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Dear Tony

The proposed accounting standards framework

Thank you for the opportunity to provide comments on the External Reporting Board (XRB) consultation papers on the accounting standards framework for general purpose financial reporting by for-profit entities and by public benefit entities (PBEs).

As members of the XRB will be aware, Grant Thornton New Zealand has extensive involvement with privately held businesses (often classified as small and medium sized enterprises or SMEs) and also with the not-for-profit (NFP) entities in New Zealand. We therefore consider ourselves well placed to assess the impact of the proposed changes on these sectors.

Both sectors are facing considerable challenges given today's tight financial conditions, so any financial reporting changes approved by the XRB must generate positive benefits for them. A critical success factor for the XRB has to be removing unnecessary complexity from today's financial reporting requirements. It is clearly apparent that the XRB has given considerable thought to these proposals and we are delighted to see appropriately scaling in the legislative requirements for external reporting by entities in both the for-profit and PBE sectors.

Opening remarks

Our responses to the XRB questions raised in the consultation documents are attached in Appendix 1 and Appendix 2.

Overall we are happy with the shape of the legislation that the XRB will have to operate under. We believe the changes that have been made respond well to the needs of users of general purpose financial reporting because they have scaled the level of obligations to the relative costs and benefits of reporting by entities in each of the various tiers.

Noteworthy are the proposals that provide for the first time a framework for financial reporting requirements for the NFP sector. It is admirable that the XRB is seeking to take such a comprehensive approach to tailoring requirements to user needs in this sector. We hope that this decision will not overwhelm or bias future XRB agendas given the XRB's limited resources.

Given the significance of the changes that are shortly to take place we think it is essential that the XRB make arrangements in early 2012 for an independent post-implementation review to take place in, say, three years time (ie 2015). We believe this is important because during this period a significant number of new standards (we anticipate well over 60) will have been issued by the XRB for both for-profit entities and PBEs. Knowing ahead of time that there will be a detailed review of all its standard setting activity should provide useful insight and consistent monitoring of what has worked really well for New Zealand and what could be improved. For example – did the new consultation forums and roundtables that have been mooted provide the insight and mandate for change that the XRB expected? If so, can these initiatives be further improved and shared with other countries around the world?

Transition to the new frameworks

One of the biggest risks we see for the XRB is making sure there is a smooth transition from the current financial reporting arrangements to the proposed ones.

At a principle level our view is that the XRB must also use all its influence to reduce the difficulties of entities transitioning from one tier to another.

As noted in the consultation papers, having consistent recognition and measurement requirements across the tiers will assist greatly. But this alone, in our view, is not sufficient. We would like to see the XRB providing readily available guidance (via its website) to assist entities making a transition from one tier to another. As new standards are released, consequential amendments to this guidance should be made available at the same time, given New Zealand does not have a "standard" balance date for reporting.

While it is important to have smooth transition, the XRB must be prudent and very mindful that many Tier 2 entities will never transition to Tier 1, either because of their ownership structure or the nature of their operations. Given that many entities will end up being "locked in" to the Tier 2 reporting regime, we cannot see why another framework option for there for-profit oriented entities should not be made available to the preparers of financial statements.

IFRS for SMEs

One of the questions the XRB raised in its consultation paper was whether or not Tier 2 for-profit reporting entities should be given the opportunity to adopt IFRS for SMEs. We believe they should, because IFRS for SMEs contains some very useful recognition and measurement concessions.

Given that Tier 2 was put in place on a policy platform of reducing compliance costs, we think IFRS for SMEs should be permitted, because compliance cost saving was a fundamental design principle that the International Accounting Standards Board took into consideration when it developed IFRS for SMEs.

Our view is that when it comes to Tier 2 reporting it is not a case of all or nothing – we think both regimes (ie the Reduced Disclosure Reporting (RDR) regime and IFRS for SMEs) can happily co-exist.

We note the XRB has already signalled to the preparers of financial statements and the auditing profession in New Zealand that it will have to grapple with 6 different accounting regimes. Our view is the providing a further option will not, in our opinion, create a lot of extra work or confusion in the market place.

While we readily accept there are some good arguments to support the adoption of RDR, particularly for reporting entities that have to report to Australia of those that have ambitions to eventually become an issuer, they are less compelling for:

- reporting entities in New Zealand that have to report to a Head Office or a parent company in an overseas jurisdiction that permits IFRS for SMEs,,or
- entities that will in fact never have to report overseas.

Our current understanding is that Australia is the only country in the world to have an RDR regime, whereas IFRS for SMEs is permitted, and is being used in over 100 countries.

For example, if there is a large New Zealand subsidiary of a South African incorporated entity that is not publicly accountable, it surely makes sense (in a compliance cost saving sense) to allow the NZ subsidiary to have exactly the same recognition and measurement requirements as the parent (ie IFRS for SMEs).

