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Changes to corporate annual reporting on the cards

Jon Moses and Victoria Wise outline proposed changes to corporate reporting, and the distribution of annual reports in Australia and by New Zealand property companies

On 16 November 2006 the Parliamentary Secretary for the Australian Commonwealth Treasurer released a Proposals Paper entitled Corporate and Financial Services Regulation Review. Of interest in regards to corporate reporting is Chapter 2, which outlines a package of proposals aimed at streamlining and simplifying corporate reporting obligations. The proposals, once finalised, are to be introduced to the Australian Parliament in a Bill during 2007.

Matters dealt with in Chapter 2 include:
• eliminating disclosure duplication in relation to executive remuneration
• increasing the thresholds for reporting relating to large proprietary companies
• reducing the compliance burden for notification of the cessation of office-holders
• streamlining the notification of company address requirements
• removing the need to notify details of the top 20 shareholders
• simplifying the process for the voluntary deregistration of a company
• allowing upfront payment of annual fees for extended periods
• allowing the distribution of annual reports via Internet websites.

We deal briefly with each of these matters below.

Executive remuneration

Reporting of executive remuneration is regulated by requirements in both the Australian accounting standards (AASB 124 Related Party Disclosures) and the Corporations Act 2001. It is proposed that the disclosure requirements be removed from the accounting standards and incorporated into Corporations Act 2001. When done, this would mean that all requirements in regard to executive remuneration would be contained exclusively in the Corporations Act 2001. Additionally, companies would be required to prepare a remuneration report.

A new disclosure requirement is also proposed in relation to the hedging of executives’ options. It is proposed that companies disclose the board’s policy on executives and directors entering into contracts to hedge their exposure to options or shares granted as part of their remuneration package.

The inclusion of components such as shares and options in an executives’ remuneration package, theoretically, provides an incentive for executives to align their work-related efforts to the company’s wealth maximisation objectives. This may be a reasonable assumption if executives carry the risk burden attaching to share-based compensation instruments such as share options. However, if executives are able to hedge these instruments they effectively remove the risk of their holdings in their employer’s equities. Buffini (2006) reports some recent views relating to this practice.

“If you have at-risk remuneration without risk, you defeat the whole purpose of aligning executive and shareholders’ interests.” (Mather R, BT Governance Advisory Service 2006)

“… hedging unvested incentives should be barred and hedging vested incentives should be disclosed… where executives are held out to have a similar interest to shareholders because they have large shareholding or options, and if they have… hedged out the risk, … that is a misleading statement.” (Balzer F, Australian Shareholders Association)

“They are supposed to be at risk, so that (hedging) shouldn’t be allowed … but once exercised they are the property of the individual, and so long as they disclose what they’ve done, they’re free to dispose of them.” (Evans R, Australian Institute of Company Directors)

Clearly, the proposal to disclose hedging arrangements relating to shares and options is aimed at improving the corporate governance of these particular components of executive remuneration.

Reporting thresholds

The Australian threshold for reporting by companies has not been amended since 1995. In New Zealand the Financial Reporting Standards Board has conducted a more recent review of the
size criteria for entities which qualify for differential reporting concessions. An entity qualifies for differential reporting if the entity does not have public accountability as defined in the Framework for Differential Reporting and if there is:

(i) no separation between the owners and the governing body of the entity at balance date, or
(ii) the entity is not large in terms of the size criteria.

Since 1 January 2005, in New Zealand, an entity is considered large if it meets any two of the following conditions:

• total income exceeds $20 million
• total assets exceed $10 million
• has 50 employees.

For reporting purposes in Australia, it is proposed that a proprietary company be considered economically significant, and thus required to prepare and lodge an audited financial report, if:

• consolidated gross operating revenue for the financial year of the company and its controlled entities is $25 million or more
• consolidated gross assets at the end of the financial year of the company and its controlled entities is $12.5 million or more.

These proposals should go some way towards alleviating the reporting burden that results from having a low reporting threshold.

Change in office-holders

Currently, an Australian company is required to notify the Australian Securities and Investments Commission (ASIC) when there is a change in its list of office-holders. A person who has ceased to be an office-holder may voluntarily notify ASIC that they no longer hold office. The Proposals Paper contains a recommendation to remove this duplication of effort. Although a relatively minor proposal, if passed, it will reduce the regulatory compliance burden on companies.

Company addresses

The proposals relating to the notification of company office details to ASIC are also aimed at reducing the regulatory burden. A single streamlined reporting process will be introduced for the reporting of a company’s address to allow the updating of its contact address, registered office address and its principal place of business.

Top 20 members

Each year private and public companies are required to notify ASIC of their top 20 members. This information provides a snapshot of the members at a particular point in time. It is argued in the Proposals Paper that this snapshot may change rapidly, particularly in respect to public companies, and so is of limited value in terms of public information. Thus it is proposed to remove this reporting requirement entirely.

If this proposal (2.5) is included in the Bill and passed into legislation in 2007, users interested in knowing and understanding the ownership structure of a company will need to seek such information elsewhere. Accessibility to ownership details may become problematic, for instance, if share registries are reluctant to, or precluded from, divulging these details.

Voluntary de-registration

The process for voluntary de-registration of a company may be prevented if annual fees fall due within the two-month period between the company’s de-registration application approval and actual de-registration. This is an unnecessary burden for a company that is in the process of voluntary de-registration and the Proposals Paper aims to remove it. This will ease the regulatory cost burden for companies.

Upfront payment of annual fees

Australian companies are required to pay review fees annually to ASIC. The fees are $1,000 for a public company, $212 for a proprietary company and $40 for a special purpose company. The Paper contains a proposal to give companies the option of making upfront payments covering extended periods to prevent the “nuisance” of paying these fees annually.

Electronic distribution of annual reports

It is recommended (proposal 2.8) that amendments be introduced to allow companies to make annual reports available on their websites (as a default option) and send hard copies only to those members who request them. The proposal applies also to concise
INTERNATIONAL

Many companies have already taken advantage of the Internet to provide corporate and other information to a far wider audience than their current shareholder base.

We gathered the Internet addresses of companies in the New Zealand property sector and checked to see if these companies were providing their annual reports and other corporate reports via their websites (refer Table 1).

We found that all companies in this sector are already providing annual reports, interim financial reports and an archive of both reports on their websites. Clearly New Zealand companies, going by the property sector, are well-equipped to cope with a regulatory change similar to that proposed in Australia.

References


Table 1: NZ property companies

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<td>Calan Health Care Properties</td>
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<td>ING Property Trust</td>
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<td>Millennium Hotels</td>
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<td>National Property Trust</td>
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<td>Trans Tasman Properties Ltd</td>
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