

Shaping our market's future

31 January 2014

Consultation: Financial Reporting

Regulatory policy for financial reporting designations and exemptions

When the Financial Markets Conduct Act 2013 comes into effect on 1 April 2014 we will have regulatory powers to vary the financial reporting obligations of FMC reporting entities by:

- Varying public accountability designations, and
- Granting exemptions.

This paper is for FMC reporting entities. It gives a brief background to the relevant changes the FMC Act brings about, explains our policy on how we intend to apply our new powers, and sets out the immediate changes we propose to make to both designations and exemptions under these powers.

We invite you to review our policies and the proposed changes and share your feedback on them with us. This is our chance to work together to shape the future for our industry.

Submissions close on 28 February 2014. The form at the back provides more details.

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Part 1. Overview of the changes

A. What is our role?

Under the Financial Markets Conduct Act 2013 (FMC Act) we will be the primary financial reporting regulator for all FMC reporting entities – and will have regulatory powers to vary public accountability designations, and to grant exemptions.

We can only use these powers to support the purposes of the FMC Act. Our aim is to find a balance between ensuring the provision of appropriate financial information for those who need it and, minimising undue costs for those providing it.

The **main purposes** of the FMC Act are to (Section 2):

- Promote confident and informed participation of businesses, investors and consumers in the financial markets
- Promote and facilitate the development of fair, efficient and transparent financial markets.

The **additional purposes** (Section 3) are to:

- Provide for timely, accurate, understandable information to be provided to people to help them make decisions about financial products or services
- Ensure appropriate governance arrangements apply to financial products, and certain financial services, to allow effective monitoring and reduced governance risks
- Avoid unnecessary compliance costs
- Promote innovation and flexibility in the financial markets.

What are we proposing?

We propose to make immediate changes to public accountability designations for some entity classes, and introduce some class exemptions.

This paper sets out our proposals for assessing designation changes or exemptions (both for classes of entities or for small groups or individual entities). For those who want to know more, we've also included an outline of the more detailed thinking behind our decisions.

We're setting these now so you have time to align your systems before you need to prepare financial statements under the new financial reporting requirements in the FMC Act.

Please note we will consult separately on any exemptions relating to offer documents before the new disclosure regime starts on 1 December 2014.

Timings

The timings for the changes are:

- Consultation workshops in February 2014 (see our website for details)
- Feedback due in by 28 February 2014
- The new law comes into force on 1 April 2014
- Policies and notices published in April 2014 (indicative timing).

Entities will become FMC reporting entities at different points in time. In March 2014 we will publish transitional guidance to help you work out which Act you need to report under for each financial year during the transitional period.

B. Background

The Financial Markets Conduct Act 2013 includes a number of changes from the financial reporting requirements in the Financial Reporting Act 1993 (FRA 93). Here's a quick summary of the key changes that will mark the new regime. Please note there is a list of the terms used and definitions on page 5

Consolidates requirements

The FMC Act consolidates the financial reporting requirements for an FMC reporting entity in Part 7. It covers the accounting record keeping requirements currently under the Companies Act 1993 and the Securities Act 1978, as well as the preparation, audit and registration requirements of the FRA 93.

Covers more entities

The FMC Act applies to more entities than before. The concept of a FMC reporting entity is broader than the definition of an 'issuer' under the FRA 93, although it doesn't cover all financial market participants.

- The **definition includes** most entities who were 'issuers' previously, as well as most licensees under the Financial Markets Supervisors Act and FMC Act.
- The **definition does not include** – brokers, qualifying financial entities, financial adviser businesses, licensed auditors and audit firms, licensed independent trustees, or retirement village operators.

At a glance: FMC reporting entities

Issuers of financial products under regulated offers	- those who make regulated offers under the FMC Act and, after a transitional period, those who made public offers under the Securities Act
Market services licensees (except independent trustees)	- MIS managers, DIMS providers, derivatives issuers, providers of peer to peer lending services and crowd funding services
Licensed supervisors	- under the Financial Markets Supervisors Act 2011
Listed issuers	- those listed on a market licensed under the FMC Act
Operators of licensed markets	- except overseas-regulated markets
Recipients of money from conduit issuers	- recipients of funds from regulated offers under the FMC Act and, after a transitional period, recipients of money from public offers under the Securities Act (during the transitional period, Securities Act issuers and recipients of money from Securities Act offers will continue to report under the FRA 93)
Registered banks	- under the Reserve Bank of New Zealand Act 1989
Licensed insurers	- under the Insurance (Prudential Supervision) Act 2010
Credit unions	- under the Friendly Societies and Credit Unions Act 1982
Building societies	- under the Building Societies Act 1965
People who have made excluded offers and are called in by Regulations	- People that have relied on exclusions in Schedule 1 of the FMC Act and are deemed to be FMC reporting entities by regulations. These regulations have not yet been finalised.

Introduces concept of ‘higher public accountability’

The FMC Act identifies classes of entities it deems to have higher public accountability – all other classes of entities have lower public accountability. These are default designations and the FMC Act empowers us to vary these for either individual FMC reporting entities, or classes of entities.

The public accountability designations influence which tier of the External Reporting Board (XRB) Accounting Standards Framework an entity will be in and, in turn, whether they will have to apply full or reduced accounting standards to their financial statements.

