

## APPENDIX 3

**A GUIDANCE CODE FOR MEMBERS ON OUTSIDE BODIES**

1. Members are appointed formally by the Council annually to serve on a range of outside bodies, including voluntary organisations and other local government associations.
2. In carrying out that role, Members act both as individuals and as representatives of the Council. What does that entail?
  - 2.1 **Positively**
    - It entails acting according to the rules, constitution and framework set out by the outside body.
    - It entails making independent and personal judgments in line with their duty of care to the outside body.
    - It entails reporting back.
    - It entails behaving ethically and following as far as applicable the Council's Code of Conduct.
    - It entails taking an active and informed role in the management of the outside body's affairs.
  - 2.2 **Negatively**
    - It does not entail representing the political party to which Members owe their political loyalty.
    - It does not entail avoiding taking part in the outside body's discussions and decisions.
    - It does not entail being there in name only and merely turning up to meetings.
3. The role of Members on outside bodies may give rise to occasional uncertainty and perhaps to conflicts of interest. The attached Appendix offers a simple legal guide on the responsibilities of Members and officers. Members are asked to read the guide and if there are issues arising from their particular situation at any time, to contact the Head of Administrative and Member Services for advice.
4. Members will appreciate that this guide and also the Council's Code of Conduct address some of the issues around the possibility of conflicts of interest. In essence, if the outside body comes into conflict with the Council

and the Member is a director or on the management committee of the outside body, it is likely that the Member's prime duty would be to the outside body in the conduct of the outside body's affairs. The Code of Conduct allows a Member to participate in the Council decision-making affecting the outside body to which he or she has been appointed. It is absolutely necessary for the membership of the outside body to be declared at the meeting as an interest when declarations are taken whenever a matter is on an agenda which in any way relates to or affects the outside body.

5. If there is a major dispute between the Council and the outside body, then the Member may be placed in an untenable situation. Before taking precipitate action the Member is advised to seek the advice of the Corporate Director (Internal Services).
6. At the end of the day, it is possible that a Member may find he/she is unable adequately to carry out his/her responsibilities properly, both as a Member of the Council and as a member or director of the outside body. But that would be an exception, and should not deflect Members generally from being prepared to participate in the management and running of outside organisations.

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**A GUIDE TO THE LAW FOR MEMBERS AND OFFICERS ON OUTSIDE BODIES**

This note is for Members and officers who represent the Council on organisations outside the Council, whether as a company director, the trustee of a charity or a representative on a management committee. It simply sets out some of the most important responsibilities. It is not meant to be a comprehensive guide.

**1 GENERAL**

- 1.1 There are some general provisions which apply to Members and officers who act in the role of company director, trustee or member of an incorporated body, such as the committee of management of an unincorporated voluntary organisation.
- 1.2 A Member in this role is under a duty to exercise independent judgment in the interest of the organisation in which he/she is involved. Whilst it is recognised that a Member or an officer may have a commitment to representing the Council on the outside organisation, he/she must be aware that it is his/her responsibility to decide what view to take on any question before the organisation. Where a Member or officer is partaking in an outside organisation in a representative capacity, he/she must declare that fact to the organisation. There will be a fine line to tread between his/her duty to the organisation and to the Council.
- 1.3 The bottom line is that in the end, the Member or officer in acting as a director/trustee or member of a management committee or an organisation, must act in accordance with the interests of that organisation. A mandate from the Council to vote one way or the other would put the Member or officer in breach of the duty to the organisation. It is permissible to take account of the Council's wishes, but not to vote simply in accordance with them. The overriding duty in considering an item before the outside organisation is to vote in accordance with the interests of that organisation.
- 1.4 A Member or an officer in this role must also ensure that avoidable loss is not incurred in managing the organisation. He/she cannot avoid this responsibility by not reading the papers or failing to ask for appropriate reports. He/she will be expected to seek professional advice where appropriate.
- 1.5 A person responsible for the management of an outside organisation can be sometimes the subject of insurance cover or an indemnity from the organisation. Membership of an outside body can give rise to personal liability so it is very important from the point of view of the Member or officers to ensure that the organisation is properly, effectively and efficiently run and operates within the limits of its powers and observes all regulatory requirements.
- 1.6 The Council provides an indemnity in certain circumstances where a Member is acting as the Council's representative on an outside body, but only to the extent that the Member acted in a reasonable manner and in good faith.

