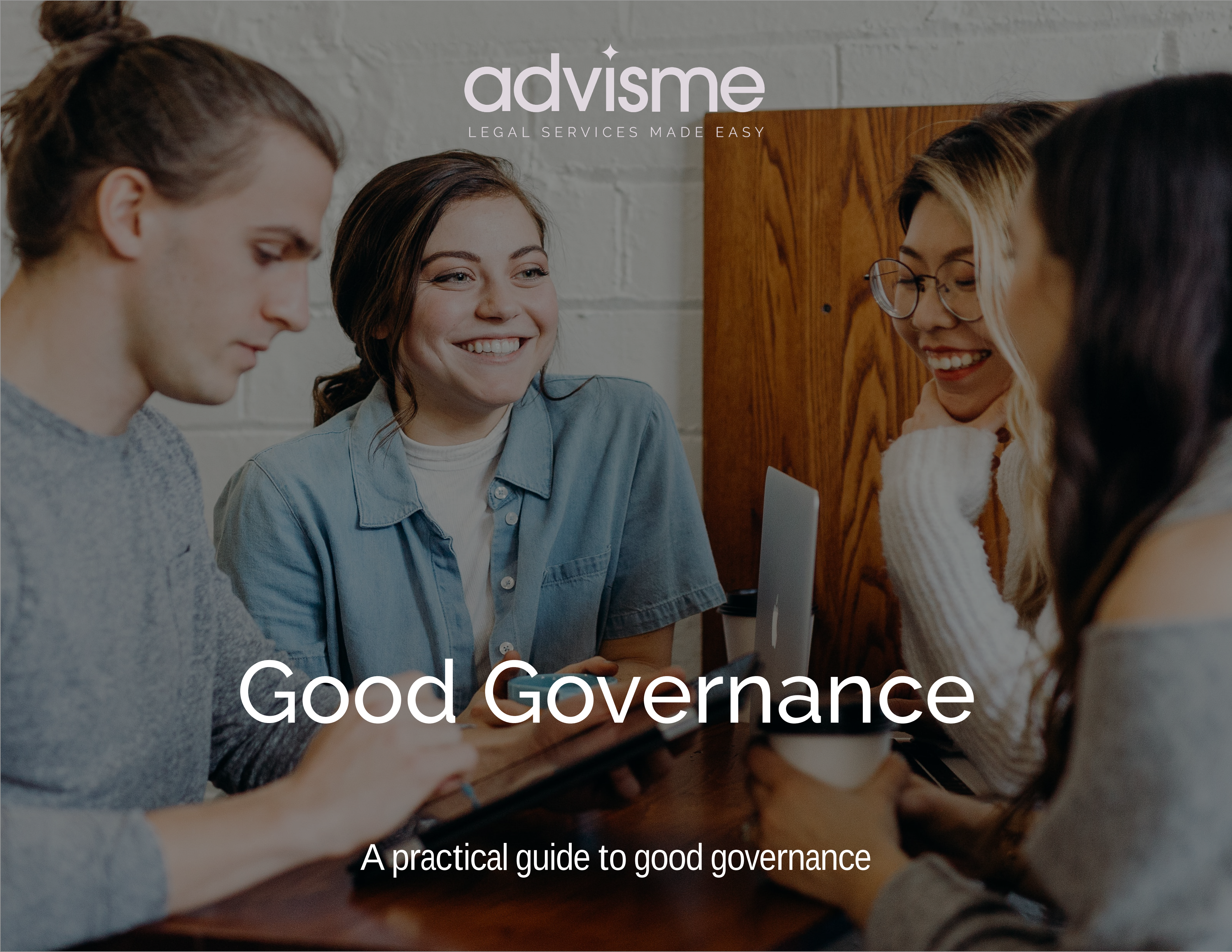

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# Good Governance

A practical guide to good governance

# 1. WHAT IS GOVERNANCE?

As an entrepreneur or small business owner, your main focus is always on your business: developing a customer base, managing finances and employees, finding innovative ways to produce or deliver products and services. It can be easy to let some of the administrative and legal aspects of the business slide, because they seem unnecessary or overcomplicated. Then suddenly you're caught short when it really matters.

