Portrait of Luca Pacioli, attributed to Jacopo de' Barbari, 1495. Pacioli is recognized as the father of accounting and bookkeeping. He was the first person to publish a work on double-entry bookkeeping.

Submission

Review of the NZX Corporate Governance Best Practice Code

October 2016

About the McGuinness Institute

The McGuinness Institute was founded in 2004. The McGuinness Institute is a non-partisan think tank working towards a sustainable future for New Zealand. *Project 2058* is the Institute's flagship project focusing on New Zealand's long-term future. As a result of our observation that in policy-making, foresight drives strategy, strategy requires reporting, and reporting shapes foresight, we developed three interlinking policy projects: *Foresight*NZ, *Strategy*NZ and *Reporting*NZ. Each of these tools must align if we want New Zealand to develop durable, robust and forward-looking public policy. The policy projects frame and feed into our research projects, which address a range of significant issues facing New Zealand. In preparing this submission, the Institute drew largely on the *Reporting*NZ project.

About the Chief Executive

Wendy McGuinness wrote the report *Implementation of Accrual Accounting in Government Departments* for the Treasury in 1988. She founded McGuinness & Associates, a consultancy firm providing services to the public sector during the transition from cash to accrual accounting from 1988 to 1990. Between 1990 and 2003, she continued part-time while having children. Over that time she undertook risk management work for the public good. In 2002, she was a member of the New Zealand Institute of Chartered Accountants (NZICA) Taskforce that published the *Report of the Taskforce on Sustainable Development Reporting*. From 2003–2004 she was Chair of the NZICA Sustainable Development Reporting Committee. In 2004 Wendy established the McGuinness Institute in order to contribute to a more integrated discussion on New Zealand's long-term future. In 2009 she became a Fellow Chartered Accountant (FCA). In July 2010 Wendy attended an integrated reporting workshop at the Harvard Business School in Boston, Massachusetts where she interviewed both the author of *One Report*, Professor Robert G. Eccles, and the CEO of the IIRC, Paul Druckman, for the Institute's YouTube Channel. In 2011 the Institute undertook a survey of the Deloitte Top 200 companies, the resulting report is titled: *Integrated Annual Report Survey of New Zealand's Top 200 Companies: Exploring Responses from Chief Financial Officers on Emerging reporting Issues.*

Contact details:

Wendy McGuinness,
Chief Executive
McGuinness Institute
Level 2, 5 Cable Street
PO Box 24-222, Wellington 6142
+64 4 499 8888
wmcg@mcguinnessinstitute.org
www.mcguinnessinstitute.org

Overview

Thank you for the opportunity to comment on the *NZX Corporate Governance Best Practice Code* (the *Code*). The McGuinness Institute's focus is on the purpose of the *Code* and how it aligns with the purpose of the NZX and public reporting requirements more generally. In this submission we explore the extent to which the NZX is fit for purpose, looking particularly at the next fifteen years to 2030. Given our understanding of the purpose of the NZX, we then make recommendations about the draft *Code*. We close by making a number of specific recommendations in the second part of this submission (see page 11).

1.0 Exploring the purpose of NZX and the Code

What is the purpose of the Stock Exchange? In David Grant's 1997 book *Bulls, Bears and Elephants: A History of the New Zealand Stock Exchange*, he states that a stock exchange has two primary functions:

> Firstly it acts as a financial intermediary in the mobilisation of capital for business enterprises in either the public or private sectors; the former included government and local bodies raising money to fund and underwrite a myriad of national and local ventures.
>
> Secondly, the Exchange acts as a facilitator, enabling individuals and institutions to buy and sell company shares and debentures and government securities in order to influence the company's directions, to help it raise capital, and as an investment option to increase the buyer's personal assets, which can readily be transformed into cash.[1]

Clearly determining the purpose of the exchange is critical for understanding what the *Code* is trying to achieve.

New Zealand Exchange Limited (NZX) is a publicly-held New Zealand company. NZX's markets are operated under a self-regulating organisation (SRO) model. This means that NZX is both an operator and regulator of markets. The NZX states that, under its regulatory model:

> It undertakes various commercial activities, including:
>
> - operating securities and derivatives markets (including the NZX Main Board, NZX Debt Market, NZX Alternative Market, NXT Market, and NZX Derivatives markets, together NZX's markets)
> - operating Clear Grain Exchange, an electronic grain trading platform in Australia
> - publishing news and data relating to the agriculture sectors in New Zealand and Australia
> - providing passive funds management products
> - being the market operator for New Zealand's wholesale electricity market, and Fonterra Shareholders' Market.[2]

The NZX website goes on to state that:

> As an SRO, NZX has two key regulatory functions in respect of the operation of NZX's markets:
>
> 1. Market rules and policies: NZX is responsible for developing and enhancing the market rules, practices and policies under which NZX's markets operate. This function is undertaken by the NZX Policy team.

---

1 David Grant. *Bulls, Bears and Elephants: A History of the New Zealand Stock Exchange* (Wellington: Victoria University Press, 1997), pp. 11-12.

2 NZX (n.d.). *NZX Regulatory Model.* Retrieved 19 October 2016, www.nzx.com/regulation/regulatory-model

2. Regulating market conduct: NZX is responsible for monitoring and enforcing the rules under which NZX's markets operate. This applies directly to issuers, market participants and indirectly (through market participants) to investors. This function is undertaken by the NZX Regulation team, with support from the NZX Market Services team.

Specifically concerning its obligations under the Financial Markets Conduct Act 2013 (FMCA), the NZX website states that:

> NZX is required to have adequate arrangements for operating its markets, including arrangements:
>
> - to ensure that the markets NZX operates are fair, orderly and transparent
> - for monitoring the conduct of participants
> - for enforcing compliance with NZX's market rules
> - for handling conflicts between the commercial interests of NZX
> - to ensure that NZX has a sufficiently independent adjudicative body to adjudicate on contraventions of market rules that are referred to it and
> - have sufficient resources (including financial, technological, and human resources) to operate licensed markets.[3]

We believe the purpose of NZX needs to be expanded. Our concern is that, currently, its purpose is too narrow and operation-focused. It does not discuss why the NZX exists or for whose benefit. The current focus appears to be solely on the shareholder or the potential shareholder, with no recognition of the NZX as a body which can act in the interests of the public. This narrow purpose is, in our view, driving the narrow set of principles proposed in the draft *Code*.