We believe Tier 2 reporting entities should be allowed to have the option to select either basis of accounting. Currently there are six different bases of accounting, depending on the sector that the reporting entity is operating in – to have one more, in our opinion, would not be adding an unnecessary extra burden on the preparers of financial statements given that IFRS for SMEs is self contained in approximately 250 pages of guidance, is to be updated only once every three years, and was authorised and issued by the same body that issued, namely the International Accounting Standards Board.

Harmonisation with Australia

We support the objective of harmonising our financial reporting requirements for Tier 1 entities to greatest extent possible with those used in Australia.

We unreservedly support the XRB's bold decision not to follow Australia's lead in public sector reporting. With interest we noted in the consultation paper that the Financial Reporting Council (FRC) and the Australia Accounting Standards Board (AASB) have both indicated a medium-term aspiration to adopt International Public Sector Accounting Standards (IPSAS). We certainly hope that Australia at some stage does follow the IPSAS approach that New Zealand will be pursuing because we believe it is the right one.

NFP Thresholds

With the thresholds that have been established for NFPs, we note that less than 4% of all the entities in that sector (approx 800 entities) will fall within Tier 1. We have a concern the XRB might channel a disproportionate level resources into this small and focused area thereby taking XRB resources away from other essential standard setting work.

We note that paragraph 25 of the PBE Consultation Paper states that:

> The need for a Tier 1 for NFP entities will therefore be considered further as the PBE accounting standards framework develops.

We would definitely support careful consideration to whether the XRB does neet develop a Tier 1 for NFPs with its own set of reporting requirements.

PBE issuers

We are of the general view that all issuers, whether for-profit, public sector or NFP should have to follow a similar level of accountability, albeit with the necessary sector variations (ie, full IFRS, IPSAS or IPSAS adapted for NFPs). The sector variations recognising that as printed "pure" IFRS without any adaption simply will not work for PBEs.

However, while we agree with the XRB that "the coherence and consistency of the overall framework would be enhanced by applying a similar approach [to that used for for-profit entities] in the PBE sector" we do think that further consideration should be given to whether there should be an exception to the general rule. This is, whether NFP issuers of a certain type (and still to be defined) should face less onerous reporting obligations than their for-profit counterparts. We are less convinced that some public sector PBE issuers should be excluded from the Tier 1 reporting requirements.

We would encourage the XRB to discuss the idea of some reporting exemptions for NFP issuers further with the Financial Markets Authority because the NFP sector has a vastly different set of drivers to the for-profit sector, even when they are issuers, and even when compared to most public sector issuers.

The difficulty of course then becomes identifying some factors that could legitimately differentiate issuer entities. Some factors that may be relevant include:

- Are the securities being offered to the public in substance an "investment" or are they in substance a "donation"? It may be that the XRB working alongside the FMA might be able to develop some criteria to help differentiate issuers operating in the NFP sector, and possibly the public sector as well. For example, some "investors" may direct that any interest they earn on their investment should be immediately treated as a donation (eg philanthropic bonds). However, for the same type of investment from other "investors" no such direction exists.

- Is the funding (debt or equity) from closely affiliated people? For example - members of a religious organisation. However, we recognise that affinity frauds (investment frauds that prey upon members of identifiable groups, such as religious or ethnic communities, language minorities, the elderly, or professional groups) is occasionally a problem in the NFP sector. If funding is from closely affiliated people, has an appropriate cost/benefit balance been struck?

- Quantum factors:

    - How much money is being sought?

    - What % of net assets of the entity?

- What % of total net assets for all borrowings after this borrowing?

- What % of debt servicing to total revenue of entity?

Other matters

Given the decision to have at least six different reporting regimes, the success of the XRB in the multi-standard environment, in our view, will be assessed by how easy it will be to access and research financial reporting requirements. We have two suggestions to make.

Financial reporting calculator

The Companies Office webpage has a very useful financial reporting calculator. We suggest that this be further developed and refined to cover all of the entities that will be covered or excluded from the new proposed financial reporting framework.

Searchable access to all XRN issued standards and pronouncements

There should be one freely accessible database maintained by the XRB that people can turn to. It should contain all of the financial reporting and auditing standards and any supporting guidance material published by the XRB. The entire database, rather than the individual documents should be fully searchable so that people fail to see how all the various standards interact. The time has come to move on from individual pdf documents – where searches can only be made within that document – to something far more comprehensive.

The name of the legislation

With a significant change occurring with financial reporting in New Zealand and a large number of entities now being caught by the Financial Reporting Act (FRA93) we recommend consideration be given to changing the name of the FRA93 to the Business Reporting Act. Changing the name would not only signal that significant changes have been made to the FRA93 Act, it would also better reflect the increasing importance of reporting on non-financial matters (eg statements of service performance) as for PBEs this is just as important, if not more important, than the reporting on financial matters.

