Submission

by

Business|NZ

to the

Ministry of Economic Development

on the

Review of the Financial Reporting Act 1993 Part II

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1. INTRODUCTION

1.1. Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 56-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

1.2. In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

1.3. Business New Zealand's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services).

1.4. It is widely acknowledged that consistent, sustainable economic growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term.

1.5. Business success and growth are fundamental in achieving the aims of higher economic growth for the country. A key way in which business success can be accurately measured is through the financial documents that are regularly compiled. Financial reporting provides all users of the data with key information about the past, present and future directions of a business. However, these responsibilities should never be set beyond what is reasonably required, both by internal and external users. Uniformity in the way financial data is presented has strong support in the business sector but there are concerns over the proposed filing requirements and the possibility that financial data may have to be released publicly. This is especially a concern for closely held companies.

1.6. After providing comments on part I of the Financial Reporting Act (FRA) review, Business New Zealand welcomes the opportunity to provide comment on part II of the discussion document that the Ministry of Economic Development has released (referred to as the 'Ministry'). While the discussion document regarding part II of the FRA review has asked a series of particular questions in each of the topics, Business NZ instead wishes to make more general comments.

2. Summary of Recommendations

2.1. Business New Zealand recommends that:

(a) The institutional arrangements relating to financial reporting are not reconstituted into a single independent Crown entity;

(b) Notwithstanding the fact that Business New Zealand does not support a reconstituted single independent Crown entity, if such a body is established it should not grant exemptions from financial reporting requirements;

(c) Fee level(s) as part of the cost recovery for a single independent Crown entity are open to wide public consultation in terms of the level(s) set;

(d) A standards setting function in New Zealand remain;

(e) A continued standards setting function in New Zealand does not include non-financial measures;

(f) The Ministry continues to investigate the option of a specialist tribunal in relation to enforcement issues for financial reporting requirements;

(g) Charitable entities should not be assessed on the same financial reporting requirements as other entities;

(h) Income from public sources as a measure for threshold size regarding the financial reporting responsibilities by charitable entities is clearly defined for charitable entities;

(i) The threshold values for the tiered approach to financial reporting is reviewed regularly;

(j) The ability of the Charities Commission or the general public to initiate the requirements for a charitable entity to require additional financial reporting measures be based on a strict and strongly justified criteria;

(k) The preferred approach regarding the requirement to produce and file audited financial reports for non-issuer companies as outlined by the Ministry is not introduced;

(l) The alternative approach regarding the requirement to produce and file audited financial reports be accepted whereby all firms no matter what their size are to meet all filing standards, but can choose to derogate from these duties on the agreement of the shareholders;

(m) Opting out of compiling financial reports be set at 25% opt in against 75% opt out;

(n) Assets should not be a criterion for evaluating whether a company is deemed to be large;

(o) Operating revenue of $20 million and the full-time equivalent employees number of 50 in regards to the thresholds for differentiating large companies from small companies be accepted;

(p) The amount of time reporting entities have to prepare financial reports stays within five months of balance date as set out in the Financial Reporting Act;

(q) Conduit issuers are not subject to the same financial reporting and information disclosure requirements as issuers;

(r) Wholly-owned subsidiaries that have public accountability obligations be subject to full reporting requirements;

(s) The Ministry revise the current requirements regarding financial reporting so that there is no differentiation on the basis of foreign ownership;

(t) Notwithstanding the fact that Business New Zealand recommends no restrictions on the resident status of any one director of a New Zealand company based offshore, any decision to impose the requirement that all such companies have at least one director who is ordinarily resident in New Zealand also includes some form of designation mechanism;

(u) Exemptions are available to provide relief from the full financial reporting requirements for overseas companies incorporated in jurisdictions where they are satisfied those adequate regulatory and enforcement mechanisms exist. Also, that the idea of local agents being accepted be dependent on widespread support from other submitters;

(v) The introduction of a deed of cross-guarantee in New Zealand continues to be investigated, provided there is strong evidence that it has brought about an overall net benefit for Australian entities;

(w) Exemptions from the Financial Reporting Act are provided for those entities deemed to be non-active;

(x) The Financial Reporting Act is modified to ensure that it is technology neutral and has sufficient scope to allow for electronic filing by methods such as XBRL. However, there should be no mandatory requirement for financial reporting through electronic means in the future;

(y) The current provisions of the Electronic Transactions Act remain in place; and

(z) Transfer of responsibility for setting auditing standards to a Crown body that is independent of the profession should not proceed.