We believe that privatization of the stock exchange is appropriate, provided that the purpose of the exchange includes a public purpose. NZX currently does not say that it has a role as an institution operating in the public interest. For example, it does not discuss its responsibilities to be a good employer (i.e. to staff and their families), to be a good neighbour (including to those living in close proximity) or to those companies using and polluting public assets (e.g. water and air). We consider quality reporting in the public domain to be a key purpose of the accounting profession. Further, we believe that an informed society is a democratic society and a democratic society is a progressive society. Appendix 1 provides an image of the recent Brexit vote, illustrating the need for information to be shared and accessible by all.

We therefore suggest adding an overarching purpose to David Grant's aforementioned two primary functions, and the two regulatory functions of NZX (quoted above). Supporting discussion is included below.

Recommendation 1: Add an overarching purpose

The overarching purpose of the NZX is to provide long-term value for its stakeholders (the New Zealand public). It will do this by reporting in a fair, balanced and understandable manner,[4] taking into consideration all four capitals (economic, natural, social and human),[5] and working towards creating a durable, trustworthy and fair place of business for investors and potential investors.

---

3 NZX (n.d.). *Securities Markets in New Zealand*. Retrieved 19 October 2016, from www.nzx.com/regulation/securities-markets

4 FRC (January 2016). *Developments in Corporate Governance and Stewardship 2015*, p. 9. Retrieved 19 October 2016, from www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Developments-in-Corporate-Governance-and-Stewa-(1).pdf

5 New Zealand Treasury, (June 2015). *Higher Living Standards*. Retrieved 27 October 2016 from www.treasury.govt.nz/abouttreasury/higherlivingstandards

Discussion

Firstly, in August 2016, Financial Markets Authority (FMA) published a report, *A Review of Corporate Governance Disclosure in New Zealand*. The report reviews disclosure of selected companies, but not their actual behaviours. The report measures whether companies have disclosed information as recommended in the FMA handbook *Corporate Governance in New Zealand: Principles and Guidelines*. The report noted that 'of the nine principles outlined in our handbook, stakeholder interests had the lowest reporting (19%), followed by reporting on remuneration (37%).'[6] The stakeholder interests means that 'the board should respect the interests of stakeholders, taking into account the entity's ownership type and its fundamental purpose.'[7] The handbook then goes on to stipulate that:

- The board should have clear policies for the entity's relationships with significant stakeholders, bearing in mind distinctions between public, private and Crown ownership.
- The board should regularly assess compliance with these policies to ensure that conduct towards stakeholders complies with the code of ethics and the law and is within broadly accepted social, environmental, and ethical norms— generally subject to the interests of shareholders.
- Public sector entities should report at least annually to inform the public of their activities and performance, including on how they have served the interests of their stakeholders.[8]

Secondly, we are more connected than ever before. What happens in the financial market drives public-good outcomes across the country. The Institute has recently undertaken a *TacklingPovertyNZ* tour, visiting Queenstown, Manawatu, Rotorua, Gisborne and the Far North.[9] What we discovered on this tour was that how 'big businesses' operate has significant impact on local regions. But this is not a New Zealand phenomenon. For example, a recent International Federation of Accountants (IFAC) workshop in London noted:

> Ongoing economic hardship in many parts of the world, including the long-term effects of actions taken to stabilize the financial system immediately following the crisis, has emphasized the divide between the "haves" and the "have nots."
>
> This, combined with the public's observation that the people whose behaviors caused the crisis have not been held accountable, has resulted in considerable political unrest including moves toward what seem like more extreme political narratives and choices across the developed world.[10]

---

6 Financial Markets Authority (2016). *A Review of Corporate Governance Disclosure in New Zealand*, p. 5. Retrieved 19 October 2016, from www.fma.govt.nz/assets/Reports/_versions/8974/160804-Review-of-corporate-goverance-disclosure.1.pdf

7 Financial Markets Authority (2014). *Corporate Governance in New Zealand: Principles and Guidelines*, p. 2. Retrieved 19 October 2016, from www.fma.govt.nz/assets/Reports/141201-FMA-Corporate-Governance-Handbook-Principles-and-Guidelines2014.pdf

8 Financial Markets Authority (2014). *Corporate Governance in New Zealand: Principles and Guidelines*, p. 38. Retrieved 19 October 2016, from www.fma.govt.nz/assets/Reports/141201-FMA-Corporate-Governance-Handbook-Principles-and-Guidelines2014.pdf

9 See www.tacklingpovertynz.org for more information.

10 International Federation of Accountants (September 2016). *From Crisis to Confidence: Good Regulation, Governance, and Culture*, p. 6. Retrieved 19 October 2016, from www.ifac.org/publications-resources/crisis-confidence-good-regulation-governance-and-culture

Further, recent developments in the United Kingdom call for reporting that is 'fair, balanced and understandable'.[11] The Financial Reporting Council (FRC) is responsible for promoting high quality corporate governance and reporting to foster investment. They set the UK Corporate Governance and Stewardship Codes as well as UK standards for accounting, auditing and actuarial work. They operate independent disciplinary arrangements for accountants and actuaries, and oversee the regulatory activities of the accountancy and actuarial professional bodies. A recent report, *Developments in Corporate Governance and Stewardship 2015* notes:

> The 2012 update to the Code asked boards to confirm that the company's annual report and accounts taken as a whole are **fair, balanced and understandable** (FBU), a primary outcome of which is for the narrative sections of the annual report to reflect more accurately the company's position, performance and prospects.
>
> The Grant Thornton review of all FTSE 350 annual reports found that all companies bar two (2014: 25) now include such a statement. While 'two thirds still give little or no insight into how they substantiate the claim, there are a few, slightly up from last year, that have embraced the intent of the Code to supply information about the various criteria used to support their statement'.[12] (emphasis added)

The report goes on to note that:

> The changes to the Code in 2014 were designed to strengthen the focus of companies and investors on the **longer term and sustainable value creation**. Measures were taken to improve the quality of information investors receive about the long-term health, strategy and risk management of listed companies.[13] (emphasis added)

There is a general acceptance globally that financial reporting practice needs to improve. One of the most interesting articles we have read this year, 'Where Financial Reporting Still Falls Short', in the July-August 2016 *Harvard Business Review*, identified five key problems:

1. Universal Standards (' … the implications of failing to reconcile GAAP and IFRS).
2. Revenue Recognition (' … a perverse system in which accounting rules influence the way business is done, rather than report on companies' performance').
3. Unofficial Earning Measures ('… caution in interpreting unofficial earning measures and should look closely at corporate explanations that might depend on the use (or abuse) of managerial judgement').
4. Fair Value Accounting ('… since not everyone agrees on what "fair value" means, the measure has injected enormous subjectivity into the financial reporting process').
5. Cooking the Decisions, Not the Books ('… corporate decision making that serves the interest of short-term reporting but undermines long-term performance').[14]

11 FRC (January 2016). *Developments in Corporate Governance and Stewardship 2015*, p. 9. Retrieved 19 October 2016, from www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Developments-in-Corporate-Governance-and-Stewa-(1).pdf

12 FRC (January 2016). *Developments in Corporate Governance and Stewardship 2015*, p. 9. Retrieved 19 October 2016, from www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Developments-in-Corporate-Governance-and-Stewa-(1).pdf

13 FRC (January 2016). *Developments in Corporate Governance and Stewardship 2015*, p. 10. Retrieved 19 October 2016, from www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Developments-in-Corporate-Governance-and-Stewa-(1).pdf

14 H. D. Sherman, and S. D. Young (July–August 2016). 'Where Financial Reporting Still Falls Short.' *Harvard Business Review*, pp. 78-82.