## 2 COMPANIES

- 2.1 On incorporation a company becomes a separate legal entity which can hold property in its own right, enter into contracts and sue and be used in its own name. The company is distinct from its shareholders and members. In the case of a limited liability company, the liability of members of the company is limited to the amount they paid or agreed to pay when they joined the company. This can be as little as £1.
- 2.2 Companies limited by shares are those which have a share capital (eg 1000 share of £1 each). Each member of the company holds shares and received a share in the profits made by the company according to the value of the shares held. Shares can be sold. Companies limited by guarantee are those when there is no shareholding. Instead, each member of the company agrees that in the event of the company being wound up they will agree to pay a certain amount. This may also be as little as £1. This form of company is the most usual in the public and voluntary sector, particularly where charitable status is sought.
- 2.3 The management of a company is generally the responsibility of a board of directors. The powers of the directors are usually set out in the company's Articles of Association (the rules each company has to govern its internal management). Sometimes even though a company has been incorporated the directors may be referred to as members of the committee of management, governors or even trustees. However this does not change their status as directors. Conversely, sometimes officials are called directors but they are not members of the board. Again their status will not be affected. Directors are those who are appointed by the company to act in the capacity.

### 2.4 Directors' Duties

A director is an agent of the company. His/her prime duties are as follows:-

- (1) **A fiduciary duty** to the company (not individual shareholders) to act honestly and in good faith and in the best interests of the company as a whole. Directors are therefore in the position of "quasi trustees" who must take proper care of the assets of the company. the fiduciary duty of the director towards the company is very similar to the fiduciary duty of Councillors to the Council Tax payers of the District.
- (2) **A general duty of care and skill** to the company, but a director requires no greater skill than might reasonably be expected of someone of that individual's particular knowledge and experience. A director is not deemed to be an expert, but is expected to use due diligence and to obtain expert advice if necessary.

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- (3) Like a Councillor in respect of Council decisions, the director is under a duty to **exercise independent judgement**, though it is permissible for him/her to take account of the interests of a third party which he/she represents. In such a case the director must disclose that position and treads a fine line between the interests of the company and the party represented (in this case the Council). The director cannot vote simply in accordance with a Council mandate. To do so would be a breach of duty.
  - (4) **No conflict.** There may be actual or potential conflicts between the interests of the Council and the interests of the company. In such circumstances the only proper way for the conflict to be resolved is for the Councillor to resign either from the company or from the Council.
  - (5) Directors are **not allowed to make a private profit** from their position. They must therefore disclose any interests they or their family may have in relation to the company's contracts. Whether they are then allowed to vote will depend on the Articles of Association.
  - (6) Directors must **ensure compliance with the Companies Acts** in relation to the keeping of accounts, and that the relevant returns are made to the Registrar of Companies. Failure to do so incurs fines and persistent default can lead to disqualification as a director.

## 2.5 Directors' Liabilities

- (1) The company's identity must clearly be shown on its stationery. The company number, place of registration, registered office address and if any of the directors' names are shown then they must all appear. Non compliance is an offence and the directors and company officers can be fined.
- (2) A company can only act within the scope set out in its Memorandum of Association (the document which sets out the objects of the company). Those directors knowingly causing the company to act beyond the activities set out in the Memorandum will be liable personally. In very limited circumstances it is possible for the actions of the directors to be ratified by the members of the company.
- (3) A director may also be liable for breach of trust, if he/she misapplies the money or property of the company. Directors may also be liable if they fail to take action to prevent the breach of a co-director of which they are aware.
- (4) In the event of failure to act in accordance with the best interests of the company, or if a director uses his/her powers improperly or makes a personal profit from his/her position as director, then the director may be personally liable for loss to the company and may be required to give the company the personal profit made.
- (5) If the level of skill and care shown by a director falls below that which could be reasonably expected and the company suffers loss, the director will be liable

to the loss incurred. However if it believes the director acted honestly and reasonably, a Court may excuse the director the liability.

