



New Zealand Chambers of Commerce (Inc)

Submission to the Ministry of Economic Development

The Statutory Framework for Financial Reporting

January 2010

Introduction

The New Zealand Chambers of Commerce (Inc), 'NZCCI', is an umbrella organisation serving the interests of 29 Chambers of Commerce nationwide. These, in turn, represent over 24,000 businesses around the country. While many of our members are in the SME category our membership includes most of the largest corporations in New Zealand.

NZCCI welcome this opportunity to comment on the Discussion Document: The Statutory Framework for Financial Reporting, issued by the Ministry of Economic Development. We support the government's intention of reviewing and tidying up the ad-hoc nature of New Zealand's financial reporting framework.

Submission

NZCCI is opposed to the proposal to require all "economically significant" non-issuer commercial entities to annually publish and file general purpose financial reports. Our submission focuses on this proposal and the related issues.

A similar proposal (applying to companies only) was presented by MED in 2004 but the previous government rejected it after significant opposition from NZCCI and the business community generally. We are surprised to see that it has been revived.

It may be that the proposal has been revived in light of the company failures on the back of the recent economic downturn. Most of these failures were in the finance company sector and many of those provided audited accounts to lenders. We see the proposed legislation for as an over the top response to that situation.

In our view the public benefits claimed in the document for the filing of financial reports by non-issuer companies and partnerships (and other

entities) would not outweigh the costs associated with the preparation of these statements.

The discussion document focuses on the benefits of the proposal without mentioning the costs.

These costs are significant. Requiring private companies to file financial reports would represent an unwarranted intrusion of privacy.

It would disadvantage the businesses concerned by providing competing (publicly owned) businesses with access to financial information such as business operations, pricing capacity, and borrowing ability which could be used to gain a competitive advantage. Shareholders funds, debt and profit information is among the most sensitive information for private companies. The information disclosure could conceivably result in a large number of company closures as competitors use the information to put private operators out of business.

The requirement would also impose significant compliance costs on businesses – particularly those at the smaller end of the scale which are less able to afford the necessary resources to file such reports. Additional audit costs may also be required.

All in all, the proposals would provide a disincentive for businesses to invest in New Zealand and have a negative impact on the economy overall.

At the same time, we consider that the declared benefits of the proposal, which revolve around the protections to stakeholders arising from increased transparency and improved financial discipline, are overstated in the discussion document.

Many of these protections are already available through common law and statute. For example, stakeholders such as suppliers, banks and other creditors have alternative means available to them to assess the risk of credit and the annual publication of financial reports would not add anything. Shareholders already have access to company records. Employees are already protected by current employment law.

With regard to the financial disciplines argument, the current requirement for businesses to prepare and audit financial reports may improve disciplines but a new requirement to publish these would not add anything nor would it reduce the prospect of financial failure.

Some businesses may find legitimate ways to avoid disclosure through multi company structures, trusts and other entities.

The full costs and benefits of this proposal need to be quantified before they are presented to the public and government decision makers. We understand that a report in 2005 showed a significant net cost to the economy.

We do not think overseas incorporated companies operating in New Zealand should be treated differently from their New Zealand counterparts in terms of filing requirements.

The desire to progress Single Economic Market status with Australia seems to be a significant rationale for the proposal. We fully support harmonisation with Australia and while we agree better alignment with Australia's financial reporting rules would be a good thing, moves in this direction should be based on best practice and sound policy rather than automatically adopting the Australian approach.

Applying the proposal to new businesses only (i.e. grandfathering), is not a good compromise because apart from the fact that an inferior policy would gradually be introduced, the operation of two sets of rules - based on when entities came into being - would be confusing and arbitrary.

We do not support the idea of introducing a threshold and applying the requirement to large companies only. Our preference is for changes not to be introduced and large and small businesses being treated the same in this regard. However, if there is to be a change, the proposed thresholds (consolidated assets in excess of \$10 million; consolidated operating revenue in excess of \$20 million; and 50 full time equivalent employees) are too low.

The Wellington Regional Chamber of Commerce surveyed businesses on their reaction to this issue and found that 65% of respondents opposed any changes which would require greater public disclosure of private company accounts than is required at present. It is likely that these views are reflected by businesses nationwide.

Finally, we are disappointed that there has not been better communication with the business community on this proposal. We note that the government has endeavored to reach out to not-for-profit organisations but it would seem that the same effort has not been applied to business.

Other Issues

We support the proposal to remove the automatic requirement for small and medium businesses to prepare general purpose financial reports although we suspect that most would still prepare special purpose statements as it would be in their best interests to do so (eg for taxation purposes). The removal of the general purpose report requirement will substantially reduce compliance costs for small and medium businesses.

We support the proposal to consolidate financial reporting and assurance standards responsibilities and to create the External Reporting Board. However, the Board must have appropriate constraints on fees to avoid excessive cost recovery from business. In this regard it must also be given adequate funding.