, use, or act in question will not, or will be unlikely to, prejudice the entity.

Again, this duty codifies the common law duty of directors and other agents not to disclose information. In this regard Halsbury's notes:²⁰⁶

It is the duty of an agent to employ the materials and information obtained by his agency solely for the purposes of the agency, and not to use any materials or information so required, whether his agency has come to an end or not, in any manner inconsistent with good faith, as by divulging them to third parties, or by using them himself in unfair competition with his principal. In the case of alleged misuse of information by competition with the principal, the agent will be liable to account for profits made unless the business in which use is made of the information is outside the scope of the business of the principal and does not compete with it.

²⁰⁶ *Halsbury's Laws of England*, Vol 1(2) Agency, para 90, (original footnotes removed).

The equivalent provision in the Companies Act 1993 is section 145.

Reliance on information

Section 61 of the Acts sets out certain circumstances in which a board member may rely on advice from other people. Members may rely on “reports, statements, financial data, and other information prepared or supplied, and on professional or expert advice given” by any of the following persons:

- (a) an employee of the statutory entity whom the member believes on reasonable grounds to be reliable and competent in relation to the matters concerned;
- (b) a professional adviser or expert in relation to matters that the member believes on reasonable grounds to be within the person’s professional or expert competence;
- (c) any other member or a committee on which the member did not serve in relation to matters within the member’s or committee’s designated authority.

A member may also rely on reports and other material supplied by the Crown. A member may only rely on information from the persons above if he or she:²⁰⁷

- (a) acts in good faith; and
- (b) makes proper inquiry if the need for inquiry is indicated by the circumstances; and
- (c) has no knowledge that the reliance is unwarranted.

This section, which is based on section 138 of the Companies Act 1993, may raise a defence to claims of breach of duty against a member. However, it appears that there may be a point where reliance on information would become unjustified.²⁰⁸

Voting

The meeting procedure for statutory entities in clause 12(4) of Schedule 5 of the Act now provides that all board members present at a board meeting are presumed to have agreed to a resolution unless they make their dissent express. It is therefore important, to avoid potential personal liability in regard to decisions by the entity, that board members who are not in favour of resolutions make it clear that they are not agreeing.

²⁰⁷ Section 61(3) Crown Entities Act.

²⁰⁸ See *Nippon Express (NZ) Ltd v Woodward* (1998) 8 NZCLC 261,765

Employee duties

A full summary of employee duties is beyond the scope of this paper, however, it is noted that at common law, employees owe their employer many of the same duties as the common law duties of directors outlined above. For example, an employee's duties include an obligation to act with reasonable care and skill, to act in good faith in performance of the employee's duties, and not to disclose the employer's confidential information.

Sanctions for breach of duty by a member of a statutory entity

Court actions requiring or restraining all board members

Where the responsible Minister or a member of a statutory entity is concerned that the proposed action of the board may contravene a requirement under the Crown Entities Act or the entity's Act, either of them may apply for a court order under section 60(1) of the Act restraining the board or a member of the board from engaging in the conduct that would contravene the requirement.

Similarly, under section 60(2), the responsible Minister (but not a board member) may apply to the court for an order requiring the board or a member to take any action that is required to be taken under the Crown Entities Act or the entity's Act.

The court may only make an order under section 60 if it is just and equitable to do so and in respect of conduct that has not been completed.²⁰⁹

This provision is similar to powers of shareholders and directors under the Companies Act 1993.²¹⁰

Breach of collective duty

It is the role of the responsible Minister to "oversee and manage the Crown's interests in a statutory entity"²¹¹ and to respond if the duties imposed on entities' boards are not being met. Under section 58(1), the collective duties of the board of a statutory entity are duties owed to the responsible Minister. If the board does not comply with any of its collective duties, all or any of the members may be removed from office.

However, this power of removal is subject to –

- section 58(3), which provides that a person may not be removed -
 - (a) if he or she did not know and could not reasonably be expected to know that the duty was to be or was being breached; or

²⁰⁹ Section 60(3) Crown Entities Act.

²¹⁰ See sections 164, 170 and 172 Companies Act 1993.

²¹¹ Section 27(1) Crown Entities Act.

- (b) if he or she took all reasonable steps in the circumstances to prevent the duty being breached;²¹² and
- sections 36 to 42, which set the standard for removal of members of different categories of statutory entity, and the process for removal.

A member is not liable for breach of a collective duty, other than to be removed from office.²¹³ If members are removed, they are not entitled to compensation or any other payment for loss of office.²¹⁴

Breach of individual duty.