The Institute has recently reviewed the financial accounts of New Zealand King Salmon Investments Limited (NZKS), and produced the working paper *New Zealand King Salmon: A financial perspective – A case study exploring the financial information of a for-profit, foreign-owned company using publicly owned resources.* This working paper is still in draft, but can be found on our website.[15] The paper was prepared before it was known that the company was intending to list itself on the NZSX. However, the paper is relevant in terms of shaping our recommendations as it illustrates a number of gaps in financial reporting and failures in our institutional reporting infrastructure.

Lastly, there has also being growing concern over whether the current SRO model is fit for purpose. We consider there is a need to develop checks and balances to minimize the weaknesses of the SRO model. A 2013 opinion piece from *The Guardian*, 'Six reasons why our stock markets are no longer fit for purpose', outlines the factors that have cumulatively made equity capital markets no longer suitable:

1. The privatisation of stock exchanges, **destroying their public purpose mandate** and instead making the growth of trading volume their single-minded goal and high-frequency traders (computers programmed to trade) their preferred customers.
2. The unrestrained technology arms race in computing power combined with the adoption of technology-driven information flow spurring the rapid acceleration of trading volume, which at critical times can be highly destabilising.
3. The misguided ascent of 'shareholder wealth maximization' (at the expense of all other stakeholder interests) in our business schools, board rooms, and the corporate finance departments on Wall Street.
4. The well-intended but equally misguided practice of using stock-based incentives, and stock options in particular, as the dominant form of senior management compensation, which incentivizes them to focus only on short-term results at the expense of the long-term health of the enterprise, people and planet.
5. The misalignment of interests between short-term focused intermediaries and real investors such as pension funds whose timeframe should be measured in decades.
6. Regulators' lack of courage and confidence to counter the trader-driven paradigm and institute substantive structural reform such as a Financial Transactions Tax and other reforms that would penalise excessive speculation while incentivising long-term productive investment.[16] (emphasis added)

Looking closer to home, however, the New Zealand Government has significantly improved the quality of its reporting. The first example of this is the latest *Financial Statements of the Government of New Zealand* (published October 2016); this is an extraordinary result and provides clear and concise reporting on New Zealand's financial position. Secondly, government departments are reporting on their strategic intentions (strategy reporting) as illustrated in the picture of the Ministry of Social Development 2014-2015 annual report (Figure 1). Compared with these examples, the *NZX Corporate Governance Best Practice Code* is being left behind.

15 See *New Zealand King Salmon: A financial perspective – A case study exploring the financial information of a for-profit, foreign-owned company using publicly owned resources*, available at www.mcguinnessinstitute.org/working-papers

16 John Fullerton and Tim MacDonald (October 21, 2013). 'Six reasons why our stock markets are no longer fit for purpose.' *The Guardian.* Retrieved 19 October 2016, from www.theguardian.com/sustainable-business/stock-markets-no-longer-fit-purpose

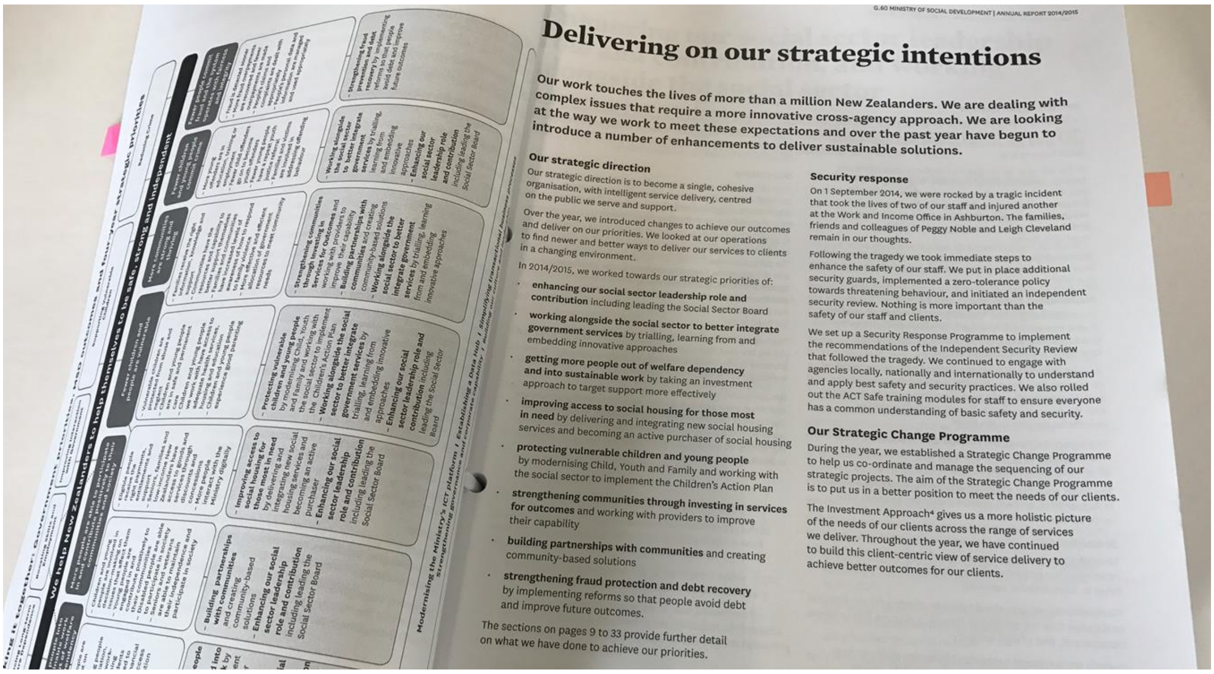


Figure 1: Exemplary strategic reporting in the Ministry of Social Development 2014-2015 annual report.