3. Institutional Arrangements

3.1. The Ministry proposes that the institutional arrangements relating to financial reporting be formally consolidated into a single, independent Crown entity with an active role in the standards setting process, thus becoming a

reconstituted Accounting Standards Review Board (ASRB). However, Business New Zealand has doubts regarding the formation of such a body.

3.2. We do not see any major shortcomings of the current regime whereby the ASRB reviews and approves financial reporting standards, and the Financial Reporting Standards Board (FSRB), which is a board of the Institute of Chartered Accountants of New Zealand (ICANZ) is the dominant provider of technical advice to the ASRB. Although ICANZ is both a representative body and a dominant provider of standards, we do not perceive the interests of the accounting profession being unduly favoured. Previous experience has shown this system to provide standards that do not undermine the confidence of investors, nor question the objectivity of the decisions reached.

Recommendation: That the institutional arrangements relating to financial reporting are not reconstituted into a single independent Crown entity.

3.3. Notwithstanding Business New Zealand's recommendation of a status quo approach to the institutional arrangements, if there is widespread support from other submitters for the establishment of a single independent Crown entity, there are some issues we believe would need to be examined carefully if the reconstituted body was established.

3.4. Firstly, we do not agree with the proposal that the reconstituted ASRB set standards as well as grant exemptions. Although the Ministry takes the view that the function of issuing exemptions should not be over used and would only occur in genuine cases, we agree that it would leave the reconstituted body with reasonably significant powers, which would certainly be above the level that we would approve of. We believe the power to provide exemptions as well as set standards to be a strong conflict of interest. Instead we would want other entities/bodies granting exemptions, which would be based on the sector in which the exemption would arise.

Recommendation: Notwithstanding the fact that Business New Zealand does not support a reconstituted single independent Crown entity, if such a body is established it should not grant exemptions from financial reporting requirements.

3.5. Secondly, we agree that direct Crown funding would be required for a reconstituted body, much like the current set-up for the Takeovers Panel. However, regarding the ability to charge fees for services, Business New Zealand would not want the fee levels to be a primary source of cost recovery, which would undoubtedly lead to fees being set at a high level. In our view this would jeopardise the possible use of such services. We note that there is currently a review of the fees charged for clearance and authorisation applications under the Commerce Act, which under the current proposals determined by the Ministry, could increase dramatically and seriously impede future applications. Business New Zealand recommends that any fees arrangement be open to wide public consultation in terms of the level(s) set.

Recommendation: That fee level(s) as part of the cost recovery for a single independent Crown entity are open to wide public consultation in terms of the level(s) set.

4. Financial Reporting Standards

4.1. As the FRA is currently predicated on the assumption that New Zealand is a "standards setter", rather than a "standards taker", Business New Zealand accepts that some modification of the FRA is required to legislatively reflect the presumption in favour of adopting International Financial Reporting Standards (IFRS). However, we also believe that some form of "safety valve" should be seriously considered, such as the current situation in Australia that will not adopt an international standard if it is not in the "national economic interest".

4.2. Despite claims by the Ministry that the exercise of such a discretion would mean New Zealand and New Zealand entities would not be able to claim international compliance, it would only arise in certain standards, and we agree that it should only occur in genuinely appropriate circumstances.

4.3. We agree that if a general shift from standards setting to standards taking for IFRS in New Zealand is introduced, it will still be necessary to maintain a standards settings function. The setting of standards in areas without international standards is a sensible step, along with the various discretions outlined under the modification of international standards, such as additional disclosures, elimination of options (providing consultation regarding which is the preferred option for the national economic interest is undertaken), guidance notes and minor word changes.

Recommendation: That a standards setting function in New Zealand remain.

4.4. However, Business NZ strongly opposes setting standards for non-financial measures, such as triple-bottom line reporting. Although the Ministry has clearly stated that it is not proposed that non-financial reporting be made mandatory through any changes to the FRA, we take the view that any standards compiled are still one step closer down the possible path of compulsion. We believe that the composition of non-financial reporting such as triple-bottom line reporting should be solely determined by the enterprise. There is sufficient worldwide literature on such subjects for enterprises to base their report on if they wish.