Under section 59, the individual duties of members of a statutory entity are duties owed to the responsible Minister and the entity. If a member does not comply with any of his or her individual duties-

- (a) he or she may be removed from office; and
- (b) the statutory entity may bring an action against the member for breach of the duty.

The power in paragraph (a) is subject to sections 36 to 42, which set out the standard for removal of members of different categories of Crown entity, and the process for removal.

The right to sue in paragraph (b) is the entity's alone to exercise.²¹⁵ Where a member has breached a duty to the entity, the entity may in theory recover both direct loss and any loss it incurs due to third party claims.

There is no explicit power of removal for breach of the Act's conflicts of interest provisions by board members. However failure to comply with those requirements would be breach of the Act and could therefore lead to removal for breach of the member's duty in section 53 not to contravene the Act and, in some circumstances, to an action for damages.

Standards for removal of members of different categories of statutory entity

Sections 36 to 42

The powers to remove members for breach of collective duty or individual duty are explicitly subject to any requirements in sections 36 to 42 of the Act. However, those sections are not explicitly tied back to breach of duty, but also operate independently.

²¹² Section 58(4) makes it explicit that "reasonable steps" do not include applying for a court order to restrain the breach under section 60 of the Act. Nor does it necessarily mean contacting the responsible Minister, although this might be appropriate in some cases.

²¹³ Section 58(5) Crown Entities Act.

²¹⁴ Section 43 Crown Entities Act.

²¹⁵ That is, there is no power equivalent to the Companies Act derivative action provisions that would allow the responsible Minister to take an action on behalf of an entity.

(That is, breach of a duty is not a prerequisite for removal under the provisions). Under sections 36 to 42:

- appointed members of Crown agents may be removed at any time and entirely at the responsible Minister's discretion;²¹⁶
- appointed members of autonomous Crown entities may be removed at any time for any reason that in the responsible Minister's opinion justifies the removal;²¹⁷
- any member of an independent Crown entity and elected members of a Crown agent or autonomous Crown entity may be removed at any time for "just cause";²¹⁸ and
- judges on statutory entity boards may only be removed if all other board members are being removed or if the general law applying to removal from office for judges applies.²¹⁹

Removal is generally by the responsible Minister, except in the case of independent Crown entities, where removal is by the Governor-General, on the advice of the responsible Minister given after consultation with the Attorney-General.

Section 41 provides that a responsible Minister may remove, or advise the removal of, a member "with as little formality and technicality, and as much expedition, as is permitted by –

- (a) the principles of natural justice; and
- (b) a proper consideration of the matter; and
- (c) the different requirements of [the] Act in relation to the different types of statutory entity."

Operation of standards

The standards for removal are generally self explanatory, however in some cases their operation may be curious.

For example, for Crown agents, removal of appointed members under section 36 is entirely at the responsible Minister's discretion and no reasons need be given. However, under section 58(2) of the Act, the power to remove a board member for breach of a collective duty, does not apply if, for example, a member could not reasonably be expected to know that the duty was being breached.

²¹⁶ Section 36 Crown Entities Act.

²¹⁷ Section 37 Crown Entities Act.

²¹⁸ Sections 38 and 39 Crown Entities Act.

²¹⁹ Section 42 Crown Entities Act.

It does not appear that the proviso in section 58(2) is intended to be read as a fetter to the power to remove at discretion under section 36, so that in reality the proviso (and indeed the power to remove for breach of a duty) will have little legal application to appointed members of Crown agents. However, it is accepted that in practice, the existence of the proviso may influence a responsible Minister when he or she is giving “a proper consideration” to the question of removal of an appointed member of a Crown agent under section 41(b) of the Act.

By contrast, for appointed members of autonomous Crown entities, there is a subjective test of “any reason that in the Minister’s opinion justifies the removal”, and reasons must be given. It appears that one reason that may justify removal, in the Minister’s opinion, will be breach of a duty owed to the responsible Minister. In this scenario, the proviso in section 58(2) would be one of the factors a reasonable responsible Minister would take into account when forming an opinion on removal.

“Just cause”

The “just cause” standard is defined as:²²⁰

[including] misconduct, inability to perform the functions of office, neglect of duty, and breach of any of the collective duties of the board or the individual duties of members (depending on the seriousness of the breach).

The first limbs of the definition were typically found in provisions in older statutes relating to removal of board members of statutory corporations and are unlikely to cause problems in interpretation. However, the last part of the definition is new. While the terminology is apparently deliberately woolly, it will, of course, be read in light of the surrounding words, and the purpose of the provision, to limit removal for breach of duty to serious breaches.