We have included in Appendix 2 some work we have been doing in terms of the content of strategy documents. We have also been looking at alignment and whether these strategy documents are included in the annual report. This is shown by Element 6 in Figure 2 below.[17] We have been undertaking the *Government Department Strategies (GDS) Index* for the last three years, and have noted that over this time there has been a gradual increase of alignment. This is something the Institute would like to see in the documents produced by companies listed on the NZSX.

17 For more information on the GDS Index, please go to www.gdsindexnz.org

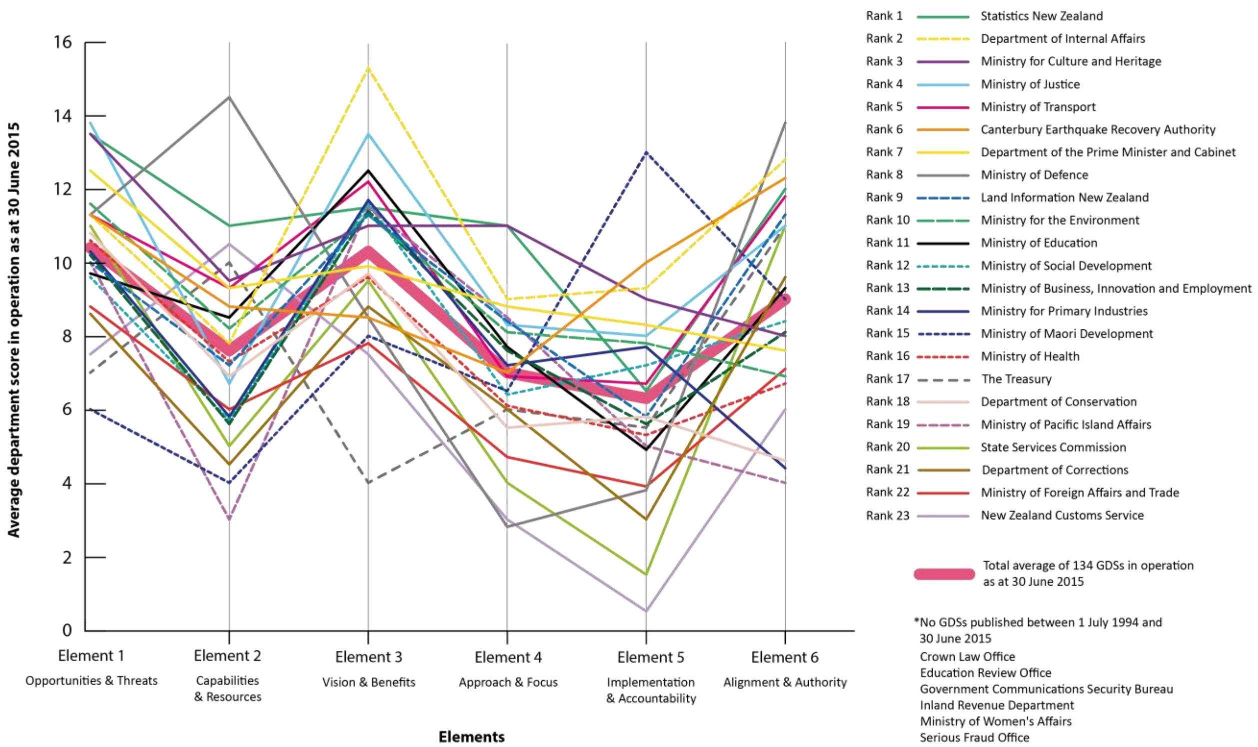


Figure 2: GDS results by element, for each department in operation as at 30 June 2015[18]

In 2011, the Institute undertook a survey of the Deloitte Top 200 companies, the resulting report is titled: *Integrated Annual Report Survey of New Zealand's Top 200 Companies: Exploring Responses from Chief Financial Officers on Emerging reporting Issues*. We will be repeating this work next year. This work is important for New Zealand because the NZSX lists many of New Zealand's largest companies, including 27.5% of the Deloitte Top 200 companies (2015) when compared with the latest NZSX All Securities as at 14 October 2016.[19, 20]

The following graphs highlight the significant role the *Code* could have in shaping good business practice, an opportunity that should not be missed.

18 Madeleine Foreman and Wendy McGuinness (April 2015) *Think Piece 21: Strategy Stewardship Matters: Utilising the Government Department Strategies Index*. Wellington: McGuinness Institute.

19 Deloitte (2015). *The Deloitte Top 200: 2015 Top 200 Rankings*. Retrieved 19 October 2016, from www.top200.co.nz/wp-content/uploads/2015-deloitte-top-200-rankings.pdf

20 NZX Limited (n.d.). *NZX Main Board (NZSX) All Securities*. Retrieved 19 October 2016, from www.nzx.com/markets/NZSX/securities