Recommendation: That a continued standards setting function in New Zealand does not include non-financial measures.

5. Enforcement

5.1. The discussion document provides two further options on top of normal criminal proceedings, which the Ministry considers are not necessarily the most adequate solution in all cases.

5.2. The first option involves the administrative remedies of a specialist tribunal, that would have the power to determine disputes involving accounting issues. This would be to correct interpretation or approach, rather than impose some form of punishment for breaching a standard. The discussion document states that a similar setup exists in Australia, which has led those perceiving an adverse decision to correct their reports without the need for further court action. Willingness to accept the decisions has primarily come about due to the panel incorporating experts in the field.

5.3. The advantages of a specialist body of experts, speedy resolution of issues and more of an informal process and relaxed rules of evidence and precedent are certainly positive, while limiting binding/non-binding determinations relating to correction of reports and initial and ongoing costs to establish have been identified as the main disadvantage.

5.4. However, we would like to point out a concern regarding the process by which the persons on the tribunal would be selected. Any selections by the Governor-General on the advice of the responsible Minister should also have the backing of the larger accounting community, given the impartial attitude the tribunal would need to have. The possibility of purely politically motivated appointments would severely hamper the integrity of such a tribunal.

5.5. Business New Zealand does not have any strong views on whether persons sitting on such a tribunal should or should not be different from those on a reconstituted standards setting body (should one be established). The most obvious impediment to having a separate group of people would be a possible shortage of expertise to fill the positions. Overall, we would not see appointments on both bodies as a significant concern.

5.6. The second option outlined involves a civil penalties approach, essentially providing a middle ground between private civil action and criminal prosecution for enforcement of the law. The main difference in relation to a specialist tribunal is that aggrieved parties would apply to the court in a civil action for remedy, rather than a dedicated body. We agree that this approach does not address the issues of timeliness of process nor the detailed technical nature of financial reporting structures.

5.7. When weighing up the two options, Business New Zealand views the specialist tribunal as the more effective way forward of the two options presented. The specialist tribunal provides more advantages than the civil penalties option, and a higher degree of flexibility.

Recommendation: That the Ministry continues to investigate the option of a specialist tribunal in relation to enforcement issues for financial reporting requirements.

6. Registered Charitable Entities

6.1. Business New Zealand generally supports moves by the Ministry to introduce a tiered system in regards to the level of financial reporting for charitable entities. While such entities should be accountable and transparent in their

operations, they should certainly not be aligned with other entities that typically have a profit focus, considering more of the share of donations should go towards the intended charitable aid, rather than to over prescriptive reporting requirements.

Recommendation: That charitable entities should not be assessed on the same financial reporting requirements as other entities.

6.2. For size thresholds to determine the level of financial reporting requirements, Business New Zealand agrees with other submitters that assets, turnover and employees are not appropriate for charitable entities. The Ministry's proposal of using income from public sources (i.e. donations, income from business activities and government grants and contracts) is more appropriate, although we believe that this approach needs to be clearly outlined so that there is no confusion as to what is or is not considered income from public sources.

Recommendation: That income from public sources as a measure for threshold size regarding the financial reporting responsibilities by charitable entities is clearly defined.

6.3. Business New Zealand has no strong view on the threshold levels set for the three tiers regarding financial reporting requirements for charitable entities, as the entities themselves would obviously provide a better understanding of how realistic the threshold values are. However, we would want to see these threshold values reviewed on a regular basis, to ensure the levels set do not disadvantage those charitable entities that have a relatively low-income level but have increased reporting requirements compared to other entities.

Recommendation: That the threshold values for the tiered approach to financial reporting is reviewed regularly.

6.4. Business New Zealand also welcomes the proposal that entities would only change their reporting tier if they exceed the threshold two years in a row, given previous concerns of one-off or extraordinary donations pushing charities beyond their current threshold value. We also consider that non-public income should not be included in determining whether an entity has exceeded the relevant thresholds, as using donations are sufficient.