Protections against liability of members, employees etc

Application of sections 120 to 126

Sections 120 to 126 of the Act set out the protections from liability of members of statutory entities, their office holders and employees. Committee members are also covered by sections 120 to 126 by operation of clause 15(1) of Schedule 5 of the Act.

The provisions in sections 120 to 126 may have limited application to judges who serve on statutory entity boards. Under section 124 of the Act, a judge who is appointed as member of a statutory entity has the same immunities and limitations or other protections from liability when acting as a member of that entity, as he or she would have as a Judge.

²²⁰ Section 40 Crown Entities Act.

Protections from liability of statutory entity

A member, office holder, or employee of a statutory entity is not liable for any liability of the entity by reason only of being a member, office holder, or employee. While this position is made explicit in section 120 of the Act, it is also a feature of the corporate status of statutory entities.

Immunity from civil liability

Under agency principles, a statutory entity will normally be bound by and liable for the authorised acts of its members, office holders or employees. (Those persons would be entitled when acting as agents to an implied indemnity from the statutory entity for their expenses and any liabilities incurred in the reasonable performance of the agency.²²¹) The entity may also be vicariously liable for wrongs committed by those persons in the course of employment or in the performance of their functions.

However, this does not mean that in some circumstances, the members, office holders or employees of a statutory entity may not incur liability to third parties in their own right. Nor does it mean that they cannot be liable to a statutory entity in relation to acts for which it is vicariously liable, where for example, an employee has breached the requisite duty of care to his or her entity employer.²²²

The immunity in section 121 of the Crown Entities Act excludes some of this potential liability for board members, office holders and employees.

Under section 121(1), a board member of a statutory entity has no civil liability:

- to a third party in respect of an act or omission by him or her in good faith and in performance or intended performance of the entity's functions; or
- to the entity in respect of act or omission by him or her in good faith and in performance or intended performance of the entity's functions, unless the act or omission is also a breach of an individual duty owed by the member to the entity under sections 53 to 57.²²³

Under section 121(2) an office holder, or employee of a statutory entity has no civil liability to *any person* (that is, including the entity) for acts or omissions by him or her, in the performance or intended performance of the entity's functions.

The immunity does not thus protect board members, office holders, and employees against criminal liability, or civil liability in relation to acts and omissions that are not in good faith or not in the performance or intended performance of the entity's functions.

²²¹ *Halsbury's*, Agency, above n 35, para 123

²²² *Lister v Romford Ice & Cold Storage Co Ltd* [1957] AC 555.

²²³ Thus, where this provision applies to committee members, those committee members who are not board members are protected from all claims by the entity in relation to their acts or omissions in good faith in performance and intended performance of the entity's functions.

Nor are board members protected against civil liability to the entity in respect of breach of an individual duty.

Indemnities by the statutory entity of liabilities of members, employees etc

The Act provides in section 122 that a statutory entity may “only” indemnify a member, office holder, or employee in relation to an act or omission in good faith and in performance or intended performance of the entity’s functions. Such indemnity is limited to –

- (a) liability for conduct; and
- (b) the costs of defending or settling claims or proceedings.

This provision is considerably more generous than that relating to indemnification by a company of its directors and employees under the Companies Act 1993,²²⁴ in that it permits, on top of the immunity given in section 122 in regard to civil liability, indemnification of –

- civil liability of a member to the entity for breach of an individual duty owed to the entity (and costs associated with that liability); and
- criminal liability of members, office holders and employees (and costs associated with that liability) –

provided that the liability stems from an act or omission in good faith and in performance or intended performance of the entity’s functions.²²⁵

If an indemnity is given to the extent permitted by the section, it will essentially provide an immunity for members in regard to claims by the entity for breach of individual duty unless the breach results from acts or omissions that are not in good faith, or not in performance or intended performance of the entity’s functions.²²⁶ While this may have little impact on the ability of the entity to sue a member for breach of the duty of honesty and integrity, or the duty of good faith, it would offer significantly higher protection to members against breach of the other three individual duties – the duty not to contravene the Act, the duty of reasonable care, diligence and skill, and the duty not to disclose information.

²²⁴ Section 162 Companies Act 1993.

²²⁵ This was a deliberate policy choice. The provision replaces much more prescriptive provisions that appeared in clauses 161 and 162 of the introduction version of the Public Finance (State Sector Management) Bill 2003. The Departmental Report on the Bill (above n 50) notes at para 452 and 453 that: Because of the possibility that an entity may bring an action against a member, with the outcome of the proceedings ultimately vindicating the member, Advisers do not suggest ruling out indemnities where the entity itself takes action....

In addition, where personnel of the entity have been convicted, although they meet the criteria of the section, depending on the circumstances, reimbursement might undermine the symbolic message conveyed by the offence provision the person has fallen foul of.