Governing your business means taking care of the 'big picture' — things like finances, long-term strategy, and risk management.

Good governance is about the checks and balances and expert advice that keep your business on track. It includes all the practices, processes and policies that help you guide your business in the right direction. Governance is the responsibility of every director — whether your business has one or many. Even if you're not officially a director, governance is good practice for all business owners. Good governance can help you grow your business, stay ahead of risks, improve compliance, and improve trust and reputation.

The good news is that good governance is achievable for all businesses. This e-book explains how to put good governance foundations in place for a company and gives you access to customisable documents to enable you to meet your governance requirements.

# 2. WHY IS GOOD GOVERNANCE IMPORTANT?

Governance helps you to always act in the best interests of the business. More specifically, it can improve the performance of your business, help it become more stable and productive, and unlock new opportunities. It can reduce risks and enable faster and safer growth. It can also improve reputation and foster trust. All these benefits mean your business is more likely to last in the long term.

Governance should be a part of any business, no matter how small. You can start with the basics and make it more structured when you like. You can do it yourself (with other business owners, or advisors to help), or you can get more people involved to create an advisory board or add to your board of directors.

Your business is unique, and your approach to governance will be too. You might go through a number of different governance arrangements as your needs change, typically adding more structure as you grow. It's really up to you and what's best for your business.

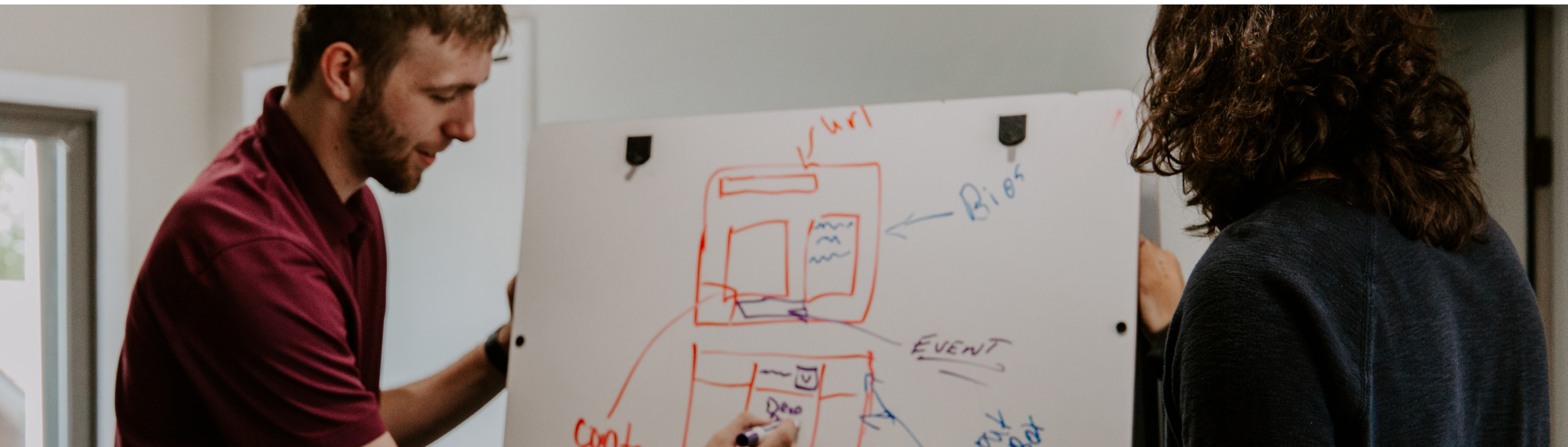
# 3. BUSINESS STRUCTURES

To oversee your business well, you need to have the right legal structures in place.