XRB have revised their Accounting Standards Framework for consistency with the FMC Act’s requirements to take public accountability designations into account.

XRB Accounting Standards Framework			
Tier 1	Full accounting standards with no disclosure concessions (NZ IFRS or PBE Standards)	For-profit entities will be on tier 1 or 2 <i>Higher public accountability entities will be in tier 1, lower accountability entities likely to be in tier 2</i>	Public benefit entities may be in any tier <i>Higher public accountability entities will be in tier 1, lower accountability entities likely to be in tier 2 or 3</i>
Tier 2	Reduced accounting standards with disclosure concessions (NZ IFRS RDR or PBE Standards RDR)		
Tier 3	For public benefit entities only – a separate set of accrual accounting standards, with limited disclosures		
Note: XRB’s Accounting Standards Framework also includes a fourth tier for public benefit entities that are permitted by law to prepare cash accounts. FMC reporting entities will not be within this tier.			

More flexible approach to exemptions

The FMC Act also gives us the power to grant exemptions where they support the purposes of the Act. This is a more flexible approach than under the FRA 93 where we had to be satisfied that there was no significant detriment to investors having regard to the financial reporting requirements in the jurisdiction where the entity is incorporated.

Another significant change is that we can now grant exemptions to any FMC reporting entity (local or overseas) if it is appropriate. Before only recipients of money from conduit issuers and overseas entities could be exempted.

Other changes in the FMC Act that will affect exemptions include:

- You won't need 'parent' financial statements if you prepare group financial statements (previously we granted a number of exemptions for overseas issuers that removed the need to prepare separate parent financial statements where this was not required under overseas law)
- Audit exemptions can be granted on their own (before, you needed an exemption from preparing financial statements).

Overseas accounting standards

All FMC reporting entities will have to apply NZ GAAP, unless they are granted an exemption by FMA. The Companies Office will no longer have the discretion to accept overseas GAAP statements for FMC reporting entities – overseas entities will need an exemption if they wish to use an overseas GAAP. Our initial exemption proposals are included in Part 3.

C. Terms used

FRA 93	Financial Reporting Act 1993
FMC Act	Financial Markets Conduct Act 2013, as amended by the Financial Reporting (Amendments to Other Enactments) Act 2013
Full accounting standards	NZ International Financial Reporting Standards (NZ IFRS), or Public Benefit Entity Standards (PBE Standards)
Reduced accounting standards	NZ IFRS with disclosure concessions under the Reduced Disclosure Regime (NZ IFRS RDR), or PBE Standards with disclosure concessions under the Reduced Disclosure Regime (PBE Standards RDR), or Public Benefit Entity Simple Format Reporting Standards – Accrual
NZ GAAP	generally accepted accounting practice as defined in the Financial Reporting Act 2013. This comprises applicable financial reporting standards and authoritative statements issued by XRB
Entity	A FMC reporting entity under the FMC Act
FMA	Financial Markets Authority – also referred to as we, us, our
MIS	Managed investment schemes

XRB	External Reporting Board (an independent Crown entity responsible for setting both financial reporting standards, and auditing and assurance standards)
Stepping stone market	A regulated financial product market that provides lighter regulation for listed issuers of securities quoted on that market

Part 2. Public accountability designations

A. Background

Under the FMC Act we have the power to vary the public accountability designations, which will influence the accounting standards an entity must use when preparing its financial statements.

We have reviewed the default designations set out in the FMC Act, and are proposing changes for some entity classes.

Currently all 'issuers' are in the highest tier and must prepare financial statements under full accounting standards. In future FMC reporting entities will include extra classes of market participants, and not all will be in the highest tier and required to apply full accounting standards.

The tier an entity is in is determined by XRB's Accounting Standards Framework, which takes public accountability designations into account.

If your market activities come under more than one class and any of them are of 'higher public accountability', your entity will have to meet full accounting standards.

B. What are we proposing?

We have reviewed the default public accountability designations in the FMC Act, and propose to make immediate changes for some entity classes. We invite your comment on our proposals.

In most cases we propose no change from the default. However, we are considering changing the designations for three classes of entities:

- Not-for-profit debt issuers
- Licensed derivative managers
- Recipients of money from a conduit issuer.

On the following pages there's a summary of the public accountability designations that will apply to classes of entities, and the reasons behind the proposed changes.

C. At a glance: public accountability – our proposed designations

The detailed thinking behind these designations is outlined in section F

<p>1. Higher public accountability</p> <p>Based on XRB Accounting Standards Framework full accounting standards will apply</p> <p>Full NZ IFRS for for-profit entities, or full PBE standards for public benefit entities</p>	<ul style="list-style-type: none"> • Equity issuers who make a regulated offer and have more than 50 shareholders • Debt issuers who make a regulated offer (exception for small one-off offers by not-for-profit entities * may apply) • Licensed derivative issuers* • Licensed MIS managers (in respect of the financial statements of the MIS they manage) • Listed issuers • Recipients of money from a conduit issuer* • Registered banks • Licensed insurers • Credit unions • Building societies <p><i>*denotes main changes</i></p>
<p>2. Lower public accountability</p> <p>Based on XRB Accounting Standards Framework reduced accounting standards will apply</p> <p>NZ IFRS RDR for for-profit entities, or PBE standards RDR for most public benefit entities</p>	<ul style="list-style-type: none"> • Licensed MIS managers (in respect of the manager’s own financial statements) • Licensed providers of DIMS (under the FMC Act) • Licensed peer-to-peer lending service providers • Licensed crowd funding service providers • Licensed supervisors • Licensed market operators (domestic)

