

# Accounting Alert

## Staying on top of developments



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The Financial Reporting Bill has been introduced to Parliament, proposing significant changes to New Zealand’s financial reporting framework. The proposals are largely consistent with the Government’s previous announcements, such as the removal of financial statement preparation requirements for most small and medium companies, and the clarification of reporting requirements for registered charities. However there are a number of other changes which will affect a wide range of entities such as the removal of the requirement to prepare parent financial statements when group financial statements are already provided, and alignment of the penalties regime.

This accounting alert summarises these proposed financial reporting requirements by entity type, bringing together the proposals included in the Bill (who has to report, whether an audit is required, filing requirements, and penalties for non-compliance) with the proposals of the External Reporting Board (XRB) on which financial reporting standards would apply.

This alert also provides an update on the Financial Market Authority’s (FMA’s) final guidance note on *Disclosing non-GAAP financial information*, issued on 1 September 2012. The guidance note is largely consistent with the previous consultation draft, but now includes an illustrative profit announcement including the non-GAAP measure “underlying profit” as an aid for issuers.

## Financial Reporting Bill proposes changes to financial reporting requirements

Last month the Minister of Commerce introduced the Financial Reporting Bill (the Bill), which proposes significant changes to New Zealand’s financial reporting framework. The Bill aims to:

- reduce compliance costs, with the main change to remove a requirement for small and medium companies (that are not issuers) to prepare financial statements,
- strengthen the law where current reporting requirements do not adequately meet user needs, such as through the introduction of financial reporting requirements for registered charities, and

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- reduce inconsistencies in current reporting requirements and make the legislation more user friendly by locating only core financial reporting principles in the Bill with all other requirements in the sector, industry and entity-specific Acts.

**What’s changed?**

The changes proposed are largely consistent with the Government’s announcement in September 2011, although there is a new proposal to allow large New Zealand privately owned companies to opt out of appointing an auditor. In summary, the Bill proposes to:

- remove financial reporting requirements for most small and medium sized companies,
- introduce financial reporting requirements for registered charities and large partnerships,
- remove the obligation to prepare parent financial statements where group financial statements are prepared,
- reduce the preparation time for financial statements from five months to three months. An additional 20 working days for filing has been retained where applicable, and
- the penalties regime has been aligned for offences relating to financial reporting obligations such as failing to prepare, register, or distribute financial statements or have them audited. Where directors or officers may be liable in addition to the entity, a due diligence defence is generally provided.

The following tables outline the proposed financial reporting requirements by entity type, bringing together the proposals included in the Bill (who has to report, whether an audit is required, filing requirements, and penalties for non-compliance) with the proposals of the External Reporting Board (XRB) on which financial reporting standards would apply.

**Issuers and other market participants**

Entity type	Preparation	GAAP if a for-profit entity	GAAP if a PBE	Audit	Filing	Penalties for non-compliance with financial reporting obligations
Entity captured by the Financial Markets Conduct Bill (FMC reporting entity) Includes: • Listed issuers • Issuers of a regulated product • Licensed supervisors • Operators of a licenced market • Recipients of money from a conduit issuer • Registered banks • Licensed insurers • Credit unions • Building societies among others...	✓ If an overseas company must include financial statements for the NZ business	NZ IFRS	PBE Accounting Standards	✓	✓	If fail to lodge accounts - \$50,000 for the entity  If fail to comply with GAAP (knowingly) the entity and every Director can be fined: \$500,000 for an individual and /or up to 5 year prison term, or \$2.5m for non-individuals  Civil remedies also available with pecuniary penalties not exceeding the greatest of the consideration for the relevant transaction, three times the amount of the gain made or the loss avoided, and \$1m in the case of an individual, or \$5m in any other case



The proposals for issuers and other market participants are included in a supplementary order paper to the Bill, as these are proposed changes to another Bill (the Financial Markets Conduct Bill) instead of established legislation.