You can operate your business through many different types of business structure, for example:

- limited liability company: a separate legal entity to the owners of the business;
- trust: trustees have legal ownership of the assets, while beneficiaries have a beneficial interest in them;
- sole trader: a person carrying on business in their own rights, though sometimes under a trading name; or
- partnership: two or more parties working together and acting in each other's best interests.

Each of these different business structures has advantages and disadvantages. There are also tax implications to choosing a structure, so you should discuss your plans with a member of the advisme team and your accountant.



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# 4. LIMITED LIABILITY COMPANY

The most common form of business structure in New Zealand is a limited liability company. The benefits of using a company are:

- The company is a separate legal entity from its owners. The owners only have limited liability for the obligations of the company (barring personal guarantees such as to banks and landlords).
- The company is its own legal "person" - it can enter into contracts and hire employees, for example.
- The owners of the business can control their exposure to financial risk. Even if the business fails, the owners will only lose their investment in the company. Their personal assets will be safe (provided that they have not given any personal guarantees as above).
- If you want to exit the business, it is easy to sell shares in or the assets of a company to a new owner.

*This Guide assumes that you will be using a company for your business structure.*

# 5. KEY LEGAL DOCUMENTS FOR A COMPANY

If you choose to operate your business through a company, you should have the following documents, plans and policies in place:

- A Business Plan and a Business Continuity Plan (in the case of emergencies);
- A Constitution;
- A Shareholders' Agreement (if you are in business with others);
- Employment contracts for any employees and employment policies (if you employ people in your business);
- Delegated authorities for key employees (so employees know their roles and responsibilities);
- Independent contractor agreements (if you use contractors);
- Health and safety policies;
- A Privacy Policy;
- Standard terms and conditions for your business customers;
- If your business has a website, you need a website terms of use policy; and
- Insurance.

# 6. A BUSINESS PLAN AND A BUSINESS CONTINUITY PLAN

Business planning means stepping out of day-to-day tasks to set work goals and decide how you're going to reach them. It makes you think about the 'big picture' both inside your company (strengths and weaknesses) and outside it (opportunities and threats). Your business plan is a platform for you to plan key tasks — for example, how to build the brand, what markets to enter, and which current weaknesses to tackle first.

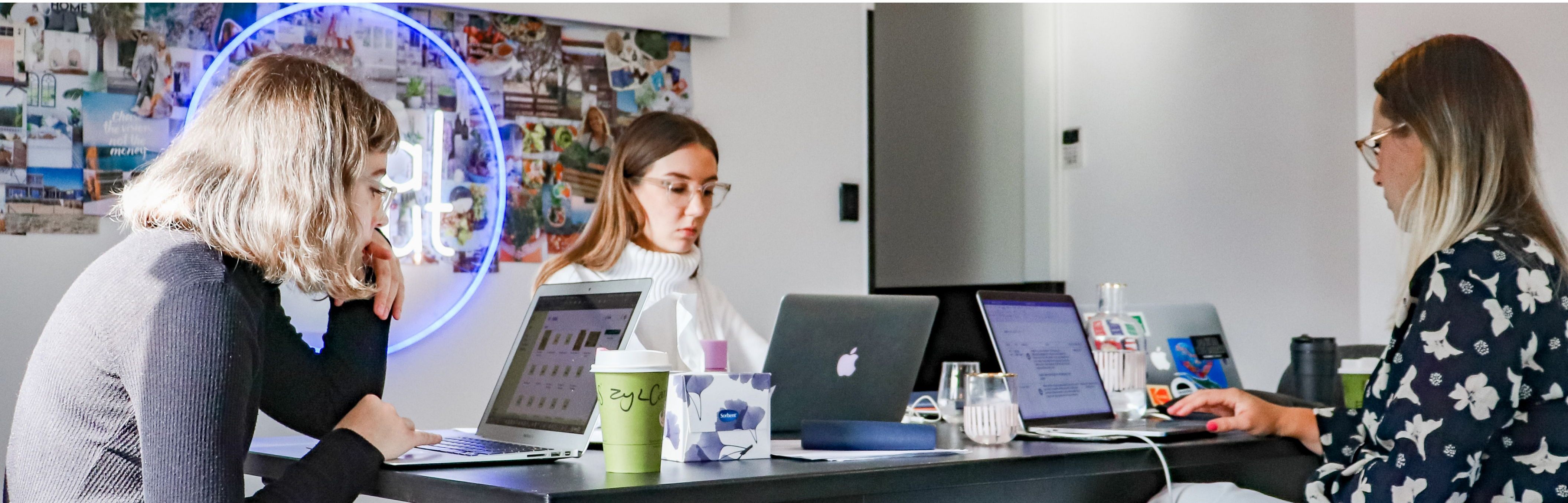
To ensure your business can keep growing or be sustainable over the long term, you need to work on your business plan not only up-front, but also when your business grows or the environment around you changes. Treat the plan as a living document that you'll update when necessary to react to change and stay ready to deal with unexpected events.