D. Proposed main changes in designations*

1. **Not-for-profit debt issuers** – some simple not-for-profit entities may be re-designated lower accountability where they only make a small one-off offer not covered by the ‘small offers’ exclusion in the FMC Act (for example because the offer is made to more than 20 people). A re-designation would provide relief to smaller not-for-profit entities where the burden of preparing full financial statements may be significant and outweigh the benefit to investors.
2. **Licensed derivative issuers** – propose to move to higher public accountability because (1) they hold material levels of financial instruments so full disclosures about financial instruments is needed in their statements and (2) investment is direct so investors take a credit risk and need full information to assess that risk.
3. **Recipients of money from a conduit issuer** – propose to move to higher public accountability level to match conduit issuers because they should have the same level of accountability as if they issued the product themselves. This is because (1) when conduit issuers raise money the main risk for investors often comes from the financial performance of the recipient of funds, rather than from the conduit issuer, and (2) the issuer’s ability to pay returns or make repayments often depends on them receiving repayments from the recipients of the investment money.

E. Our policy: assessing public accountability

These are the main considerations we intend to use to assess changes to designations

<i>Principle</i>	<i>Our thinking</i>
1. Information required by investors and analysts	What information is likely to be needed by investors and investment analysts, and how important are the extra disclosures required by full accounting standards? More financial information is required if there is direct investment in the entity, because (1) the fair value of a financial product may depend on the financial performance of the entity and (2) the failure of the entity is more likely to cause financial loss to investors. Where this is the case, the entities should generally have higher public accountability. Entities only licensed to provide financial services will often have lower public accountability.
2. Treatment under IASB's accounting framework (international standards)	Would the entity be 'publicly accountable' under the International Accounting Standards Board (IASB) definition? This definition includes entities (1) whose financial products are traded on a public market and (2) that 'hold assets in a fiduciary capacity' for a broad group of people as one of its primary businesses – this applies to institutions such as 'banks, credit unions, insurance providers, securities brokers/dealers, mutual funds, and investment banks'. Entities that meet this definition should generally have higher public accountability.
3. Information required by regulators	What level and nature of information is needed for prudential regulation or monitoring of other financial resource requirements? Prudentially regulated entities should have higher public accountability, as the information in their financial statements is used as part of their regulation.
4. Relevance of disclosures omitted under reduced accounting standards	Does the nature of the entity's business make the extra disclosures required under full accounting standards important for that entity? For example, extra disclosures on financial instruments that are not required under reduced accounting standards will be important for banks, non-bank deposit takers, and derivative issuers. Where this is the case, entities will generally be higher public accountability to ensure these disclosures are made.
5. Consistency between classes	Is there consistency where activities are similar or related? For example, most listed issuers will also be issuers of financial products under a regulated offer (or a Securities Act offer). Therefore, listed issuers should not have a lower level of public accountability than equivalent unlisted issuers.
6. Cost of reporting under full accounting standards	Are the costs of producing financial statements under full accounting standards justified? Reporting costs can be significant particularly for small business and not-for-profits, so we will provide relief where appropriate. But if full standards apply to many in a class, we may require them of everyone in that class (we note some disclosures can be omitted under full standards if they are not material).
7. Other options for the activity	Are there other ways the business can undertake the activity without becoming an FMC reporting entity? For example, by relying on exclusions in Schedule 1 of the FMC Act.
8. Consistent policy across the FMC Act	Are there other exemptions for the entity (or subset of entities) and what is the appropriate level of public accountability given the overall regulatory treatment? For example, if a class of entities can rely on an exemption from disclosure requirements for offers and/or governance requirements, it may be appropriate to also give financial reporting concessions for the same reasons.

F. Class designations – our thinking

The FMC Act identifies classes of entities with higher public accountability, and by default other classes have lower accountability. We have reviewed the designations for all entity classes.

Here we set out the thinking behind our proposals to either retain the default set by the FMC Act, or to re-designate entity classes.

1. Equity issuers who make a regulated offer and have over 50 shareholders

Default: higher public accountability | Proposed: no change

Generally a high level of disclosure in financial statements is relevant to shareholders because shares are an investment in the issuer, and share value is directly linked to the company's financial position and performance. For voting shares, the disclosures may be relevant to voting decisions.

Issuers of equity securities vary in size, complexity and activities. The extra disclosures required by full accounting standards may be less important in some cases – but there are already provisions to support those entities:

- a. Companies with less than 50 shareholders (who only issue regulated products that are voting shares) are not FMC reporting entities
- b. There are ways to make small/private offers without becoming a FMC reporting entity
- c. Small-medium entities with simple financial arrangements can apply a materiality threshold under the financial reporting standards so they don't have to provide disclosures that are not relevant or useful to investors.

Companies with over 50 shareholders are not generally very small, and this size is the threshold associated with a higher level of obligations in other legislation, including the Takeovers Act 1993.

2. Debt issuers who make a regulated offer

Default: higher public accountability | Proposed: no change for most; exception for some offers by not-for-profits

Most debt issuers making regulated offers are banks, non-bank deposit takers, large corporates or corporate groups and full disclosures are of significant interest to investors, analysts and regulators.