There are some changes proposed to the nature of entities captured by this proposed legislation. For example, all building societies and credit unions will be captured by the Financial Markets Conduct Bill once it is passed into law. Alternatively, some operators of retirement villages will not be issuers – particularly if they only issue licences.

### Public benefit entities (PBEs)

If an issuer or other market participant is a PBE it will have to comply with PBE Accounting Standards. There will not be any disclosure exemptions. A PBE is defined as “A reporting entity whose primary objective is to provide goods or services for community or social benefit and where any equity has been provided with a view to supporting that primary objective rather than for a financial return to shareholders”.

### Companies and partnerships

(that are not an issuer or other market participant)

Entity type	Preparation	GAAP if a for-profit entity	GAAP if a PBE	Audit	Filing	Penalties for non-compliance with financial reporting obligations
Large <sup>1</sup> company (less than 25% overseas ownership)	✓	NZ IFRS RDR [or NZ IFRS if entity is a large <sup>2</sup> public sector company)	Standards to apply depend on the level of operating expenditure	✓ (can opt out)	×	Maximum penalty of \$50,000 for the company and every director.
Large <sup>1</sup> company (subsidiary of foreign company or 25% or more overseas ownership)	✓	NZ IFRS RDR [or NZ IFRS if entity is a large <sup>2</sup> public sector company)	Standards to apply depend on the level of operating expenditure	✓	✓	Maximum penalty of \$50,000 for both the company and every director. The infringement offence system for failing to register financial statements (where required) has been carried forward (\$7,000)
Large <sup>1</sup> overseas companies that carry on business in NZ	✓ (Including financial statements for the NZ branch/ group business as well as overseas company/ group)	NZ IFRS RDR (Registrar may allow other country GAAP for overseas company)	Standards to apply depend on the level of operating expenditure	✓	✓	Maximum penalty of \$50,000 for both the company and every director. The infringement offence system for failing to register financial statements (where required) has been carried forward (\$7,000)
Every other company with 10 or more shareholders	✓ (can opt out)	NZ IFRS RDR unless opt out	Standards to apply depend on the level of operating expenditure	✓ (can opt out)	×	Maximum penalty of \$50,000 for the company and every director
Every other company with fewer than 10 shareholders	×	If opt in - NZ IFRS RDR	If opt in - standards to apply depend on the level of operating expenditure	×	×	Maximum penalty of \$50,000 for the company and every director
Large <sup>1</sup> Limited Partnerships	✓	NZ IFRS RDR	Not expected to be applicable	✓ (can opt out)	×	Maximum penalty of \$50,000 for every general partner
Large <sup>1</sup> Partnerships under the Partnership Act 1908	✓	NZ IFRS RDR	Not expected to be applicable	✓ (can opt out)	×	Maximum penalty of \$50,000 for every partner

1 For an entity and its subsidiaries (if any), large is at least one of assets greater than \$60m, or revenue greater than \$30m, both in respect of the two preceding accounting periods

2 Large in this respect is operating expenditure of greater than \$30m.

**What is large?**

The size criteria have increased to more than \$30 million revenue or \$60 million assets for an entity and its subsidiaries (if any), determined over the two preceding periods.

**For profit companies in the public sector**

As these entities are publicly accountable, other legislation will limit the ability to opt out of the preparation and audit requirements. We note that for-profit companies in the public sector will be required to prepare financial statements in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) if operating expenditure is greater than \$30 million, otherwise NZ IFRS Reduced Disclosure Regime (NZ IFRS RDR) would apply.