- (6) If a director knows or ought to know that there is no reasonable prospect of the company avoiding liquidation, a Court may require that director to contribute to the company's assets on liquidation if the company continues to trade. This is known as wrongful trading. No such order will be made if the Court is satisfied that the director took all reasonable steps to minimise the loss to creditors. If a director has concerns about the company's financial position he/she would be well advised to inform the other directors and seek advice from the company auditors. He/she should try to ensure that further debts are not incurred.
- (7) A director will also be liable if his/her knowledge the company carries on business with intent to defraud creditors or any other person, or for any other fraudulent purpose. Fraudulent trading can also lead to disqualification from acting as a director.
- (8) All cheques and similar documents which purport to be signed on behalf of the company must bear the company name. Where they do not, the director signing on behalf of the company may be liable to a fine and may also be liable to the payee if the company fails to honour the cheque. It is therefore wise for directors to make sure that all documents they sign on behalf of the company state very clearly that they act as agent for the company (eg Director, for and on behalf of.....).
- (9) A third party who enters into a contract on the assumption that a director has power to bind the company, may be able to claim damages against the director if it subsequently transpires that the director had no such power. Directors would be well advised to ensure that contracts are approved by the board and that the authority to enter into any contract has been properly delegated before signing it.
- (10) Though company liability ceases on dissolution, the liability of the directors (if any) may still be enforced after dissolution.

## 2.6 Indemnities

Directors cannot be indemnified against liability arising out of negligence, default, or breach of duty or trust. However the company's Articles of Association may allow for directors to be indemnified by the company in respect of the cost of defending such proceedings if the director is granted relief by the Court or acquitted. It is lawful for companies to purchase insurance to protect its directors against claims of negligence, breach of duty, trust, default. Directors would be well advised to ensure that such a policy of insurance is maintained at all times.

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## 2.7 Local Authorities (Companies) Order 1995

- (1) This Order, made under the Secretary of State's powers contained in Part V of the Local Government & Housing Act 1989, sets out rules concerning local authorities' involvement in "regulated companies" which are subject to extensive controls, and their involvement in other companies where a number of rules apply.
- (2) "Regulated companies" are so defined if they are controlled or influenced by the local authority. "Influenced companies", under the effective control of the local authority, will be subject to capital finance regime and special propriety controls. In broad terms, the test as to whether companies are local authority influenced is whether the local authority has the right to, or in fact does, exercise a dominant influence over the company in question.
- (3) The original concept of controlled, influenced, and minority interests in companies were introduced by the 1989 Act. "Influenced" means at least 20% interest. The concept in the 1989 Act stands, but the Order introduces the term "regulated".
- (4) Councillors who are directors of outside companies to which they have been nominated by the Council are under the following obligations:-
  - (a) that the remuneration they receive from the company should not exceed that received from a local authority, and should be declared;
  - (b) to give information to Councillors about their activities as required by the local authority (save for confidential information), and
  - (c) to cease to be a director immediately upon disqualification as a Councillor.

## 3 INDUSTRIAL AND PROVIDENT SOCIETIES

- 3.1 These are corporate bodies formed under Acts of Parliament which created this type of organisation and registered with the Registrar of Friendly Societies. A common example of these is a housing association. However, a Society can carry on any trade or business but must either be a co-operative society or carry on its trade or business for the benefit of the community, so it is appropriate for it to be registered as a society and not a company.
- 3.2 Instead of a board of directors the Society is run by a management committee. Members of the Society hold shares in it and their position is similar to that of shareholders in a company.

- 3.3 The responsibilities, duties and liabilities of members of the management committee are similar to those of directors of a company.

#### **4 CHARITIES**

- 4.1 To be a charity an organisation must operate for a charitable purpose. There are four:

- the relief of poverty and human suffering
- the advancement of education
- the advancement of religion
- another purpose for the benefit of the community.

It must operate for the public benefit and have exclusively charitable purposes. An organisation which operates for political purposes will not qualify for charitable status.

- 4.2 To register as a charity the organisation must submit its Trust Deed (usually the Memorandum and Articles of Association of a company limited by guarantee) to the Charity Commissioners for approval. If they are satisfied that the organisation is charitable it will be registered as such.
- 4.3 Those who are responsible for the control and administration of a charity are referred to as its trustees, even where the organisation is a company limited by guarantee even though they are not strictly trustees. Trustees of a charity retain personal liability, and can only delegate if the trust deed authorises them so to do.

#### **4.4 Trustees' Duties**

- (1) Trustees must take care to act in accordance with the Trust Deed and to protect the charity's assets. They are also responsible for compliance with the Charities Acts.
- (2) Trustees must not make a private profit from their position. They must also perform their duty with the standard of care which an ordinary, prudent business person would show. Higher standards are required of professionals, and in relation to investment matters.
- (3) Charitable trustees must ensure that the information relating to the trust and trustees is registered with the Charity Commissioners and that annual accounts and returns are completed and sent.
- (4) If charitable income exceeds £5000, the letters, adverts, cheques etc must bear a statement that the organisation is a registered charity.
- (5) Trustees are under a duty to ensure compliance with all relevant legislation (eg in relation to tax matters).