Banks and financial institutions are 'publicly accountable' under the IASB definition and higher public accountability with full reporting is consistent with international practice.

Investors and analysts are likely to need the extra disclosures about management of financial instruments and impairment of assets (especially loans) required under full accounting standards.

The Reserve Bank is likely to require full reporting for regulatory purposes.

For issuers of corporate bonds who are not financial institutions, the scale and complexity of the business often warrants the preparation of full financial statements.

Smaller, less complex corporate debt issuers can apply materiality so they don't have to provide disclosures that are not relevant or useful to investors.

Possible exception

We are considering an exception for smaller not-for-profit entities making one-off non-commercial offers, which will provide relief to people who make small loans to support a charitable project, or to help a cultural, religious, sport or recreational organisations get facilities or equipment, and will reduce reporting costs for the charity or club.

It is likely that individual loans and the total that can be raised will be capped. Approaches we are considering include basing borrowing caps on:

- a. The \$2 million threshold used in some Schedule 1 exclusions, or
- b. Thresholds in any exemptions under the FMC Act that correspond to those in the Securities Act (Charities-Debt Securities) Exemption Notice 2013, which provide for charities to raise money for their charitable purpose.

The exemption won't be available to entities that raise money as a conduit issuer or for lending activities, as lenders are likely to need disclosures about financial instruments, impairment of assets, and capital management. We don't consider an exception is appropriate for public sector or for-profit entities.

3. Licensed derivative issuers

Default: lower public accountability

Proposed: re-designate to higher public accountability

Derivative issuers are likely to be 'publicly accountable' under IASB's standards, and should be required to comply with full accounting standards in line with international standards. We also consider higher public accountability is appropriate because of these characteristics of the business:

- a. Clients enter into contracts which expose them to credit risk if issuers can't meet their obligations
- b. Issuers have a significant level of financial instruments on their balance sheet, so it is appropriate to provide full disclosures about these.

We also intend to apply on-going capital adequacy requirements to most derivative issuers, and the greater detail provided under full accounting standards may help us assess compliance.

4. Licensed fund managers in respect of financial statements for a MIS

Default: higher public accountability | Proposed: no change

Managed investment products are important to many less experienced retail investors, so these schemes need higher public accountability. The IASB definition provides for mutual funds to be 'publicly accountable'.

Scheme arrangements vary depending on the type of scheme and the investment strategy. They range from schemes with very large portfolios of mixed assets and complex trading strategies – to small schemes with a simple strategy or single investment where only limited disclosure is needed.

There may be scope to lower the designation of some small, simple funds, particularly forestry schemes and single-site property funds. But we don't propose to make changes because many of the more detailed disclosures won't be relevant for these types of funds.

5. Other Licensees

5.1 Licensed MIS managers (in respect of their own financial statements)

5.2 Licensed DIMS providers (under the FMC Act)

5.3 Licensed peer-to-peer lending service providers

5.4 Licensed crowd funding service providers

5.5 Licensed supervisors

5.6 Licensed market operators (domestic markets only)

Default: lower public accountability | Proposed: no change

With these entities, the investor does not invest in the licensee – rather the licensee provides a service to manage or facilitate an investment. The licensee's conduct or performance can impact on the investment performance, but its financial position is only one component of its ability to provide the market service effectively. These entities do not have investor funds invested in their business, and their financial performance does not directly contribute to the investment returns investors will receive.

The main purpose of the licensee's financial statements is to show investors and FMA that:

- a. You have sufficient resources and funds to continue providing an effective service
- b. For licensed market operators, that you are able to allocate adequate resources to meet your general obligations (especially adequate market oversight).

So the option to apply reduced accounting standards is appropriate.

We note this designation represents a change for MIS managers who will have lower public accountability, and so in future can apply reduced accounting standards to their own financial statements (under the FRA 93, full accounting standards applied to both the managers and the schemes). Schemes will have higher public accountability and must continue reporting under full accounting standards.

6. Listed issuers

Default: Higher public accountability | Proposed: no change

The default 'higher public accountability' designation is appropriate for listed issuers because:

- a. They are 'publicly accountable' under IASB's definition (including those listed on a stepping-stone market)
- b. This is consistent with the higher public accountability designation given to larger equity and debt entities
- c. Listed issuers generally have to meet higher on-going disclosure standards.

Stepping-stone markets:

We considered whether the designation for issuers quoted on a stepping stone market should be different, but don't propose to change this generally. We may consider applications to re-designate entities listed on a particular market if this fits with the overall level and structure of disclosure for that market. As many entities on stepping stone markets will have made regulated offers of equity securities, we would need to consider consistency with other classes, particularly unlisted issuers of equity securities. The FMC Act also provides the ability for regulations to remove issuers listed on a particular market from being a FMC reporting entity all together.

7. Recipients of money from a conduit issuer*

Default: lower public accountability | Proposed: re-designation to higher public accountability

Recipients of money from a conduit issuer receive all/much of the proceeds from a regulated offer. This category also includes those who receive the proceeds of a public offer under the Securities Act after the transitional period.

The conduit issuer's primary activity is often raising money for related companies, while one or more secondary recipients within the group carry out the substantive business. The risk for investors is often closely linked to the recipient's ability to generate the returns required to repay the conduit issuer (and in turn investors).