**GAAP for PBEs**

The financial reporting standards that would apply are currently the subject of exposure drafts of the XRB so could be subject to change. In summary:

Tier	Who captured	Applicable Accounting Standards
Tier 1	Publicly accountable entities (refer issuers and other market participants above) Large (expenses > \$30 million)	PBE Accounting Standards (PAS)
Tier 2	Non publicly accountable and non-large Elects to be in tier 2	PBE Accounting Standards Reduced Disclosure Regime (PAS RDR)
Tier 3	Non-publicly accountable with expenses ≤ \$2 million Elects to be in tier 3	PBE Simple Format Reporting Standard – Accrual (PSFR-A)
Tier 4	Entities allowed by law to use cash accounting – operating payments less than \$40,000 Elects to be in tier 4	PBE Simple Format Reporting Standard – Cash (PSFR-C)

For more information on the XRB's tiers for financial reporting by for-profit entities and public benefit entities (PBEs) refer to our [May](#) and [July](#) Accounting Alerts.

**Opt out requirements**

Non-large companies with ten or more shareholders are required to prepare financial statements and have them audited, unless they opt out. In addition, large New Zealand privately owned companies may opt out from appointing an auditor (although must prepare financial statements). In order to opt out, a meeting of shareholders held within the opting period (as defined below) can opt out of compliance by way of a resolution approved by a majority of 95% of the votes of those shareholders entitled to vote and voting on the matter.

The opting period for a company is defined as the period from the start of the accounting period to the earlier of:

- the date that is 6 months after the start of the accounting period,
- the date of the annual meeting to be held in the accounting period, or
- in the case of an accounting period that is shorter than 6 months (as a result of the date of the registration of the company or a change of the balance date of the company), the balance date of the period.

Companies cannot opt out if the constitution expressly provides that this section of the Bill (allowing opt-out) does not apply.

Large partnerships and limited partnerships can also annually opt out of appointing an auditor if within 6 months from the start of an accounting period a resolution is passed or signed by partners who together have contributed at least 95% of the capital contributions of all partners. They cannot opt out if the partnership agreement expressly provides that this section of the Bill (allowing opt-out) does not apply.

Entities will need to implement procedures to ensure the relevant opt-out requirements are met within the timeframes specified if they intend to invoke them.

### Opt in requirements

Non-large companies that have fewer than 10 shareholders have no financial reporting obligation unless shareholders with at least 5% of the voting shares require the company to prepare financial statements (and may also require audit).

### Other entity types

(that are not an issuer or other market participant)

Entity type	Preparation	GAAP if a for-profit entity	GAAP if a PBE	Audit	Filing	Penalties for non-compliance with financial reporting obligations
Registered charity (Charities Act 2005)	✓	Not expected to be applicable	Standards to apply depend on the level of operating expenditure	✓ (if operating expenses are above \$200,000) <sup>3</sup>	✓	Maximum penalty of \$50,000 for the charitable entity and every officer of the entity for non compliance with GAAP or a non GAAP standard (knowingly)
Friendly Societies (registered society or branch) (expenditure >\$30m)	✓	Not expected to be applicable	PBE Accounting Standards	✓	✓	Maximum penalty of \$50,000 for the society or branch
Friendly Societies (registered society or branch) (expenditure <\$30m in each of the two preceding years)	✓ (can opt out)	Not expected to be applicable	Standards to apply depend on the level of operating expenditure	✓ (unless opt out or operating payments are less than \$40,000)	✓	Maximum penalty of \$50,000 for the society or branch
Industrial and Provident Societies Note – Societies that are issuers should apply the requirements of an FMC entity as above	✓ (some societies can opt out)	NZ IFRS RDR	Standards to apply depend on the level of operating expenditure	✓ (some societies can opt out)	✓ if large <sup>4</sup>	Maximum penalty of \$50,000 for the society and every member of its committee
An operator of a retirement village	✓ For the operator and each village (refer below)	NZ IFRS RDR	Standards to apply depend on the level of operating expenditure	✓	✓	Maximum penalty of \$50,000 for an operator
Maori Incorporations under the Te Ture Whenua Maori Act 1993	✓	NZ IFRS RDR	Standards to apply depend on the level of operating expenditure	✓ (unless operating payments are less than \$40,000)	✓	The Court has the power to require officers to attend to explain non-compliance with statutory requirements
Community Trusts	✓	NZ IFRS RDR	Standards to apply depend on the level of operating expenditure	✓	✓	Maximum penalty of \$50,000 for every trustee
Corporate Society under Gambling Act 2003	✓	NZ IFRS RDR	Standards to apply depend on the level of operating expenditure	✓	✓ (if operate gambling equipment at a non-commercial class 4 venue)	Maximum penalty of \$10,000 for the corporate society