6.5. The remaining recommendations by the Ministry in areas such as consolidation of financial reports, auditing, filing, duplication of reporting requirements, exemptions and timing are supported by Business New Zealand. However, these issues as well as to whom charitable entities should report could be looked after by the Charities Commission, rather than some type of independent body. The same logic applies to other specific bodies that could set the reporting standards and requirements.

6.6. We would also like to point out that under the issue of stakeholder discretion and shifting tiers, Business New Zealand would be concerned if the notion of either a legitimately concerned member of the public or the Charities

Commission requiring additional financial reporting measures or a shifting up of tiers for specific charitable entities be abused in any way. We would not want to see the requirements for such moves set too low so as to lead to inappropriate use of procedures.

Recommendation: That the ability of the Charities Commission or the general public to initiate the requirements for a charitable entity to require additional financial reporting measures be based on a strict and strongly justified criteria.

7. Non-Issuer Companies

7.1. Regarding non-issuer companies, the Ministry has highlighted a preferred and alternative option. The preferred option is similar to the Australian regime where there is the requirement for large economically significant entities to produce and file audited financial reports, while small companies would be permitted to derogate from some or all of their financial reporting requirements on the basis of shareholder agreement. The alternative approach is that while all firms no matter what their size are to meet all filing standards, all (i.e. both large and small) could choose to derogate from these duties based on the agreement of the shareholders.

7.2. Business New Zealand is <u>strongly opposed</u> to the preferred approach. This approach is based on the notion that other than shareholders, there are other stakeholders who have an interest in information disclosed in financial reports. Overall, the Ministry considers there are large enough groups of stakeholders to make the mandatory filing of information sufficiently useful to outweigh the costs to commercial confidentiality and personal privacy. Business New Zealand believes this is completely inaccurate, and an extreme shift in balance away from the interests of the shareholders of non-issuer companies. Adoption of the preferred approach would take the decision to produce and file audited financial reports out of the hands of shareholders where it should fundamentally belong.

Recommendation: That the preferred approach regarding the requirement to produce and file audited financial reports for non-issuer companies as outlined by the Ministry is <u>not</u> introduced.

7.3. Apart from the shift in balance away from shareholder powers, we have two further concerns with the preferred approach. Firstly, the approach goes against the notion of what it means to be a non-issuing company, in that as a private company there is considerable importance put on the need for privacy, including the detailed financial reports of the company. From our perspective, the Ministry has not given this incursion into privacy sufficient weighting when assessing the counterbalance of the needs of stakeholder information. Secondly, we believe the Ministry has not fully considered the probable significant financial costs attached to the preferred approach for private companies, which would be large for many that find themselves meeting two or more out of the three threshold criteria outlined.

7.4. Although the Ministry has mentioned in the discussion document that a company that is deemed to be economically significant would have the ability for exemptions in "appropriate circumstances" under the preferred approach, this does not instill any reassurance that the preferred approach would create an overall net benefit given the subjective nature of what an "appropriate circumstance" might end up being.

7.5. The current position in Australia regarding the requirement to produce and file audited financial reports has been given heavy weighting in the discussion document. While the trans-Tasman perspective is important to at least consider, the fact that an Australian Parliamentary Joint Statutory Committee on Corporations and Securities issued a report that requested Australia revert back to its previous exempt propriety companies regime shows any automatic acceptance of a similar approach in New Zealand is questionable at best. In addition, when comparing New Zealand to other overseas regimes in terms of financial reporting requirements, most others have a wider range of corporate forms available to entrepreneurs. If the company form is too onerous, there are other options for them to choose from such as Limited Partnerships, Limited Liability Partnerships or Special Companies. New Zealand does not have these options.

7.6. Business New Zealand supports the alternative approach, given either approach is exactly the same for small companies, but the alternative provides greater freedom of choice for large firms in terms of the preparation, auditing and public filing of financial reports. Decisions on all three elements should rest with the shareholders, rather than an outside organisation or government department that applies an arbitrary threshold for compliance.

7.7. Business New Zealand's preferred option would be that all small companies are exempt, and large companies have the option of opting out, so that there is greater flexibility for small and large firms. However, we accept the Ministry's view that it seems practical that a company obtain shareholder agreement to satisfy lesser requirements in advance, rather than go to the expense of fulfilling some lesser requirements, only to be subsequently requested to comply with more onerous requirements by shareholders. Overall, the alternate approach provides greater empowerment to shareholders, which we fully support.