So it's appropriate that the recipients of money from a conduit issuer provide the same level of financial information as they would have to provide if they raised the funds themselves. Generally debt and equity issuers, and MIS managers in respect of schemes, have higher public accountability.

This re-designation will impose the same obligations on recipients of money from conduit issuers as they have currently under the FRA 93.

We don't plan to introduce an exemption for this category to correspond with the one proposed for small, simple not-for-profit debt issuers. It's not appropriate for complex commercial structures involving conduit issuers.

8. Financial institutions

8.1 Registered banks

8.2 Licensed insurers

8.3 Credit unions

8.4 Building societies

Default: Higher public accountability | Proposed: no change

Financial institutions are generally 'publicly accountable' under IASB's definition. The nature of their business makes it likely they will have commercial lending, insurance obligations, derivatives or other financial instruments on their balance sheet. So the information provided under full accounting standards on financial risk management, impairment of assets and capital management is important.

Their financial position is important to their clients (including depositors and policy holders), as there is a significant level of credit risk for clients under debt securities and other financial products, insurance policies, custody arrangements, and other transactions.

These entities will be subject to prudential regulation by RBNZ under the Reserve Bank of New Zealand Act or the Insurance (Prudential Supervision) Act.

9. People who have made excluded offers and are called in by Regulations

Default: lower public accountability | Proposed: yet to be determined

Schedule 1 of the FMC Act provides a number of exclusions from when an offer is a 'regulated offer'. People who rely on these exclusions will not generally be FMC reporting entities, but can be called in by regulations.

It is contemplated that Regulations will prescribe some issuers of equity securities that have relied on certain exclusions and have more than 50 shareholders. The content of the Regulations is yet to be finalised.

At this stage, we have not determined whether these entities should be designated higher or lower public accountability. We will form a view on this, and determine whether consultation on that position is appropriate, once the final content of the Regulations is known.

Part 3. Financial reporting exemptions

A. Background

From 1 April 2014 we will have much broader exemption powers under the FMC Act. At this stage, we don't intend to withdraw the existing exemptions under the Financial Reporting Act 1993. These will still be available, subject to any amendments or expiries, for entities who continue to report under the FRA 93 during the transition period (we will publish transitional guidance soon).

Our proposed exemptions policy is not significantly different to the current policy, although we have made refinements to:

- Align the policy with new initiatives in the FMC Act
- Extend the policy to cover new circumstances where we can consider exemptions.

However, the structure of the class exemptions we're proposing are likely to be significantly different from the current ones.

B. Policy considerations

1. Does it promote the purpose of the FMC Act?

Before granting an exemption under the FMC Act, we must be satisfied that it is necessary or desirable to promote the purposes of the FMC Act.

We note that this will often involve balancing the purposes of the FMC Act. While financial reporting exemptions will help reduce compliance costs, and may encourage more businesses to enter the marketplace (one of the FMC Act's purposes), reducing financial disclosures may be contrary to other purposes in the FMC Act. So there must be a good balance between benefits to reporting entities and the quality and timeliness of financial information.

2. Can we make our approach more consistent?

In general terms, where practical and appropriate we want to simplify the different classes of exemptions. Where exemptions are limited by jurisdiction, we want to include as many appropriate jurisdictions as possible.

3. Will it affect those who currently rely on an exemption?

There are many issuers who currently rely on class or individual exemptions under the FRA 93 or Securities Act. We propose to retain exemptions for these entities, unless it isn't appropriate or necessary under the FMC Act.

C. Summary of proposed exemptions policy

This is a high level overview of our proposed exemptions policy. Below we summarise exemptions that could be granted to New Zealand incorporated FMC reporting entities or to any FMC reporting entity, whether incorporated here or overseas. On the next page are those that only apply to overseas incorporated entities. More detail is outlined in section D.

1. Proposed exemptions: for New Zealand and overseas entities		
Type of exemption	Currently	Under FMC Act
a. Compliance with overseas law and accounting standards by NZ entities	No exemption power under the FRA 93.	Exemptions considered on merit. There will be a high threshold for demonstrating an exemption is needed.
b. Recipients of money from conduit issuers	Exemptions are possible when all material information is available from another source. They are considered on an individual basis as the circumstances are very case specific. Applications are rare.	No significant change to policy.
c. Conduit issuers	No exemption power under the FRA 93.	Exemptions considered on merit. We will consider individual applications on a similar basis to that applied to recipients of money from a conduit issuer. We expect exemptions to be rare.
d. Partial and technical exemptions	Exemptions to address specific issues for overseas issuers are considered on an individual basis. Applications are rare.	No significant change to policy. But we will also be able to consider exemptions for New Zealand entities.
e. Exemptions to extend filing deadlines	Exemption powers exist for overseas entities, but no exemptions have been granted.	Exemptions considered on merit. There will be a high threshold for extensions. Shorter filing deadlines may result in applications. You must demonstrate specific circumstances that make timeframes unreasonable or inappropriate – it is unlikely we would grant exemptions just because you don't make arrangements in time.