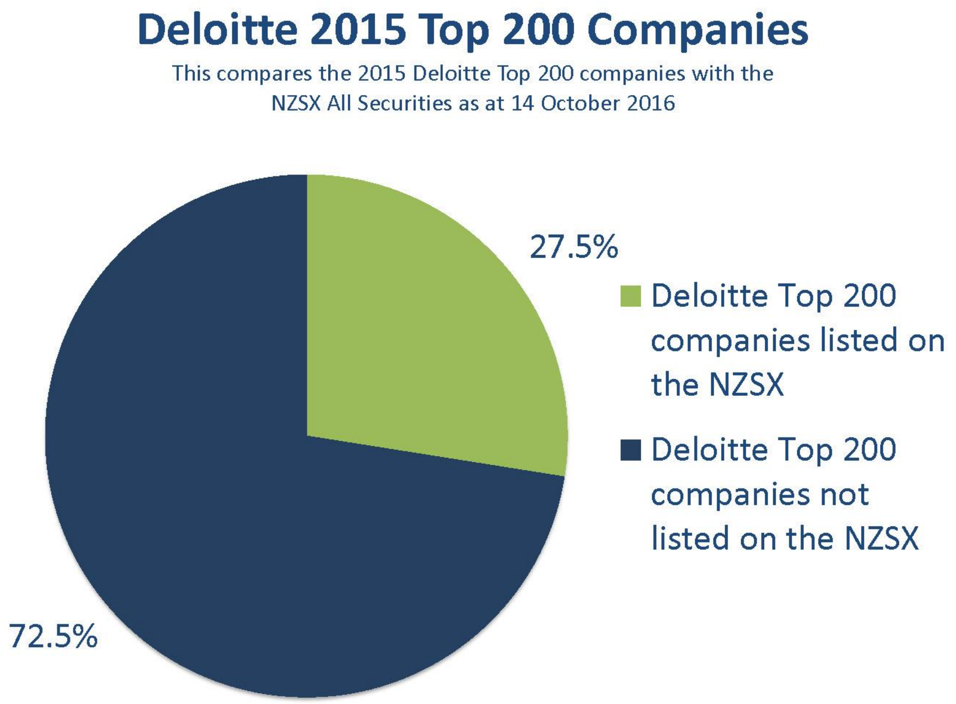


Figure 3: Deloitte 2015 Top 200 Companies compared with the NZSX All Securities

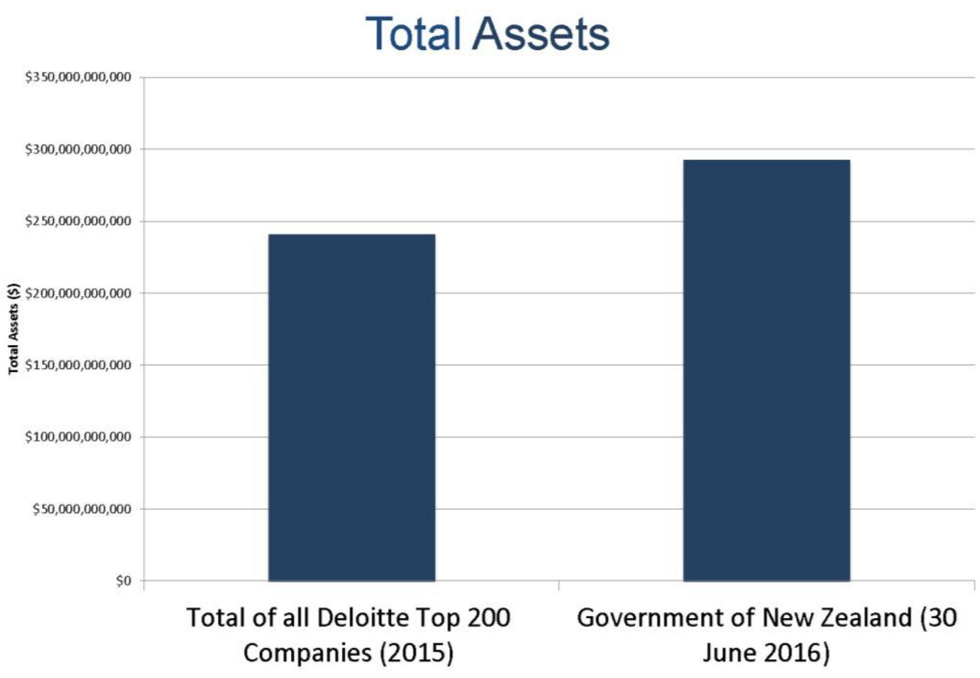


Figure 4: Total Assets of all Deloitte Top 200 Companies (2015) and Government of New Zealand

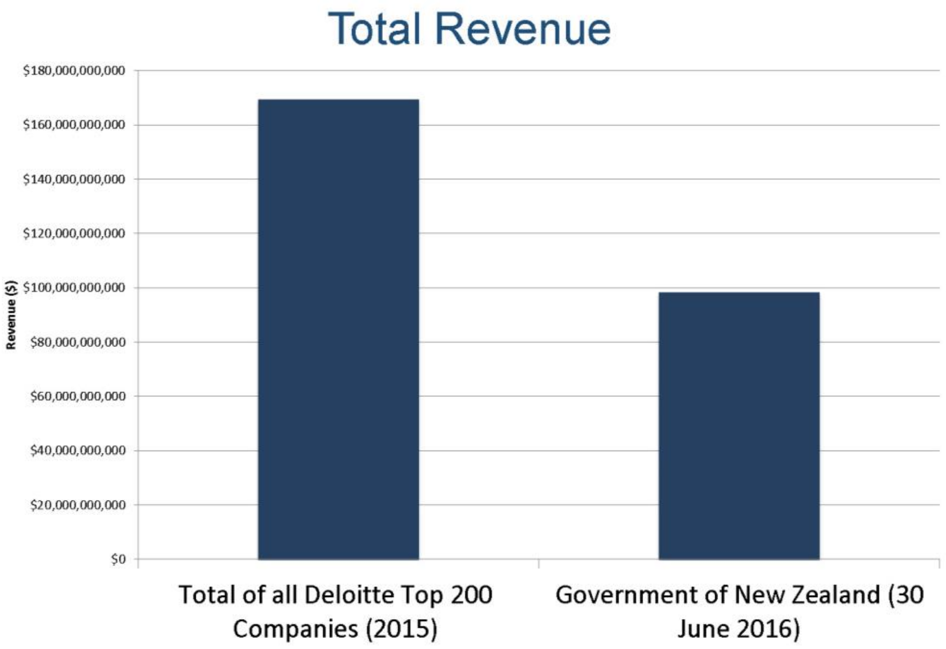


Figure 5: Total Revenue of all Deloitte Top 200 Companies (2015) and Government of New Zealand

There are a number of international frameworks being progressed around the world and in New Zealand to improve reporting practices. The Institute is a proponent for integrated or extended reporting, including more frequent use of the term capitals and reporting on how the performance of a company changes in terms of these capitals.

In our view the Global Reporting Initiative (GRI) is outdated and new models are likely to arise. We personally subscribe to the Framework advocated by the International Integrated Reporting Council (IIRC).[21] Appendix 3 contains an infographic we produced for the CPA conference held in Auckland on 18 October 2016. Please note the framework uses six capitals according to the Integrated Reporting International Framework: financial capital, manufactured capital, intellectual capital, human capital, social and relationship capital and natural capital.[22] We prefer the four capitals in Treasury's *Living Standards Framework*: economic, natural, social and human capital, as they are less complex.[23]

As NZX are proposing something that will last for 10 to 15 years, we suggest NZX use more up-to-date frameworks or at least also include recent models in the list of options. We also suggest thinking more broadly about the changing landscape and tensions that might shape behaviour going forward. Examples include the changing nature and complexity of financial instruments, the complexity of ownership structures both locally and internationally, cybercrime, emerging banking relationships, and the challenges of policing rules and legislation (ensuring they are fit for purpose and do not create unintended consequences).

---

21 See www.integratedreporting.org/resource/international-ir-framework for more information on the IIRC framework.

22 International Integrated Reporting Council (December 2013). *The International <IR> Framework*, pp 11-12. Retrieved 25 October 2016, from www.integratedreporting.org/wp-content/uploads/2013/12/13-12-08-THE-INTERNATIONAL-IR-FRAMEWORK-2-1.pdf

23 New Zealand Treasury, (June 2015). *Higher Living Standards*. Retrieved 27 October 2016 from www.treasury.govt.nz/abouttreasury/higherlivingstandards

2.0 Recommended Changes to the Draft Code

Given Recommendation 1 (repeated below), our suggestions to improve the *Code* would include:

Recommendation 1: Add an overarching purpose
We suggest the overarching purpose of the NZSX is to provide long-term value for its stakeholders (the New Zealand public). It will do this by reporting in a fair, balanced and understandable manner, taking into consideration all four capitals (economic, natural, social and human),[27] and working towards creating a durable, trustworthy and fair place of business for investors and potential investors.