A business continuity plan lays out how your business will continue its main tasks after an emergency. This could include natural disasters, equipment failure or a supplier going out of business. If you're unable to perform an important task due to an emergency, continuity planning helps your business to continue functioning. For example, you might plan how you would work from a different location, or how you would work around key staff or services if they weren't available.

# 7. COMPANY CONSTITUTION

The company constitution is a publicly available document that sets out the rules regulating the relationship between the company and its shareholders. It controls the internal management of the company and how it will be governed.  If you incorporate your company without a constitution, it will automatically be governed by the Companies Act 1993, which only sets out the bare basics for governance.

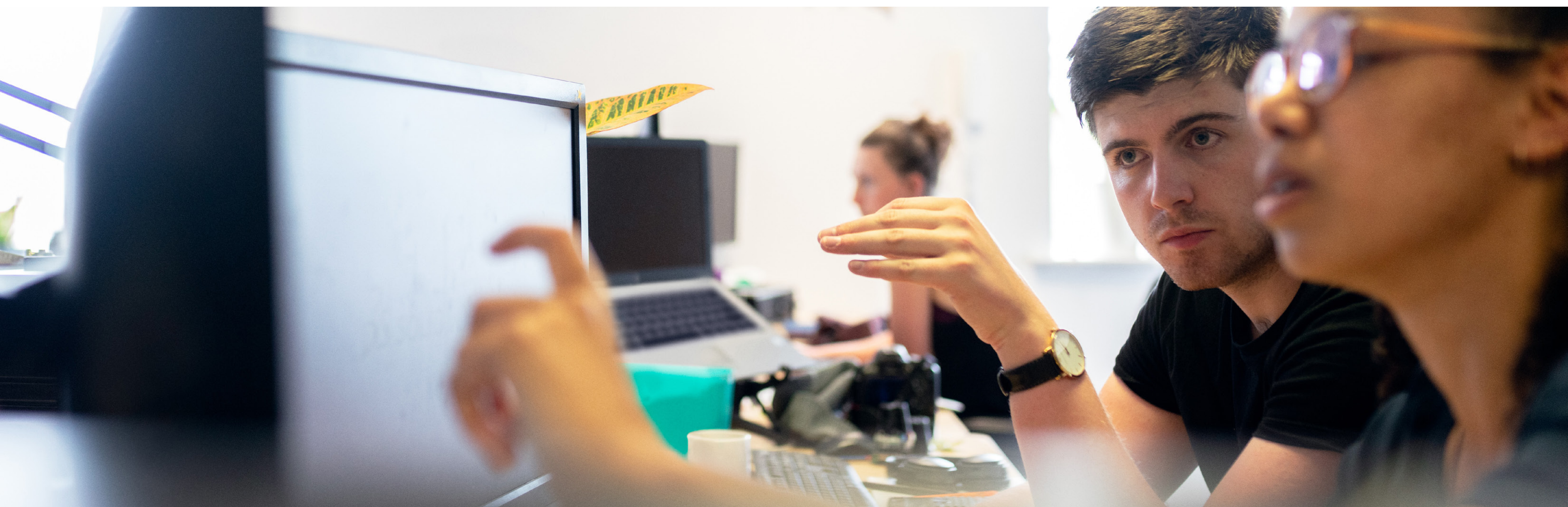
You can use our free constitution bot to create a customised constitution for your company, available at advisme.co.nz.