Challenges

We see that the biggest financial reporting challenge is likely to be for NFP entities that are currently using old Kiwi GAAP. If the large NFP experience of transition of NZ IFRS is anything to go by we believe the transition from old Kiwi GAAP to the NFP version of IPSAS will not be easy. We therefore support the proposed later adoption date for NFP reporting entities.

Another challenge will be dealing with the "large" entity, as defined in the new Framework that becomes "not large" at the following balance date. We are unsure whether the entity will have to be "not large" for two consecutive annual accounting periods before it can step down from the Tier 2 reporting requirements. Clarifying this aspect of the regime would be helpful.

Director responsibility statements

Given all the changes that are to take place we would strongly encourage the XRB to take up with the Minister of Commence a legislative need to follow what Australia already has and that is to require directors' responsibility statements for all Tier 1 and Tier 2 Entities. If change to legislation is no longer possible then we hope that the XRB will use all of its powers to actively promote the adoption of these statements when financial statements are prepared.

There will always be an expectations gap between those involved in preparing (and auditing) financial statements and those relying on financial statements but we see directors' responsibility statements as a way of seeking to reduce the extent of the gap. This will encourage directors to focus on the impact of accounting policies that have approved and the level of disclosure that accompanies them. This is particularly relevant in our view given that we are about to enter a new reporting regime.

Please do not hesitate to contact either of us if further insight or background on any aspect of this submission is needed.

Yours sincerely

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National Technical Director

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National Director, Government Advisory

APPENDIX 1

Submission on Accounting Standards Framework for General Purpose Financial Reporting by For-Profit Entities

Introduction/For-Profit Tier Structure	
Q1	Do you agree that the deeming approach should be used to supplement the IASB definition of public accountability for defining the for-profit tiers? If not what alternative would you suggest and why?
	Yes we agree with the deeming approach.
Q2	Do you agree that all publicly accountable for-profit entities should be in Tier 1 regardless of size? If not what alternative would you suggest and why?
	We agree that all publicly accountable for-profit entities should be in Tier 1 regardless of size.
Q3	Do you agree that large for-profit public sector entities should be included in Tier 1? If not what alternative would you suggest and why?
	We agree that large for-profit public sector entities should be included in Tier 1.
Tier 1 Accounting Standards: Supplemented IRFS	
Q4	Do you agree that the accounting standards applying to Tier 1 for-profit entities should be NZ IFRS converged with IFRS, supplemented by additional New Zealand specific standards, and harmonised with Australia as appropriate? If not what alternative would you suggest and why?
	Yes we agree with this approach.
Tier 2 Accounting Standards: RDR	
Q5	Do you agree that: (a) the accounting standards applying to Tier 2 for-profit entities should be a Reduced Disclosure Requirements approach, consisting of the same recognition and measurement requirements as Tier 1 but with disclosure concessions? If not what alternative would you suggest and why? (b) if adopted the Reduced Disclosure Requirements should be harmonised with Australia? If not what alternative would you suggest and why?
	Please refer to our comments in our covering letter. We see that there are two viable options for Tier 2 entities. IFRS for SMEs and a regime based on the proposed Australian RDR regime. While RDR provides cost savings, IFRS for SMEs cannot, and should not be overlooked. What we find particularly appealing about IFRS for SMEs is the guidance is self contained (in

	approximately 250 pages), is to be updated only once every three years thus providing some certainty as to when changes will be made, and was issued by the same body that issued "pure" IFRS that will be used by Tier 1 entities. If adopted we agree that the Reduced Disclosure Requirements should be harmonised with Australia - except where legitimate NZ factors necessitate variations to the required disclosures.
Q6	Do you agree with the disclosure concessions contained in the Proposed Tier 2 Reduced Disclosure Requirements attached to this Consultation Paper? If not which specific concessions would you add or delete and why (please indicate the specific standard and specific paragraph numbers)?
	We agree with all of the RDR disclosures concessions proposed because they follow the architecture of IFRS for SMEs. What we particularly like about the RDR regime is the removal of these disclosure requirements: 1. Financial instrument disclosures – financial risk management objectives and policies – sensitivity/maturity/receivable aged analysis – fair value hierarchy table and related disclosures 2. Impairment disclosures 3. Associate summarised financial information disclosures 4. Various related party and key management disclosures (eg option/shareholdings; aggregate remuneration) 5. Capital management disclosures 6. Operating cash flow reconciliation to profit 7. Accounting Standards Not Yet Effective 8. Auditors remuneration 9. Dividends/imputation credits 10. Previous year's movement reconciliation (for PP&E and intangibles)
Adoption and Transition Arrangements	
Q7	(a) Do agree that the effective date for the new tier structure and the Reduced Disclosure Requirements should be 1 July 2013 or such later date as the amendments to the Financial Reporting Act come into force? If not what date do you suggest? (b) Do you agree that early adoption of the new tier structure and RDR should be permitted from 1 July 2012? If not what alternative would you propose?
	We agree: (a) that the effective date for the new tier structure and the Reduced Disclosure Requirements should be 1 July 2013 or such later date as the amendments to the Financial Reporting Act come into force; and (b) that early adoption of the new tier structure and RDR should be permitted from 1 July 2012.
Q8	Do you agree that entities currently required to prepare GPFR, but which will not be required to do so under the Government's new financial reporting framework, should be able to continue to report in accordance with the existing NZ IFRS Framework for Differential Reporting or old GAAP (including the Old GAAP Framework for Differential Reporting) or the Financial Reporting Order (as applicable) until 1 July 2013 (or such other date as the legislative amendments come into force)?
	We agree with this.