²²⁶ In other words, no statutory entity will sue a member for breach of duty, where the conduct falls within an indemnity given to the member by the entity.

So far as criminal liability goes, while indemnities of penalties resulting from intentional criminal activity (for example, fraud) would be excluded by section 122, in theory indemnification of criminal penalties stemming from acts or omissions in good faith is permissible. These might include fines for infringement offences under some Acts, or perhaps traffic offences under the Land Transport Act 1998.

However, it is noted that indemnities in relation to at least some consequences of criminal acts are illegal as being against public policy,²²⁷ and there has been some debate about how far this rule extends or should extend, most recently in regard to insurance against fines and penalties.²²⁸

Statutory entities will need to consider these issues carefully, when deciding whether and to what extent to exercise their power to indemnify members, office holders and employees in accordance with section 122. Such indemnities may either be provided on a discretionary basis after the event, or under a contract of indemnity.²²⁹

It is noted that standard Directors and Officers insurance policies provide reimbursement cover for any amounts an entity is required to pay out under an indemnity of its directors and officers. It may be prudent if statutory entities do enter into indemnities of their board members and employees in accordance with section 122, for them to insure this potential liability under such a policy.²³⁰

Under section 125 of the Act, a member, office holder or employee who is indemnified or insured by a statutory entity in breach of the Act is liable to repay to the entity the amount by which the indemnity or insurance exceeds that permitted by the Act.

Insurance against liability of members, employees etc

Section 123 of the Act provides that:

A statutory entity may effect insurance cover for a member, office holder, or employee of a statutory entity in relation to her acts or omissions, except an act or omission that is-

(a) in bad faith:

²²⁷ *Gray v Barr* [1970] 2 QB 626; affd [1971] 2 QB 554.

²²⁸ See Burrows, Finn & Todd *Law of Contract in New Zealand* (2nd ed, LexisNexis Butterworths 2002) 423. Public policy concerns about indemnification of fines and penalties resulted in a change in 2003 to the Health and Safety in Employment Act 1992, to provide in section 56I(2) that a person must not:

- (b) indemnify, or offer to indemnify, another person for the other person's liability to pay a fine or an infringement fee under [the HSE] Act; or
- (c) be indemnified, or agree to be indemnified, by another person for that person's liability to pay a fine or an infringement fee under [the HSE] Act; or
- (d) pay to another person, or receive from another person, an indemnity for a fine or an infringement fee under [the HSE] Act.

²²⁹ Section 163(2)(a)(i) expressly provides that the pre-conditions on the entering into of indemnities do not apply to indemnities given under section 122.

²³⁰ Anecdotal evidence suggests that 99% of claims on D & O policies are made under the "reimbursement" cover, rather than the personal cover effected by the company for its directors and employees.

- (b) not in the performance or intended performance of the entity's functions.

The power to insure is ostensibly wider than the power to indemnify, in that it permits insurance of acts that are not in good faith, so long as those acts are not in "bad faith". It is not entirely clear what practical implications this difference may have.

What is clear though, is that like the indemnity provision, section 123 permits insurance of –

- criminal liability;
- liability for breach of duty owed to the entity –

so long as such liability does not stem from a bad faith act or omission, or from acts that were not in the performance or intended performance of the entity's functions.

Like the indemnity provision, this provision goes further than that permitted under the Companies Act 1993 in relation to directors and company employees.²³¹ Where statutory entities do decide to effect insurance on behalf of their members, office holders and employees, careful attention will therefore need to be given to the wording of the policy to ensure that it correctly reflects their needs.

Offences

The Act contains a small number of offence provisions, which in the main replicate provisions which previously covered Crown entities through operation of the Public Finance Act 1989. These are –

- section 168 (failure to cause proper accounting records to be kept),²³²
- section 171(1) (which provides it is an offence for a person to knowingly:
 - (a) refuse or fail to produce any information that is in that person's possession or under that person's control in relation to the management, performance, or operations of a Crown entity when required to do so under the Act; or
 - (b) restrict or obstruct any person acting in the discharge of that person's functions or in the exercise of that person's powers under the Act; or

²³¹ Under section 162(5) of the Companies Act, while a company may, if permitted by its constitution, insure its directors and employees for the costs in defending criminal proceedings in which they are acquitted, it cannot otherwise insure criminal liability.

²³² It is a defence to the charge if the member took all reasonable and proper steps to ensure that the section was complied with.