Recommendation: That the alternative approach regarding the requirement to produce and file audited financial reports be accepted whereby all firms no matter what their size are to meet all filing standards, but can choose to derogate from these duties on the agreement of the shareholders.

7.8. The Ministry's believes the requirements for opting out of compiling financial reports should be based on the decision of the shareholders, but with unanimous support. However, as other submissions have discussed, rogue shareholders may negatively influence such steps for whatever reason, thus leading to the possibility of some leeway of say a 5% opt in versus 95% opt out balance. While the Ministry has asked what would be an appropriate level of assent required to opt out of reporting requirements taking into account adequate protection for minority shareholders, we find this concern

somewhat unwarranted against the background of the traditional place majority versus minority shareholders have had in a company.

7.9. The idea of one share, one vote has meant that majority shareholders have a greater say in the running of the business by purchasing a larger share of a company in comparison with a minority shareholder. The potential downside of purchasing more shares is that majority shareholders also take a greater risk if the value of the company's shares were to fall or the company collapses. It would be reasonable to assume that a majority shareholder would have the best financial interests of the company in mind, and any decisions voted for by majority shareholders should be to the benefit of shareholder wealth. Owning shares in any company always carries an element of risk and protection of minority interests should not go as far as to impede the interests of shareholders with a much stronger ownership of the company. Therefore, we support a lower level of assent required to opt out of reporting requirements, and support reporting requirements to stand at 25% opt in versus 75% opt out – the same level as special resolutions.

Recommendation: That opting out of compiling financial reports be set at 25% opt in against 75% opt out.

7.10. Regarding the size thresholds outlined for small and large companies, the discussion document has proposed assets, turnover and the number of FTE employees. Business New Zealand's submission on part 1 of the FRA viewed turnover as a more accurate measure in terms of a threshold, because asset testing can be subject to manipulation by companies. Assets can be placed in a trust and leased back to the company, meaning a company can control asset value. However, a turnover value cannot be so easily manipulated.

Recommendation: Assets should not be a criterion for evaluating whether a company is deemed to be large.

7.11. However, we are pleased to see that the Ministry has taken up our recommendation from part 1 of the FRA review to increase the threshold for the number of full-time equivalent workers from 20 to 50, which would encompass many entities still expanding their business to the point of developing new product lines and looking at possible export opportunities. Once an entity is large enough, trained in-house workers are more likely to be employed to handle financial reporting responsibilities. Therefore, it is important that as many compliance costs and barriers are reduced as much as possible so that the transition from a small-medium size business to a large one is easily made.

7.12. Furthermore, Business New Zealand would not want to see the addition of any further criteria such as a debt figure, given the extra complications placed on business. Some leeway in terms of companies being able to exceed their threshold for a single but not consecutive years will create less volatility around reporting requirements.

Recommendation: That operating revenue of $20 million and the full-time equivalent employees number of 50 in regards to the thresholds for differentiating large companies from small companies be accepted.

7.13. Regarding considerations for both small and large companies, Business New Zealand does not have a firm stance on the amount of exact time the FRA should allow reporting entities to prepare financial reports, which is currently set at within five months of balance date. The Ministry believes this amount of time is too long and may mean data disclosed is quickly outdated, and should be brought down to four months. Companies would still be permitted to extend this time if a required number of shareholders agrees. We take the view that there is relatively little difference between the proposed four months and the current five months in terms of disclosure, which could easily be outweighed by changes to administrative systems for reporting within companies, as well as resources requesting an exemption. In light of the relative minor difference between the two time periods, we recommend that the amount of time remain at five months.

Recommendation: That the amount of time reporting entities have to prepare financial reports stays within five months of balance date as set out in the Financial Reporting Act.

8. Issuers of Securities to the Public

8.1. Issuers of securities to the public should be required to produce a set of financial reports in accordance with all applicable standards and statutory requirements. However, the discussion document outlines two further matters in relation to types of issuers.

8.2. The first matter involves “conduit issuers” – issuers that raise funds from the public but subsequently pass the funds on to a related entity for operational purposes. The Securities Commission has recommended that such issuers in particular circumstances be subject to the same financial reporting and information disclosure requirements as issuers, which the Ministry has deemed to be worth considering.