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#### 4.5 Trustees' Personal Liability

- (1) If in doubt, always consult the Charity Commissioners. A trustee who does so will avoid personal liability for breach of trust if he/she acts in accordance with the advice given.
- (2) Generally though, a trustee incurs personal liability if he/she:-
  - acts outside the scope of the trust deed
  - falls below the required standard of care
  - makes a personal profit from the trust assets
- (3) In such circumstances the trustee will incur personal liability for losses incurred.
- (4) Trustees can be liable personally to third parties because unlike a company, a trust has no separate identity from the trustees. Trustees are however entitled to an indemnity from the trust assets, provided they act properly in incurring the liability. Trustees remain personally liable once they retire (eg if they have entered into a contract on behalf of the trust) and should therefore seek an indemnity from their successors. If the charity is a company however the trustees for the time being will be responsible.
- (5) Trustees may be liable to fines if they do not comply with the duty to make returns etc.

#### 4.6 Indemnities

An indemnity can be given from the trust fund provided the trustee has acted properly and within his/her powers. Trustees may take out insurance to protect themselves against personal liability but not for criminal acts, fraud etc. There will be no problem if the trustees themselves pay the premiums but if they are paid out of the charitable funds the trustees will need the consent of the Charity Commissioners unless the trust deed allows it.

### 5 COMMITTEES OF MANAGEMENT

#### 5.1 Unincorporated Associations

Groups which are not charitable trusts or limited companies are "unincorporated associations" and have no separate legal identity from their members. The rules governing the members' duties and liability will be set out in a constitution which is simply an agreement between the members as to how the organisation will operate. Usually the constitution will provide for a management committee to be responsible for the everyday running of the organisation. An unincorporated organisation may be charitable and may register as a charity.

- 5.2 Property will have to be held by individuals as the organisation has no existence of its own.

**5.3 Duties**

Broadly, Management Committee members must act within the constitution and must take reasonable care in exercising their powers.

**5.4 Liabilities**

- (1) Generally, the Management Committee members are liable for the acts of the organisation, but are entitled to an indemnity from the funds of the organisation if they have acted properly. If there are not enough funds, the Committee members are personally liable for the shortfall.
- (2) If one person is appointed by the constitution to act as the agent of the organisation for certain purposes, then that person acts as the agent of all the members, who have joint liability for the agent's actions.
- (3) Members of the Committee of Management will have personal liability if they act outside the authority given to them or if they do not comply with statute eg the payment of employees' tax etc.

**5.5 Indemnities**

Members will be entitled to an indemnity if they act in accordance with the constitution and are not at fault. It is possible to obtain insurance but if the organisation is to pay the premium it must be permitted by the constitution.

**6 OTHER CORPORATIONS**

- 6.1 There are bodies created by an Act of Parliament to carry out particular functions and whose constitution is set out in the legislation relating to that specific body.
- 6.2 The powers of the members of the body and duties and liabilities of those members individually and collectively depend upon the wording of the legislation in question. In general terms the position of a member is similar to that of a Councillor. It is prudent therefore for a member of one of these bodies to obtain information for himself/herself from the clerk or chief administrative officer of the body on the powers and duties of the body, its standing orders and other procedures which it must follow and financial or other regulations which govern conduct of its business.

**7 JOINT COMMITTEES OF LOCAL AUTHORITIES**

- 7.1 The position of a Member on a joint committee is identical to that of a Member on any Committee of the Council.

**8. CONSULTATIVE BODIES**

- 8.1 These are bodies set up by another body or the Council to advise it. These bodies do not take decisions or authorise action; however, the advice given can be persuasive and result in a particular decision being taken or action carried out by the body which the consultative body advises. Accordingly a member of one of these consultative bodies should always ensure that any advice given is soundly based on all relevant factors being taken into account, any irrelevant ones being disregarded, and is in accordance with the law and is reasonable. Advice which is tainted by malice or negligently given which results in an adverse effect on another can give rise to legal liability.
- 8.2 Members on consultative bodies are bound by the Council's Code of Conduct.