Recommendation 2: Add a new Principle: 'Public Rights to Information'
This principle would include reporting for the public good, ensuring reports are easily accessible by the public, that historical documents are archived and that value is preserved for current and future generations. NZX may like to align the role of record keeping with the Public Records Act 2005. This should include an understanding of the wider stakeholders' interest in information about the performance of a company. Key examples include staff, neighbours and councils. The Principle should also discuss the role of capitals with examples (e.g. the IIRC's six capitals or Treasury's *Living Standards Framework* four capitals). There needs to be an obligation placed on companies to seek out what information the stakeholders (as distinct from shareholders) want to know about the operations of the company.

Recommendation 3: Change Principle 1: Ethical Standards to 'Code of Ethical Behaviour'
This principle should require Issuers to develop and adopt a code of ethical behaviour that is published on the Companies Office website for everyone to access (including staff). The *Code* should make this mandatory and specify actual practices that must be included, but allow the Issuer concerned to add to it. It should also require their code of ethical behaviour to be reviewed by the Board annually. Issuers' websites change frequently and only the latest version is likely to be publicly available; hence, we recommend that their code of ethical behaviour should be uploaded onto the Companies Office website as a matter of historical record. We also consider Principle 1 clause (e) … as required by law, should become clause 1.1 (a), or be removed completely as it is a given. We also consider 1.2 should form part of Principle 5. Remunerations. (see discussion below). You may also like to direct readers or add directly a reference to the Companies Act 1993. Furthermore, any breach of the Issuers code should be reported on the Companies Office website. The Companies Office should be a one-stop shop for the shareholders and the broader public.

Recommendation 4: Add to Principle 2: Board composition and performance
Add the terms gender and cultural diversity to the opening text '… experience, *gender balance, cultural diversity* and perspectives', otherwise their importance is easily lost when mentioned in the subtext. Diverse teams make for innovative thinking; it was great to see NZX working and thinking in this space. We were also not sure if the role of the independent board member needed more context and expansion under Principle 2 to direct readers to the current legislation.

---

27 We prefer the four capitals in Treasury's *Living Standards Framework*. New Zealand Treasury, (June 2015). *Higher Living Standards*. Retrieved October 27, 2016 from www.treasury.govt.nz/abouttreasury/higherlivingstandards

Recommendation 5: Remove Principle 3: Board Committees
We consider this operational in nature, hence it is up to the Board to determine.

Recommendation 6: Keep Principle 4: Reporting and disclosure
We suggest Principle 4 remains but a new Principle is added. Alternatively, the suggested new Principle on future focused-reporting below could be included into Principle 4. Our view is that they are better separated. We would also prefer to see Principle 4 adopt the terminology used by the Financial Reporting Council (FRC) in their latest report, *Developments in Corporate Governance and Stewardship* 2015, 'Fair, balanced and understandable (FBU)'.[28] We would also like the 'ultimate holding company' to be disclosed in the annual report and the Companies Office register. Financial instruments are becoming much more complex and shareholders and stakeholders alike need to know who they are relying upon. We see more clarity over who owns which company as being critical for shaping legislation and public policy going forward.

Recommendation 7: Add a new Principle: Future-focused reporting
This principle would require reporting on strategic intentions: looking forward. NZX could suggest entities develop the most appropriate method of future-focused reporting for them, but also highlight the number of good frameworks and models in existence.

Recommendation 8: Change Principle 5: Remuneration to 'Directors and Staff'
We would like to see health and safety also included in here; remuneration is a narrow term when it comes to some of the incidents occurring in our big industries (e.g. forestry). We also consider directors and staff should be brought together under one principle due to the complex relationships and remuneration packages that are emerging. For example, we suggest Principle 1 clause 1.2 should be included in this Principle.

Recommendation 9: Add to Principle 6: Risk Management
Principle 6 needs to require the Issuer to report on risk in its annual report. NZX could instill risk management into the proposed new principle of Recommendation 7 above. Risk is only one aspect of future-focused reporting (others include emerging trends and opportunities). NZX could also direct readers to good international frameworks.

Recommendation 10: Change Principle 7: Auditors to 'Independent Verification of External reports and Documentation'
There are not just auditors that have an important role in verifying the information contained in the annual report and other documentation. We consider the obligation should be on any person or entity verifying data and information. This is particularly relevant given the move towards infographics and social media. NZX also might like to draw a distinction between verification and an opinion.

Recommendation 11: Change Principle 8: Shareholder Rights and Relations to 'Shareholders Rights to Information'
This is to align with the proposed new principle 'Public Rights to Information' (Recommendation 2 above). NZX may find better terminology.

---

28 FRC (January 2016). *Developments in Corporate Governance and Stewardship 2015*, p. 9. Retrieved 19 October 2016, from www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Developments-in-Corporate-Governance-and-Stewa-(1).pdf

Recommendation 12: Add a new Principle: Fraud and CyberCrime
Trust is going to be key going forward and it is arguably timely to think of embedding a principle on fraud and cybercrime. This is particularly relevant considering recent hacks in the United States. We tend to be only a few years behind the United States in such areas. We suggest that all crime is reported and more significant crime is reported in the annual report; for example, any fraud above $100,000 and any successful cybercrime attacks that deal with private information and/or deal with blackmail. These should also be reported on the Companies Office register.

Recommendation 13: Align with other standard-setters and regulators
Make sure the *Code* fits within the wider reporting framework, both in New Zealand and with our major trading partners, using the same language and ethics as other standard setters.

Recommendation 14: Consider the role of outing bad behaviour and penalties
Large companies are more concerned about reputation than penalties; although the latter can directly contribute to the policing costs. We suggest NZX need to think harder about what happens if the *Code* is not applied or adopted. We would like to see a record of 'bad behaviour' on the register at the Companies Office. It was unclear what resources the NZX would put in place to understand how the *Code* will be actioned (or policed).