8.3. However, the discussion document also states that such a move could have significant impacts on entities entering into such arrangements for sound business reasons. Any drafting for the matter is likely to be problematic and would need to be carefully worded to avoid sound business arrangements being halted.

8.4. On the balance of the arguments for and against, Business New Zealand does not believe there is strong enough justification for conduit issuers to be subject to such reporting and disclosure requirements.

Recommendation: That conduit issuers are not subject to the same financial reporting and information disclosure requirements as issuers.

8.5. The second issue involves group financial reports for those companies that are a wholly-owned subsidiary that has public accountability obligations such as being an issuer of securities. However, unlike other types of wholly-

owned subsidiaries that are exempt from the full obligations of preparing group financial reports, the Ministry believes that wholly-owned subsidiaries with public accountability obligations should be subject to the full reporting requirements.

8.6. Business New Zealand agrees that there does appear to be an imbalance of information for investors of the wholly-owned subsidiary that are issuing securities, and supports moves that such companies should be required to complying with full reporting requirements.

Recommendation: That wholly-owned subsidiaries that have public accountability obligations be subject to full reporting requirements.

9. Overseas Companies

9.1. The discussion document has highlighted two issues in relation to overseas companies and the FRA, the first being overseas-owned companies and the second being overseas-incorporated companies. The former is deemed to fall into this category if 25% or more of its shareholdings are overseas. Such companies do not enjoy any relief from preparing full financial reports, and in fact have to provide additional reporting requirements. The latter are obligated to produce reports for the company as a whole, but must also produce reports for their New Zealand branch operations.

9.2. We agree that the general regimes of the Securities Act and the Companies Act are sufficient for all locally incorporated companies, and therefore no differentiation should be based on the notion of foreign ownership.

Recommendation: That the Ministry revise the current requirements regarding financial reporting so that there is no differentiation on the basis of foreign ownership.

9.3. However, Business New Zealand is opposed to the idea of a requirement for companies to have at least one director who is ordinarily resident in New Zealand. While enforcement actions may be difficult if some directors are beyond the reach of New Zealand law, on balance the limitations placed on one of the directors for all overseas companies would probably outweigh the relatively minor number of enforcement actions that would take place. Such a requirement on one of the company's directors could prevent the best applicant obtaining the position.

9.4. The Ministry is also considering some form of designation mechanism, as an alternative to the situation described in 9.3, whereby a New Zealand resident director would not be required, but instead one or more of the directors could be based in particular designated jurisdictions where suitable arrangements for cross-border enforcement exist. Although Business New Zealand disagrees with the Ministry that such restrictions are required, we would favour the inclusion of a designation mechanism over one director required to be ordinarily resident in New Zealand if one of the two options was to be implemented.

Recommendation: Notwithstanding the fact that Business New Zealand recommends no restrictions on the resident status of any one director of a New Zealand company based offshore, that any decision to impose the requirement that all such companies have at least one director who is ordinarily resident in New Zealand also includes some form of designation mechanism.

9.5. Business New Zealand is pleased to see that the Ministry is reviewing the policy of overseas-incorporated companies having to produce reports for both the company as a whole and for their New Zealand branch operations, given the substantial compliance costs that can arise from such requirements.

9.6. Business New Zealand is concerned that the Ministry has received anecdotal evidence that the cost of preparing additional financial reports to meet the existing New Zealand FRA requirements may exceed any profits that are expected to be earned from New Zealand operations. As the Ministry rightly points out, such circumstances could easily jeopardise existing operations and deter the establishment of new ones.

9.7. We agree that it would not be appropriate to impose such blanket reporting requirements on all overseas-incorporated companies, especially given the main concern was potential inadequacies of foreign jurisdiction companies' regulatory regimes, although many countries currently have sound corporate regulatory regimes in place. Business New Zealand agrees that there should be permission for institutional bodies to grant exemptions to provide relief from the full requirements of financial reporting for overseas companies incorporated in jurisdictions where they are satisfied that adequate regulatory and enforcement mechanisms exist.

9.8. The possibility of having a "local agent" would be less restrictive on a company than the requirements placed on one director as discussed in 9.3. As Business New Zealand has no firm view whether having a local agent would be beneficial, we would only want to see the idea continued to be investigated if there was strong wide-spread support from other submitters.