2. Proposed exemptions: for overseas entities only

Type of exemption	Currently	Under FMC Act
a. Accounting records	<ul style="list-style-type: none"> Complete exemptions are included in a number of class and individual exemption notices Exemptions are linked to the circumstances of an offer. 	<p>Exemptions will be more limited.</p> <ul style="list-style-type: none"> Exemptions from keeping accounting records to support NZ GAAP financial statements will be linked to preparing financial statements under an overseas GAAP. Exemptions from keeping records in NZ and in English will be linked to whether the entity's circumstances mean NZ based people need access to the records.
b. Use of overseas GAAP financial statements	The Registrar of Companies has broad discretion to accept overseas GAAP financial statements without the entity being exempt. Class exemptions are generally linked to the place of incorporation and the standards in that jurisdiction.	<p>Exemptions will be broader.</p> <p>The Registrar of Companies won't have discretion to accept overseas GAAP financial statements. Exemptions will be broader, but still based on the adequacy of the overseas reporting framework and applicable GAAP.</p>
c. Use of overseas auditors	<p>Exemptions have been given if issuers and their auditor are subject to regulation and oversight standards similar to those in NZ. This includes entities that:</p> <ul style="list-style-type: none"> Extend overseas regulated or incidental offers to NZ investors (with a broader approach for Australian issuers) Are listed on an overseas exchange and NZX Are regulated as insurers overseas and in NZ Are regulated as banks overseas and offer debt in NZ (on an individual basis). 	<p>No change to high-level policy.</p> <p>There will be refinements to specific categories covered by exemptions.</p>
d. Registration of financial statements	Exemptions from filing financial statements are relatively rare. They are reserved for overseas companies with a very low and transitory involvement in NZ markets (such as overseas listed issuers who include a few NZ investors in a rights offer, or in an offer arising from a restructuring transaction).	<p>No change to existing policy and exemptions.</p> <p>We may exempt overseas companies who only become FMC reporting entities because they made an offer that would be excluded under Schedule 1 of the FMC Act when it comes into effect.</p>
e. Branch financial statements	Overseas companies with a NZ business must prepare and register branch financial statements. These can be prepared and audited overseas (under GAAP) if the entity as a whole has a corresponding exemption.	No change to existing policy.

D. Exemptions – our thinking

Our approach to financial reporting exemptions under the FMC Act is based on the approach taken under the FRA 93, but we are proposing refinements to reflect the new regime.

1. Accounting records

for overseas entities only

Generally, we won't grant total exemptions from the accounting record keeping requirements of the FMC Act. But we may grant exemptions for certain aspects which cause difficulties for some entities.

a. Keeping records to comply with New Zealand standards

Section 445 requires your entity to keep accounting records that enable you to prepare financial statements in accordance with New Zealand GAAP. This may not be practical if you prepare statements using an overseas GAAP – it may be more appropriate to keep records that comply with those standards instead. You'll need an exemption to use an overseas GAAP, but if we grant this, we'll also consider an exemption from Section 445.

b. Holding records in New Zealand

Section 456 requires that where your accounting records are kept overseas, you must also hold documents in New Zealand so you can prepare financial statements and annual reports required here. This is not practical if you offer financial products here but have no other business in New Zealand.

c. Keeping records in English

Section 457 requires your financial records to be in English, or in a form easily converted to English. If your main place of business is in a non-English speaking country, it may be more practical to keep your records in another language and duplicating them in English may increase compliance costs.

d. When is an exemption appropriate?

In general for **sections 456 and 457** we'll only grant an exemption if there is a low likelihood of relevant people in New Zealand needing to inspect your records. Your entity won't be exempted if:

- You have, or must have, a New Zealand resident director
- You must appoint a supervisor
- You must use a New Zealand auditor
- We or other New Zealand regulators need to access the records for monitoring (so licensees, supervisors, entities regulated by the Reserve Bank of New Zealand, and those who offer financial products mainly in New Zealand are less likely to be exempted).

We anticipate there will be class exemptions if your entity offers equity, debt or managed investment products – and your offer and governance obligations are mainly regulated in another appropriate jurisdiction.

2. Use of overseas GAAP standards

for overseas entities only

In future, your entity will need an exemption to use an overseas GAAP – the Registrar of Companies will no longer have discretion to accept financial statements prepared under an overseas GAAP.

a. Exemption to use GAAP standards

We propose an exemption to allow overseas entities to continue using certain overseas GAAP financial statements in New Zealand, providing you:

- Are required to use *that* GAAP in a relevant *specified* jurisdiction, or
- Elect to use that overseas GAAP from a small range of acceptable GAAPs permitted in the relevant *specified* jurisdiction, and
- Can use that GAAP in your home jurisdiction.

Before we ‘specify’ a jurisdiction we need to be satisfied there is adequate regulatory control and enforcement to promote compliance with that jurisdiction’s GAAP. We also need to know that, if required, the overseas regulator will co-operate with us. For example, they belong to the International Organisation of Securities Commissions and are party to the IOSCO Multilateral Memorandum of Understanding. The jurisdictions will be specified in the exemption notice.

Initially we are likely to base ‘specified jurisdictions’ on those already recognised in class exemptions under the FRA 93 (Australia, the United States, Canada, the United Kingdom, Ireland, France, Germany, the Netherlands, Switzerland, Singapore, and Hong Kong). We’ll also consider other jurisdictions identified as relevant during this consultation process.