APPENDIX 2

Submission on Accounting Standards Framework for General Purpose Financial Reporting by Public Benefit Entities

Introduction	
Q1	Do you agree that public sector PBEs should be defined by reference to the definition of public entities in the Public Audit Act 2001? If not what alternative would you suggest and why?
	Yes. This is a practical and comprehensive approach to determining the public sector.
Q2	Do you agree that not-for-profit PBEs should be defined as all PBEs other than public sector PBEs? If not what alternative would you suggest and why?
	Yes we agree.
PBE Tier Structure	
Q3	The proposed PBE tier framework incorporates feedback from respondents to the Discussion Document Proposals. Are there any other factors not already considered that you think should be? If so please outline them.
	We have no further comments to make.
Q4	Do you agree that all PBE issuers should be allocated to Tier 1 regardless of their size; or do you think that PBE debt issuers that would not otherwise be in Tier 1 should be able to be in Tier 2 but be required to comply with relevant Tier 1 requirements, particularly relating to financial instruments, to ensure that the needs of their users are met?
	As per our covering letter we recommend that the XRB consider further whether certain NFP issuers should be allowed to fall into Tier 2. If an accommodation can not be found then we agree that all PBE issuers should be allocated to Tier 1 regardless of size.
Accounting Standards	
Q5	Taking the XRB Board's decision to adopt a multi-standards approach as a given, do you agree that a suite of NZ PBE standards that use IPSAS as its base, but which are modified: • for any recognition, measurement or disclosure matters considered inappropriate in the New Zealand context; and • to make them relevant, applicable and understandable in the NFP context be adopted at this juncture (rather than pure IPSAS)? If not what alternative approach would you suggest and why?
	We agree with the modified IPSAS approach at this stage. Longer term New Zealand should be seeking to influence IPSAS to ensure that any good ideas that we have are incorporated as part of IPSAS; and we agree with the comment made by the XRB in paragraph 62 that "A move to "pure" IPSAS is an aspiration over the longer term".

Q6	Do you agree that the same recognition and measurement requirements should apply to all tiers, subject to the possibility of some concessions for Tier 3 entities to reflect the simple nature of their requirements? If you do not agree, please identify the specific recognition and measurement requirements that you think should differ between tiers.	
	We agree that the same recognition and measurement requirements should apply to all tiers, subject to the possibility of some concessions for Tier 3 entities to reflect the simple nature of their requirements.	
Q7	Do you agree that a Reduced Disclosure Requirements version of the full NZ PBE Accounting Standards should apply to Tier 2 entities? If not what alternative approach would you suggest and why?	
	Please refer to our comments in our covering letter. While RDR will provide some cost savings, there are some recognition and measurement concessions in IFRS for SMEs that, in our opinion, should not be overlooked.	
Q8	Are there any other matters relating to the accounting standards for PBEs that have not already been considered by the XRB Board that you think it should consider? If so please outline them.	
	We have no further comments to make at this stage.	
Adoption and Transition Arrangements		
Q9	Do you agree that (a) all public sector PBEs should be required to adopt the NZ PBE Accounting Standards in the same financial year; and (b) the target date for this adoption should be the financial year beginning 1 July 2013? If not what alternative would you suggest and why?	
	We agree with the same date for adoption for all public sector PBEs and also that the adoption date should be for the financial year beginning 1 July 2013. We recognise that for some entities this might be a challenging deadline to work to, but in our view it is reasonable.	
Q10	Do you agree that the target date for NFP entities to compulsorily adopt the NZ PBE Accounting Standards should be financial years beginning on or after 1 July 2014, with early adoption from 1 July 2013? If not what alternative would you suggest and why?	
	We agree that the target date for NFP entities to compulsorily adopt the NZ PBE Accounting Standards should be financial years beginning on or after 1 July 2014, with early adoption from 1 July 2013.	