Recommendation: That exemptions be available to provide relief from the full financial reporting requirements for overseas companies incorporated in jurisdictions where they are satisfied that adequate regulatory and enforcement mechanisms exist. Also, that the idea of local agents going forward be dependent on widespread support from other submitters.

10. Consolidation of Financial Reports

10.1. Whether it is appropriate to adopt the requirement of a deed of a cross-guarantee as is currently the case in Australia before providing relief to the wholly owned subsidiaries of reporting entities would largely come down to whether a net benefit is provided for the company in terms of compliance costs.

10.2. Although Business New Zealand does not oppose the idea of a cross-guarantee being at least further considered, any decision to implement a

deed of cross-guarantee should largely depend on how measured its success or otherwise has been in Australia since its inception.

10.3. Regarding parent financial reports, Business New Zealand agrees that legislation should not attempt to provide general relief for parent financial reporting obligations, given the information would be helpful to particular groups in relation to certain entities.

Recommendation: That the introduction of a deed of cross-guarantee in New Zealand continues to be investigated provided there is strong evidence that it has brought about an overall net benefit for Australian entities.

11. Non-Active Entities

11.1. Business New Zealand agrees that the requirement under the FRA for some entities to produce financial reports even though there has been no trading activity is not ideal, nor justified. While we are not in a position to ascertain whether this is an issue of wider scope than just companies, we see a change in requirements as a positive step.

11.2. Our preferred choice of the two options highlighted in the discussion document (namely a “names register” or exemptions from the FRA) is the same as the Ministry’s. The preferred choice of exemptions from the FRA are based on the grounds of ease of application in comparison with the more rigorous examination of companies beforehand and the flow-on effects regarding the Companies Act of taking the “names register” approach.

Recommendation: That exemptions from the Financial Reporting Act are provided for those entities deemed to be non-active.

12. Technical Neutrality

12.1. Business New Zealand agrees that technological advances over recent decades have meant electronic documentation and record keeping has become more prevalent among enterprises. Given its increased use, Business New Zealand supports moves that the FRA be made technology neutral and has sufficient scope to allow electronic filing.

12.2. We do note however that in regards to the electronic format for simplifying the flow of financial reports, records and information, called eXtensive Business Reporting Language (XBRL), there may be mandatory use of the format in the future. Although the discussion document only touched upon the possibility and did not provide any further context, Business New Zealand would not support any mandatory requirement of financial reporting through electronic means, regardless of the type of entity.

Recommendation: That the Financial Reporting Act be modified to ensure that it is technology neutral and has sufficient scope to allow for electronic filing by methods such as XBRL. However, there should be no mandatory requirement for financial reporting through electronic means in the future.

12.3. Regarding the electronic publication of financial reports, Business New Zealand understands that there may be some difficulty in companies implementing the requirement to obtain consent in advance so that shareholders can receive an electronic copy of the financial reports, rather than a paper copy. However, Business New Zealand does not see any viable solution, as a change to only an electronic format going out to shareholders would disadvantage those without access to a computer, meaning the company has not fulfilled the requirement as set out in the Companies Act.

Recommendation: That the current provisions of the Electronic Transactions Act remain in place.

13. Auditors and Auditing Standards

13.1. Business New Zealand agrees with the Ministry that auditing standards have received increased international attention given the collapse of certain high profile companies. However, any changes regarding New Zealand's auditing operations should always be balanced against the perceived scale of potential problems that might arise in this country.

13.2. The discussion document points out that ICANZ sets audit standards in New Zealand for companies and issuers, while the Auditor General is responsible for auditing standards of all public entities. This may cause some shortcomings given the processes may be seen as insular and protectionist, while the penalty for breaches of the internally devised standards cannot result in sanctions such as criminal proceedings.

13.3. To alleviate these shortcomings, the Ministry has proposed the transfer for setting auditing standards to a Crown body that is independent of the profession. Business New Zealand would be opposed to this idea, based on the fact that such a solution is far beyond the scale of any perceived problem that may exist in regards to obtaining a more transparent and independent arrangement.

Recommendation: That transfer of responsibility for setting auditing standards to a Crown body that is independent of the profession should not proceed.