# 8. SHAREHOLDERS' AGREEMENT

If you are in business with a third party, one of the most important governance documents for a company is its shareholders' agreement (SHA). The SHA sets out the commercial terms of the agreement between the owners of the company. Unlike the constitution, it is not publicly available, so it is a confidential document between the company owners.

If you want to know more, have a look at our Guide to Shareholders' Agreements, available now on our website at advisme.co.nz.



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# 9. OTHER KEY DOCUMENTS

Advisme also provides information on some of the other key documents required. For example:

- Premium Independent Contractor Agreement
- Premium Terms and Conditions of Trade
- Free Privacy Policy
- Free Website Terms of Use

*All these documents are available online at advisme.co.nz*

# 10. INSURANCE

Insurance is an investment in managing your risk. You've probably already thought about fire and natural disasters, theft, and stock damage. But you also need to protect yourself against problems like employment disputes or injury or property damage caused by your products or services.

Liability insurance can protect you against damages and costs from legal action. Indemnity insurance is particularly relevant to people involved in overseeing a business. It can protect you and other directors if you cause damage, or make a mistake of judgement that negatively affects your business. Directors' and officers' (D&O) insurance is the most common type of indemnity insurance for directors.

Insurance can be a significant expense, so make sure your insurance fits your business risks and delivers good value. Expert advisors can help you find the right balance. You may want to speak to an insurance broker about the types of insurance your business needs.

# II. HOW COMPANIES MAKE DECISIONS

As a company has no “brain” its decisions are made by its board of directors. Often these decisions are delegated to management – but the board must maintain ultimate control and oversight.

The size and composition of the board should reflect the scale and complexity of the company’s activities.

Day to day decisions in companies are usually made by the CEO or the managing director, but the board of directors are responsible for setting the company’s strategic aims and helping to achieve them. If your company is small, then the board might just be you. But if your company is growing, it might be worth bringing independent directors on board or having an advisory board to broaden the skills and experience available to the company.

The board of directors is also responsible for keeping the company solvent and reporting to the shareholders. Directors are legally required to act in the best interests of the company.

In small companies, the directors may be the same people as those running the company. Board meetings are a good opportunity to step back from the day to day and focus on where you want the company to go and how it’s going to get there. You should hold regular board meetings and take minutes to record what happens at the meeting.

The board should meet sufficiently regularly to discharge its duties, and be supplied in a timely manner with appropriate information. Too many board meetings may result in the board becoming too operational. On the other hand, too few meetings may pose problems for the fulfilment of the board’s duties. Therefore sufficient attention should be given to the appropriate number of board meetings.

Smaller companies will typically have four to eight board meetings per annum, possibly including a full-day strategic board meeting. However, the exact number of meetings required by the board to fulfil its responsibilities will depend on the specific needs of the company.

# 12. WHAT ABOUT THE SHAREHOLDERS?

In a legal sense, it is the directors rather than the shareholders who operate the company. However, shareholders must be kept informed and have rights in relation to “major transactions”.

Every company must have an annual shareholders’ meeting, unless the company constitution says otherwise, or the directors decide it’s in the interests of the company not to hold one because there’s nothing for the shareholders to decide.

If the company wants to enter into a major transaction, it must have the approval of at least 75% of the shareholders. A major transaction involves buying or selling assets worth more than 50% of the company’s total assets before the transaction, or incurring obligations or liabilities worth more than 50% of the company’s total assets before the transaction.