The use of an overseas GAAP will be linked to your main place of operation rather than where you are incorporated. For example, if your entity is incorporated in Bermuda but mainly operates in the United States, an exemption would let you prepare financial statements under US GAAP, providing you must do this under United States law.

We don’t propose to grant an exemption if you elect to comply with a particular overseas GAAP, but are not required to do so by law.

b. Only specified GAAPs may be used

We intend to specify which overseas GAAPs may be used in the exemption notice. We are still identifying and assessing the various standards and seek submissions on this. Initially we will consider the following:

- Australian IFRS
- EU IFRS
- US GAAP
- IFRS (unmodified international standards)
- Singapore FRS
- HK FRS
- Canadian IFRS
- UK GAAP
- German GAAP
- Japanese GAAP.

c. Reduced GAAP standards

We'll only approve the use of a reduced GAAP standard if:

- Your entity is of lower public accountability
- It is an approved reduced standard in relation to the GAAP you are using, and is the equivalent of the New Zealand reduced standard
- The reduced standard doesn't affect the recognition or measurement of any account balances.

d. Registered schemes and GAAPs

Registered managed investment schemes (MIS) will only be able to use overseas GAAP for their financial statements if the scheme is:

- Constituted outside New Zealand
- Offered to the public under a regulated offer in the overseas jurisdiction it was constituted.

If you're an overseas licensed MIS manager this may mean you can prepare your own financial statements using an overseas GAAP – but you'll still need to prepare the financial statements for some or all of your registered schemes using New Zealand GAAP.

3. Audit of financial statements

for overseas entities only

a. Exemptions policy

Our policy for exemptions from using a licensed auditor will be broadly the same as the policy for 'full exemptions' under the FRA 93. We propose to allow exemptions where:

- Your offer is ancillary to a regulated offer in your home jurisdiction
- You are a Australian entity and the offer in New Zealand is part of a regulated offer in Australia
- Your offer is an incidental offer made primarily in another jurisdiction (for example, employee share purchase or dividend reinvestment schemes)
- Your entity is listed on an exchange in your home jurisdiction
- You are regulated as a bank in your home jurisdiction, and are an FMC reporting entity because you offer debt securities here
- You are regulated as an insurance company here and in your home jurisdiction.

All entities that receive an exemption from having an audit in accordance with the FMC Act will instead be required to have their financial statements audited by an appropriately qualified overseas auditor.

b. Offers made primarily in New Zealand

Exemptions are unlikely to be granted for offers made solely or primarily in New Zealand, unless we are satisfied that both your entity and your auditor have the same level of regulation and oversight as a New Zealand issuer and its auditor.

c. Alternative licensing standards for overseas auditors

We are aware the proposed audit exemption policy won't exempt all overseas entities with reason to use an auditor from their home jurisdiction. So we're considering allowing some overseas auditors to become licensed here without meeting all of the current minimum standards (including completing courses in New Zealand commercial law) where these are not relevant to the FMC audits they undertake.

The auditor would need to be qualified and regulated in a jurisdiction with an equivalent audit oversight regime to the Auditor Regulation Act 2011. The licence would only apply if the audit client's main financial reporting obligations are in the auditor's home jurisdiction. This won't affect Australian auditors, who are already recognised here under the Trans-Tasman Mutual Recognition Act 1997.

The approach would provide greater visibility of who is auditing FMC reporting entities than where exemptions are used, and would allow us to exclude some auditors if necessary. However, there are issues with the proposal in the short term. For example, this could only apply to jurisdictions prescribed in the Auditor Regulations 2012 (which don't cover all relevant jurisdictions, such as Japan, Canada and Switzerland).

Currently, overseas audit companies or limited liability partnerships can't become registered audit firms here, so their auditors can't sign off reports in the firm's name. There are legislative proposals to address this but these changes will not be in effect by 1 April 2014. We will publish a separate consultation paper before making any final decisions on changes.

4. Registration of financial statements for overseas entities only

We plan to continue the same approach towards registering financial statements. Most overseas incorporated entities will still have to publicly register their financial statements in New Zealand. However, we propose to consider exemptions in some limited circumstances.

a. Limited and transitory involvement

We may consider granting an exemption if the entity's involvement in the New Zealand market is limited and transitory. This may apply when:

- Your entity issues debt, equity or managed investment products
- Your offer is made under the laws of an overseas jurisdiction
- The offer is made to New Zealand investors solely because they have already participated in the financial markets of that jurisdiction (for example by buying a particular security on an exchange in that jurisdiction)
- For that offer you didn't have to fully comply with New Zealand law relating to regulated offers of financial products (or the offer would be exempt under the FMC Act)
- The participating New Zealanders can reasonably be expected to understand that your offer and on-going obligations are under the laws of the overseas jurisdiction
- Appropriate financial information will be available through another source (for example through an overseas exchange).

b. Incidental offers

We have had suggestions that incidental offers, such as overseas entity's employee share purchase scheme, should be exempt from our registration requirements.

For consistency, we are considering an exemption if:

- Your offer could be made under a Schedule 1 exclusion (and you wouldn't become an FMC reporting entity as a result), and
- You are only an FMC reporting entity because that offer was made under the Securities Act.

However, if your offer is, or would be, a regulated offer under the FMC Act, you'll need to register financial statements in New Zealand.

