

# New Zealand

## Corporate Governance Institutions, Practices and Developments

### 1. Key Institutional Features of Corporate Governance and Company Profile in New Zealand

#### 1.1 Background

The basis for New Zealand's corporate governance system is set out in the following laws:

***Companies Act 1993:*** this Act describes the basic requirements for incorporating, organising, and operating companies. It defines the relationships between companies, directors and shareholders, sets out the duties of directors and provides for the protection of shareholders and creditors against the misuse of management powers. It provides procedures for realising and distributing the assets of insolvent companies. It also outlines the powers and duties of the Registrar of Companies (ROC), which include registering and inspecting documents.

***Securities Act 1978:*** this Act establishes the Securities Commission, defines its powers and functions, regulates the offer of securities to the public for subscription and confers on ROC the responsibility of registering prospectuses and associated documents for the offer of securities to the public. The term security is widely defined and covers equities, debt securities including bank and finance company deposits as well as corporate and other bonds, interests in partnerships and syndicates, interests in unit trusts, life insurance policies with an investment component, and interests in superannuation schemes.

***Securities Markets Act 1988:*** this Act regulates various activities on securities markets including insider trading and market manipulation. It provides a statutory framework for continuous disclosure by public issuers, substantial security holder disclosure, disclosure of dealings by directors and officers of public issuers, registration of stock exchanges, and dealings in futures contracts including the authorisation of futures exchanges. It confers on the Securities Commission the power to regulate in these areas.

The Securities Commission issued a set of corporate governance principles and guidelines in 2004 following a public consultation process that showed significant support for a principles-based approach to corporate governance. The principles cover: ethical standards, board composition and performance, board committees, reporting and disclosure, remuneration, risk management, auditors, shareholder relations and stakeholder interests.

New Zealand Exchange Limited, NZX, the only regulated securities exchange, demutualized in late 2002, and self-listed in 2003. The NZX listing rules set corporate governance standards for issuers listed on the exchange. The listing rules include corporate governance standards such as requirements for appointment of directors, remuneration of directors, transactions with related parties and major transactions. One third of directors must be independent directors and every issuer must have an audit committee which must have a majority of members that are independent directors.

## 1.2 Trends

Year	2005	2006	2007	2008	2009
Number of listed companies	153	151	152	147	143
Domestic market capitalisation (US\$ million)	40,592.5	44,816.5	47,485.6	24,209.6	35,306.8

Domestic market capitalisation peaked in May 2007, and fell to a low of US\$20 billion in February 2009. Stock prices and capitalisation have improved since. The number of listed companies, previously stable, declined slightly over the past two years.

### 1.3 Key Corporate Governance Rules and Practices

See Key Corporate Governance Rules and Practices in New Zealand, p. 167.

## 2. Development, Enforcement and Assessment of Implementation of Corporate Governance Rules

### 2.1 Development of Corporate Governance Rules

The Ministry of Economic Development has the role of advising the government on corporate governance policy and implementing changes to corporate governance laws and regulations.

The Securities Commission has a role in encouraging good corporate governance. At the request of the Minister of Commerce, the Commission developed and issued a set of corporate governance principles in 2004. The Commission was assisted by other work done in New Zealand, in particular by New Zealand Exchange Limited, the Institute of Directors in New Zealand, and the Institute of Chartered Accountants of New Zealand. The commission reviews a sample of issuers' annual reports and assesses them against the principles. The commission's review aims to assess the current level and quality of disclosure and provide useful feedback to the market.

NZX develops its listing rules. Any new rules or changes to existing rules are submitted to the Minister of Commerce, who can disallow the proposed rule or change where it is in the public interest to do so.

### 2.2 Enforcement of Corporate Governance Rules

The National Enforcement Unit (NEU) of the Ministry of Economic Development is responsible for ensuring that New Zealand's financial and commercial institutions are effectively monitored and that business regulations are enforced. The NEU investigates and, where appropriate, prosecutes offences under various legislation on behalf of the ROC. The NEU also assesses and determines whether candidates should be prohibited from being directors of a company under section 385 of the Companies Act 1993.

In 2009, six companies were delisted from the NZX, and in 2008, seven companies were delisted. It is not known how many of these were for failure to comply with corporate governance rules. NZX referred 13 matters relating to compliance with insider trading, substantial security holder, and continuous disclosure provisions to the Securities Commission in 2009.

In 2008-09 the Securities Commission filed civil and criminal proceedings against directors of two companies in receivership, alleging that directors misled investors by making untrue statements in their companies' offer documents.

### **2.3 Assessment of Corporate Governance Practices**

New Zealand has not been subject to a ROSC assessment with respect to observance of the OECD Principles of Corporate Governance.

## **3. Awareness and Advocacy for Good Corporate Governance**

### **3.1 Company Directors**

The Institute of Directors in New Zealand (Inc.) promotes excellence in corporate governance, represents directors' interests and facilitates their professional development through education and training. It is a membership organisation of around 4,700 individuals representing the spectrum of New Zealand enterprise, from the public and private sectors. The Institute offers a range of courses in corporate governance for company directors.

### **3.2 Media**

There are often articles in the financial press which comment on corporate governance issues. Examples of recent topics are:

- The performance of directors in the collapse of a number of finance companies;
- Directors' workloads—are they taking on too many directorships and hence not devoting enough time and effort to each;
- Representation of women on boards; and
- Whether a lack of ethics by directors is a contributing factor to investors' reluctance to invest in capital markets.

### **3.3 Educational System**

Tertiary education courses in business and law include corporate governance topics.

Corporate governance courses are available in programs for MBA and other advanced business degrees.