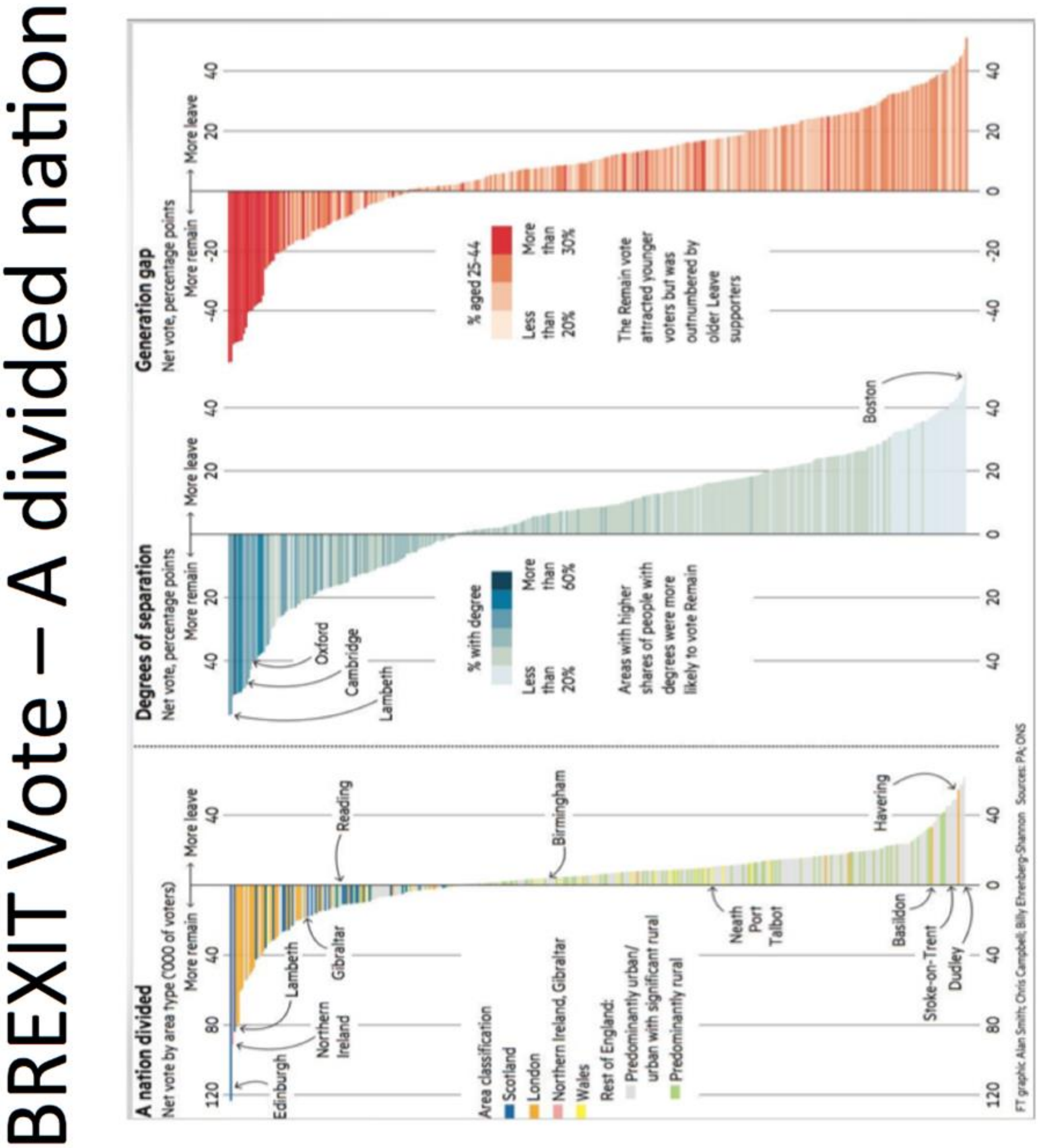
Recommendation 15: Review date embedded in the Code
We suggest a review date is installed in the *Code*. For example, '*a review is undertaken of the Code*' in 2021 or earlier.

We close by adding a list of recommendations we produced for the Chartered Professional Accountants (CPA) Congress in Auckland on 18 October 2016 for your further consideration:

1. Require all NZSX companies and government departments to publish extended financial reports by 2020; providing information on foresight, strategy and changes in all capitals (economic, natural, social and human).
2. Expand the Companies Office role to make it responsible for registering the annual reports of all New Zealand organisations (and become a one-stop shop for the public).
3. Require all government departments to publish a list of their strategy documents in their annual reports and for a register to be made available to the public of all government department strategy documents.
4. Require all significant health and safety incidents to be published both in the annual report and in the Companies Office register.
5. Require all significant environmental incidents and subsequent penalties to be published in both the annual report and the register at the Companies Office.
6. Require organisations that use and pollute significant public resources to report on that use and pollution and explain in their annual report how those impacts were and will be managed going forward.
7. Require the Companies Office to clearly record the 'ultimate holding company' in the register and specify the stock exchange board/s the company is listed on – this could happen when the company uploads its annual report.
8. Require the Companies Office to specify a searchable format for all documents (so that the public can search a company's records).