5. Branch financial statements

for overseas entities only

Under the FMC Act, all overseas incorporated companies with a New Zealand business must prepare branch financial statements. Currently only entities that need to register as an overseas company under our Companies Act must prepare branch statements, so the new law has a broader impact.

For this class no change in policy is proposed. If you have substantive business in New Zealand you will still have to prepare, audit and register branch financial statements. Inland Revenue uses these statements to assess the tax liability.

However, we will consider an exemption to allow you to use an overseas GAAP or an overseas regulated auditor if the same exemptions are available to your entity as a whole.

6. Local entities and overseas GAAPs

for local entities only

Currently we can't exempt New Zealand incorporated entities from complying with NZ GAAP, but under the FMC Act we can consider an exemption if it is consistent with the purposes of the Act.

We haven't identified any situations an exemption would be appropriate. New Zealand incorporated entities should generally comply with our law and standards, rather than those of another jurisdiction.

Individual applications for exemptions will be considered on their merit. You will need to demonstrate that:

- An exemption is necessary or desirable to promote the purposes of the FMC Act
 - Your business activities and circumstances mean it is necessary or desirable to be subject to the financial reporting requirements of another jurisdiction so you can carry out your business in an appropriate and compliant way
 - The financial reporting requirements of that jurisdiction can't be met by the use of NZ GAAP financial statements (and you can't get an exemption or waiver in that jurisdiction)
 - The exemption would be consistent with the policy on exemptions for overseas entities.
-

7. Recipients of money from conduit issuers **for local and overseas entities**

In the past a small number of issuers that are recipients of money from conduit issuers have been exempted from all or part of their financial reporting obligations.

Our policy has generally been that you may be exempted if all the information that would be in the financial statements, and important to investors, is publically available from another source. For example if you are the sole or main subsidiary of an issuer, and your financial position and performance can be ascertained from your parent's financial statement. Or if you are an intermediate party, and the credit risk lies with another entity.

At this stage, we don't propose any change in policy and will continue to assess individual applications on their merit. We don't consider a class exemption appropriate because conduit issuer arrangements and the circumstances that make an exemption appropriate tend to be unique.

Re-designating a recipient as having lower public accountability is a possible option instead of, or as well as, granting an exemption.

8. Conduit issuers **for local and overseas entities**

In the past it has not been possible to grant an exemption from reporting requirements to conduit issuers, but under the FMC Act this will be possible and we would consider granting exemptions on similar grounds to the recipients. However, it is likely that issuers' financial statements will contain information that is important to investors and not available from another public source. We will consider applications on their individual merit.

Re-designating a conduit issuer as having lower public accountability is a possible option instead of, or as well as, granting an exemption.

9. Partial and technical exemptions **for local and overseas entities**

We may consider exemptions to financial reporting requirements if there are:

- Technical difficulties complying with the requirements
- Difficulties with specific aspects of the requirements.

In the past an exemption has only been available to overseas entities, but under the FMC Act we can consider exemptions for both local and overseas entities. Applications are rare and usually arise from specific circumstances, so we propose to consider any applications on their individual merit.

If it will resolve the specific issue, we may consider re-designating an entity as having lower public accountability instead of, or as well as, granting an exemption.

10. Exemptions to extending filing deadlines for local and overseas entities

Our powers of exemption will allow us to consider applications to extend the deadline for filing financial statements. However there will be a very high threshold and we expect exemptions to be rare.

Filing deadlines will be shorter under the FMC Act. For this class we will consider individual applications for exemptions. But you'll need to have a compelling reason why you can't comply with the four month period, or specific circumstances that make it inappropriate.

While overseas entities may have longer timeframes to prepare financial statements under overseas law, we don't consider this sufficient reason on its own to grant exemptions.

Exemptions won't be available just because you haven't made arrangements in time to comply with the timeframes in the FMC Act.

The next step

How do I make a submission?

Please use the form on the next page – this gives the details of what you need to do. Forms must be submitted electronically in both PDF and word formats and emailed to consultation@fma.govt.nz – please put ‘Feedback financial reporting’ in the subject line.

Alternatively, you can make an online submission on our engagement site www.talktous.fma.govt.nz. You need to register to be able to use the site.

Submissions close on 28 February 2014.

Where can I get more information?

You’ll find more about the new financial reporting requirements in the Act on our website www.fma.govt.nz.

If you have questions about the consultation process, please get in touch.

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Feedback: Financial reporting – regulatory policy for financial reporting designations and exemptions

Please submit this feedback form electronically in both PDF and MS Word formats and email it to us at consultation@fma.govt.nz with 'Feedback financial reporting' in the subject line. Thank you. **Submissions close on 28 February 2014.**

Date: _____ Number of pages: _____
 Name of submitter: _____
 Company or entity: _____
 Organisation type: _____
 Contact name (if different): _____
 Contact email and Phone: _____

Part#	Section#	Paragraph#	Comment	Recommendation
<i>You don't need to quote from the consultation document if you use part & paragraph numbers. You may attach extra pages - please label each page with your name & organisation.</i>				

Feedback Summary – if you wish to highlight anything in particular

Please note: Feedback received is subject to the Official Information Act 1982. We may make submissions available on our website, compile a summary of submissions, or draw attention to individual submissions in internal or external reports. If you want us to withhold any commercially sensitive or proprietary information in your submission, please clearly state this and note the specific section. We will consider your request in line with our obligations under the Official Information Act.