# 13. ROLE OF THE BOARD

The board of directors are responsible for setting the company's strategic aims and helping to achieve them. One of the key roles of the board of directors is to identify risks and opportunities in your business, and plan for these. For example:

- Changes in competition.
- Changes in technology.
- Changes in law.
- Shortages in appropriate staffing.
- Growth, where does it come from and how is it funded?
- Succession.

Companies like Kodak and Blockbuster are examples of companies whose boards have failed to identify risks and opportunities in their business, but there are many others.

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# 14. HOW TO ACHIEVE GOOD GOVERNANCE IN YOUR COMPANY

There are generally considered to be four pillars of good governance:

- Pillar One - Determining purpose

  Purpose is often achieved by the creation of a company strategy and business plan, which is updated at least yearly after reflecting on the company's financial results and results against plans.

- Pillar Two - Creating an Effective Governance Culture

  Culture flows from the top. Often the board will have a charter setting out expectations and should have processes in place to ensure good governance practice. Think regular meetings, with a set agenda and formal minutes and a feedback loop on tasks and their achievement from the last meeting. Financials should be reviewed along with any health and safety incidents.

  The board should also consider their own expertise and composition. Should an independent director or advisory board be considered? Or a proposed successor be included on the board to grow governance experience?

- Pillar Three - Holding Directors and Management to Account

  It is a key role of the board to appoint senior management, to undertake the operation of the business. The board should put in place delegated authorities, so key employees know their roles, KPI's and responsibilities. It is the job of the board to supervise management and hold them to account.

  It is key that internal controls are put in place to ensure that your reporting is reliable and on time. These controls will help you stay on the right side of the law and deter employees from being tempted into stealing or committing fraud. You can use two types of controls: preventative and detective. Preventive controls are sensible processes that deter errors or fraud. For example, separating duties so that more than one person is needed to authorise and record transactions (such as invoices and expenses). You can also physically limit who can access cash or valuable assets. Detective controls are a safety net for anything you couldn't prevent. This includes regularly checking your finances and correcting any errors. You can also ask an accountancy firm to carry out an external audit of your controls.

- Pillar Four - Effective Compliance

  Director's must be aware of and comply with their legal compliance obligations. These include their directors' duties and the solvency test under the Companies Act 1993, their financial reporting obligations as well as disclosing any conflicts of interest.

# 15. INVOLVE THE RIGHT PEOPLE

Depending on your business and key risks, you may want to have different types of people helping you in your governance activities, such as:

- other business owners can share their experiences from the same industry or the stage of business you're going through, as well as providing useful networks
- accountants can help you understand your cash flow and finances in order to be financially prudent
- lawyers can help you avoid pitfalls — they have often seen many ways things can go wrong for a business
- compliance experts can help you improve practices - eg a health and safety expert can help you identify hazards and make things safer.

As always, the advisme team is happy to discuss your governance structures and processes, including any of the above.

# DISCLAIMER

This guide is intended as a general overview of some of the key legal issues that are likely to be relevant to the governance of a New Zealand Limited Liability Company. It does not claim to be comprehensive or provide specific legal advice or other advice. It is not possible to provide comprehensive advice, whether legal or otherwise, on the matters that may apply in your particular circumstances without knowing those circumstances. Accordingly, matters that you consider to be important, or that may otherwise be considered important, to your particular circumstances or business may not have been addressed in this guide, or may not have been addressed in sufficient detail for your purposes. Consequently, this guide cannot act in any way as a substitute for obtaining your own legal advice and other advice. We have not updated this guide since 1 March 2020 to take account of any subsequent events or changes in law, and we have no duty or responsibility to do so. While every endeavour has been made to supply accurate information, errors and omissions may occur. Accordingly, we do not accept any liability for any loss or damage which may directly or indirectly result from any advice, opinion, information, representation or omission, whether negligent or otherwise, contained in this guide. This guide is subject to our terms and conditions available at www.advisme.co.nz.