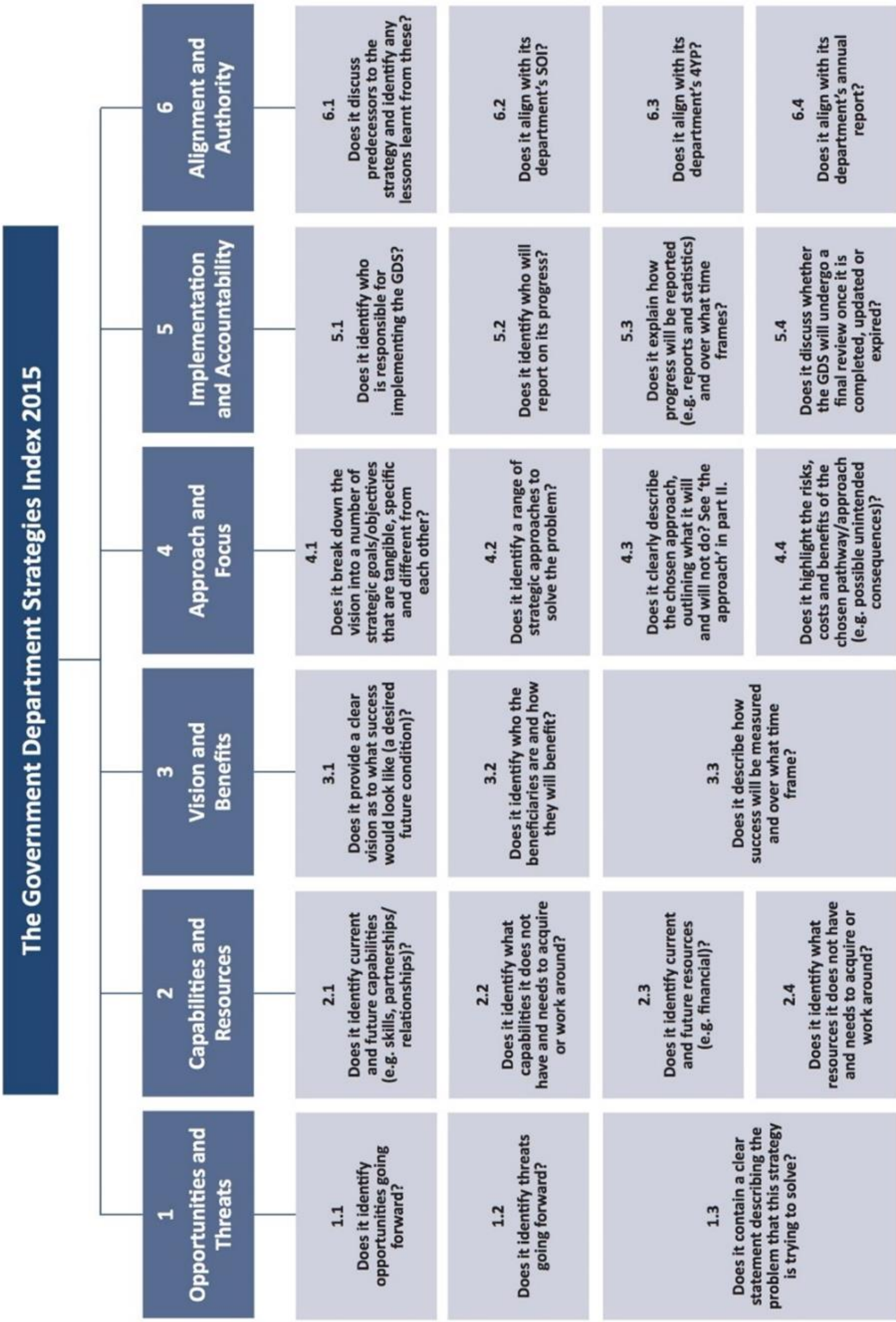
Thank you for reading our submission. If you have any questions, please do not hesitate to contact us.

Appendix 1: Infographics on Brexit (2016)[29]



29 FT graphic Alan Smith; Chris Campbell; Bill Ehrenberg-Shannon Sources: PA; ONS

Appendix 2: Government Department Strategy Index Scorecard (2015)



Appendix 3: Extended Reporting Card (October 2016)

HOW TO EXTEND YOUR ANNUAL REPORT

SIX CAPITALS →	ASK QUESTIONS →	BE GUIDED BY THE PRINCIPLES →	SEEK OUT THE RIGHT CONTENT →	REPORT ON NET VALUE ADDED TO THE SIX CAPITALS
Financial Capital	1. What time frame?	1. Strategic focus and future orientation	1. Organisational overview and external environment	Financial Capital
+				+
Manufactured Capital	2. What stakeholders?	2. Connectivity of information	2. Governance	Manufactured Capital
+				+
Intellectual Capital	3. What reporting boundaries?	3. Stakeholder relationships	3. Business model	Intellectual Capital
+				+
Human Capital	4. What business model?	4. Materiality	4. Risks and opportunities	Human Capital
+				+
Social and Relationship Capital	5. What reporting format?	5. Conciseness	5. Strategy and resource allocation	Social and Relationship Capital
+				+
Natural Capital	6. What buy-in do we have from the governing body?	6. Reliability and completeness	6. Performance	Natural Capital
=			7. Outlook	=
VALUE	7. What can we improve?	7. Consistency and comparability	8. Basis of presentation	VALUE

7 GUIDING PRINCIPLES

Strategic focus and future orientation
An integrated report should provide insight into the organisation's strategy, and how it relates to the organisation's ability to create value in the short, medium and long term, and to its use of and effects on the capitals.

Connectivity of information
An integrated report should show a holistic picture of the combination, interrelatedness and dependencies between the factors that affect the organisation's ability to create value over time.

Stakeholder relationships
An integrated report should provide insight into the nature and quality of the organisation's relationships with its key stakeholders, including how and to what extent the organisation understands, takes into account and responds to their legitimate needs and interests.

Materiality
An integrated report should disclose information about matters that substantively affect the organisation's ability to create value over the short, medium and long term.

Conciseness
An integrated report should be concise.

Reliability and completeness
An integrated report should include all material matters, both positive and negative, in a balanced way and without material error.

Consistency and comparability
The information in an integrated report should be presented: (a) on a basis that is consistent over time; and (b) in a way that enables comparison with other organisations to the extent it is material to the organisation's own ability to create value over time.

8 CONTENT ELEMENTS

Organisational overview and external environment
What does the organisation do and what are the circumstances under which it operates?

Governance
How does the organisation's governance structure support its ability to create value in the short, medium and long term?

Business model
What is the organisation's business model?

Risks and opportunities
What are the specific risks and opportunities that affect the organisation's ability to create value over the short, medium and long term, and how is the organisation dealing with them?

Strategy and resource allocation
Where does the organisation want to go and how does it intend to get there?

Performance
To what extent has the organisation achieved its strategic objectives for the period and what are its outcomes in terms of effects on the capitals?

Outlook
What challenges and uncertainties is the organisation likely to encounter in pursuing its strategy, and what are the potential implications for its business model and future performance?

Basis of presentation
How does the organisation determine what matters to include in the integrated report and how are such matters quantified or evaluated?

Adapted from: *The International Integrated Reporting Framework*
Learn more at www.integratedreporting.org

Published by: Grant Thornton An instinct for growth
XRB External Reporting Board Te Kāwai Ārahi Pūrongo Mōwaho
McGuinness Institute

6 GLOSSARY

Business model
An organisation's system of transforming inputs through its business activities into outputs and outcomes that aims to fulfil the organisation's strategic purposes and create value over the short, medium and long term.

Capitals
Stocks of value on which all organisations depend for their success as inputs to their business model, and which are increased, decreased or transformed through the organisation's business activities and outputs. The capitals are categorised in this Framework as financial, manufactured, intellectual, human, social and relationship, and natural.

Content Elements
The categories of information required to be included in an integrated report; the Content Elements, which are fundamentally linked to each other and are not mutually exclusive, are stated in the form of questions to be answered in a way that makes the relationships between them apparent.

Guiding Principles
The principles that underpin the preparation and presentation of an integrated report, informing the content of the report and how information is presented.

Integrated report
A concise communication about how an organisation's strategy, governance, performance and prospects, in the context of its external environment, lead to the creation of value in the short, medium and long term.

Reporting boundary
The boundary within which matters are considered relevant for inclusion in an organisation's integrated report.