<sup>3</sup> There is a current proposal by the Ministry of Economic Development to require charities with operating expenditure above \$300,000 to have an audit, and charities with expenditure between \$200,000 and \$300,000 to have either an audit or review.

<sup>4</sup> For an entity and its subsidiaries (if any), large is at least one of assets greater than \$60m, or revenue greater than \$30m, both in respect of the two preceding accounting periods

### **Retirement villages**

As noted above, some operators of retirement villages will not be an issuer – particularly if they only issue licences to occupy and no other debt or equity instruments. We also note that the Retirement Villages Act will require operators to prepare financial statements of both the operator and its retirement villages where the operator's financial statements include:

- more than one retirement village, or
- another trading activity that operates independently of the retirement village,

and the statutory supervisor or Registrar requires it.

### **GAAP for PBEs**

Refer above for discussion.

### **Opt out provisions**

These differ depending on the entity type. We note that the requirements have strict timeframes so entities will need to implement procedures to ensure the relevant opt-out requirements are met on an annual basis.

### **Read the Bill**

The Financial Reporting Bill and Supplementary Order Paper are available at:

<http://www.legislation.govt.nz/bill/government/2012/0042/latest/versions.aspx>

The Bill currently proposes commencement by **1 April 2015**. The comment period is yet to be announced.



## Final guidance note issued by the FMA on non-GAAP financial information

On 1 September 2012, the Financial Markets Authority (FMA) issued its final guidance note on *Disclosing non-GAAP financial information*. The guidance note is largely consistent with the previous consultation draft, but now includes an illustrative profit announcement including the non-GAAP measure “underlying profit” as an aid for issuers.

In particular, we note that the principles for presenting non-GAAP financial information in investor communications (other than in financial statements and transaction documents) remain unchanged:

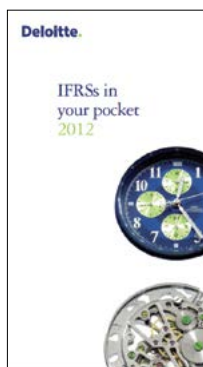
- outline why the information is useful,
- consider prominence,
- ensure an appropriate label is used,
- explain the calculation,
- provide a reconciliation,
- apply a consistent approach period to period,
- ensure adjustments are consistent with comparatives,
- ensure the measure is unbiased,
- take care referring to one-off items, and
- explain if audited or reviewed.

The principles for presenting non-GAAP financial information in transaction documents also remain unchanged except that the principle to explain if audited or reviewed is now included for consistency.

The FMA will assess non-GAAP financial information disclosures against the guidance note from 1 January 2013 onwards.

The **guidance note** is available on the FMA’s website: [www.fma.govt.nz](http://www.fma.govt.nz)

As a further aid for issuers, the Deloitte publication *Understanding Performance: Underlying Profit* surveys current practice in annual reports against the FMA’s principles for presenting non-GAAP financial information in investor communications. The survey notes that the disclosure of alternative profit measures in annual reports may need some revision to align with the FMA’s guidance as issued. The publication is available at [www.deloitte.com/nz/financialreportingsurvey](http://www.deloitte.com/nz/financialreportingsurvey)



## New publications

### IFRSs In Your Pocket 2012

The Deloitte Global Office has published the 2012 update to our IFRSs In Your Pocket publication which summarises current standards and interpretations and provides an update on the status of active projects. It is available at: <http://www.iasplus.com/en/news/2012/august/ifrss-in-your-pocket-2012>

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