- (c) represent directly or indirectly that he or she holds any authority under the Act knowing he or she does not hold that authority; and
- section 171(2) (offence for a person to make a statement or declaration or give information or certificate required by or under the Crown Entities Act, knowing it to be false or misleading)

Section 135 confirms that members, office holders, and employees of statutory entities and their wholly owned Crown entity subsidiaries are “officials” for the purposes of 105 and 105A of the Crimes Act 1961. Those provisions provide that an official is liable to imprisonment for corruptly accepting or offering bribes, or corruptly using or disclosing information gained in an official capacity for his or her own, or another person’s, pecuniary gain.

Accountability of Crown entity companies

Under section 87, board members of Crown entity companies are explicitly accountable to the company’s shareholding Ministers for performing their duties as members “under this Act” (that is, the Crown Entities Act). This statement recognises that the directors will also be accountable to the shareholding Ministers for the management of the company in terms of the Companies Act 1993.

Additional duties of board members of Crown entity companies

Like the regime for statutory entities, the Act requires members to disclose interests to the shareholding Ministers before appointment.²³³ The Act also imposes three new duties on directors of Crown owned companies, in addition to those owed under the Companies Act 1993.²³⁴

Collective duties of directors of Crown entity companies

Under sections 92 and 93 of the Act, boards of Crown entity companies are given the same collective duties as statutory entities to:

- ensure that the company acts in a manner consistent with its objectives, functions, current statement of intent, and current output agreement (if any); and
- ensure that the company complies with the regime in sections 96 to 101 of the Act in relation to acquisition and control of subsidiaries and other interests.

The commentary on those duties in the previous section will largely apply to Crown entity companies, save that they are not required to comply with section 98 of the Act

²³³ Section 89 Crown Entities Act.

²³⁴ At least the first duty, to comply with the company’s statement of intent may not be new for all Crown entity companies.

(which applies only to statutory entities) or section 101 (which is limited to corporations sole).

The collective duties are owed to the shareholding Ministers and the sanction for their breach is the same as for statutory entities. That is, where there is a breach of a collective duty of the board, all or any members may be removed from office, unless the member:²³⁵

- (a) did not know and could not reasonably be expected to know that the duty was to be or was being breached; or
- (b) took all reasonable steps in the circumstances to prevent the duty being breached.

Again, this proviso casts some doubt on the intended operation of the section. That is, unless a company's constitution provides otherwise, a director of a company may normally be removed by ordinary resolution.²³⁶ There are no pre-conditions such as breach of duty attached.

However, in this regard, section 94(5) provides that the section “does not affect any other ground for removing a member from office, or section 156 of the Companies Act 1993 (which relates to the process for removal of a company director)”. It therefore appears that the proviso is not intended as a legal obstacle to removal of a director. Rather, like the equivalent proviso in regard to statutory entities, it may be a practical curb on the shareholding Ministers' use of their power to remove a director under section 156 of the Companies Act.

Individual duty of directors of Crown entity companies

The third duty which is imposed on Crown entity company directors by the Act is an individual duty to comply with the Crown Entities Act and the entity's Act. Section 95 provides that:

A member of a Crown entity company must not contravene, or cause or agree to the company's contravention of, this Act or the entity's Act (if any).

As was commented in relation to the equivalent duty of statutory entity board members, this appears to be a codification of the director's duty to act within their authority and according to law. As with statutory entities, the Crown entity company may bring an action against a member for breach of the duty. The member may also be removed by the shareholding Ministers.²³⁷

²³⁵ Section 94(2) and (3) Crown Entities Act.

²³⁶ Subject to anything in the company's constitution – see section 156 of the Companies Act 1993.

²³⁷ Section 95(5) Crown Entities Act.

Immunities and indemnities

There are no provisions in the Crown Entities Act relating to indemnities or immunities of Crown entity company board members. The provisions in sections 162 of the Companies Act 1993 will therefore continue to apply.

Under section 91 of the Crown Entities Act, a member of a Crown entity company is not entitled to any compensation or other payment for loss of office.

Crown entity subsidiaries

The Act does not impose any new duties or liabilities directly on directors of Crown entity subsidiaries.²³⁸ Rather, the duties in relation to subsidiaries are imposed on the board members of the parent Crown entities under sections 52 and 93 of the Act.

Subject to anything in an entity's Act, the duties and liabilities of Crown entity subsidiary directors will therefore continue to be governed by the Companies Act 1993. However, it is likely that the constitutions of the subsidiaries will contain a range of powers of shareholders which may impact on directors' actions.

It is noted that parent Crown entities are required to ensure to the extent of their powers, that no compensation is payable to a board member of a Crown entity subsidiary for loss of office.²³⁹

²³⁸ Although the subsidiary itself is caught by a limited number of provisions in the Act.

²³⁹ Section 97(f) Crown Entities Act.