## **4. Corporate Governance of State-Owned and Family-Controlled Enterprises**

### **4.1 State-Owned Enterprises**

The Crown Ownership Monitoring Unit (COMU) within the Treasury monitors the state's investments in companies.

COMU:

- Provides strategic ownership advice to the New Zealand government on the commercial assets it owns and monitors the performance of those assets;
- Assists with the appointment of directors to Crown company boards;
- Advises shareholding Ministers on performance and governance issues; and

- Works with other monitoring departments and agencies to share good practice and lift performance.

COMU monitors the following entities:

- 17 state-owned enterprises;
- Eight Crown research institutes;
- Four Crown financial institutions;
- Air New Zealand Limited;
- Five other Crown companies;
- Some statutory entities; and
- The Crown's shareholding in a shipping line and four airports.

The establishing Acts for the companies owned by the Crown set out some additional requirements. For example, the State-Owned Enterprises Act 1986 requires each SOE to annually submit a Statement of Corporate Intent (SCI), which in part sets out the objectives of the SOE, and the nature and scope of its activities. SOEs are required to make all decisions in accordance with their SCI.

The Crown expects all SOEs to act in accordance with best practice corporate governance principles, including, for example, the observation of high ethical standards and the effective management of any conflicts of interest. The principal objective of every SOE, as per its establishing Act, is to operate as a successful business and to this end, to be as profitable and efficient as comparable businesses that are not owned by the Crown.

The OECD undertook a survey of OECD economies and the results were favourable for NZ and its ownership model. The survey considered all aspects of the guidelines including the ownership function, relationship of SOEs with shareholders, transparency and governance.

## **4.2 Family-Controlled Enterprises**

The majority of large New Zealand-controlled firms are listed on the stock exchange. Many private companies, including family-owned businesses, lack good governance structures (such as external board members). Governance and compliance costs are likely to be factors deterring them from becoming listed companies.

# **5. The Role of Professional Service Providers in Corporate Governance**

## **Accounting and auditing firms**

The directors of the company are responsible for preparing financial statements which give a true and fair view of the financial position of the company, the results of its operations and cash flows for the accounting period. The financial statements must be prepared in accordance with International Financial Reporting Standards (IFRS).

Auditors are required to express an independent opinion on the financial statements stating whether:

- Proper accounting records have been kept;
- The financial statements:

- comply with IFRS;
- comply with New Zealand generally accepted accounting practice; and
- give a true and fair view.

### **Professional bodies**

Professional bodies such as the New Zealand Institute of Chartered Accountants and the New Zealand Law Society, and industry bodies, such as the New Zealand Institute of Directors and the Listed Companies Association are important stakeholder organizations in consultation during the corporate governance policy development process.

## **6. Recent Developments in Corporate Governance**

### **6.1 Corporate Governance Developments**

*Reform of the minority buy-out provisions of the Companies Act 1993:* A Bill was enacted in 2008 aimed at clarifying and improving the efficiency of provisions requiring companies to buy-back the shares of minority shareholders in the event of a transaction that fundamentally changes the nature of the company or its business.

*Enactment of the Limited Partnerships Act 2008:* On 2 May 2008 the Limited Partnerships Act 2008 came into force. This Act provides for the establishment of the new legal form of limited partnership, whose key features include flow-through tax status; limited liability for investing partners and separate legal personality. The primary objective of the introduction of the Limited Partnerships regime is to facilitate sustainable growth in New Zealand's venture capital and private equity industries.

### **6.2 Enforcement of Corporate Governance Rules**

A number of company directors are being taken to Court by the Registrar for breaches of the Companies Act, following from the collapse of around 30 finance companies in New Zealand over the last three years. One person has been convicted for the provision of misleading information in a prospectus and filing reports containing false information in the 2009-10 year. Other cases are still before the courts.

In 2010 the Securities Commission has initiated two separate cases of civil and criminal proceedings under the Securities Act against finance company directors for making false statements in offer documents. Similar proceedings were filed in 2008 against directors of two companies. The Commission has also filed civil proceedings in 2010 against a company and its directors for a breach of continuous disclosure obligations.

The New Zealand Markets Disciplinary Tribunal, which is an independent body responsible for hearing and determining matters referred to it in relation to the conduct of parties regulated by the NZX Participant Rules and NZX Listing Rules, in 2009 considered four cases concerning breach of periodic reporting requirements, noting that this was a significant increase in number from previous years.

### **6.3 Current Issues and Challenges for Corporate Governance**

#### **6.3.1 Challenges**

The collapse of finance companies referred to above has led to media comment on the role of prominent people (such as former politicians) taking up directorships on companies that have

subsequently failed. Investors in these companies have suffered significant losses and have questioned the qualifications and judgment of such directors.

### **6.3.2 Priorities for Reform**

A major concern for the government has been to rebuild the trust of investors in capital markets, and to develop New Zealand's capital markets to allow for business growth while ensuring that investors get proper levels of protection.

The New Zealand government has begun the process of establishing a new regulator for New Zealand's financial markets, to be called the Financial Markets Authority (FMA). The FMA will take over all the work of the Securities Commission. It will enforce securities, financial reporting, and company law as they apply to financial services and securities markets. It will also regulate and oversee, trustees, auditors, financial advisers and financial service providers, including people who offer investments. Legislation establishing the FMA will be passed in 2010 year, and it will be operating early in 2011.

A further priority is to complete the Review of the Financial Reporting Framework. The review aims to achieve a framework that is appropriate for all types of entities and is enduring. The government has made a decision to consolidate all accounting and auditing standards setting responsibilities within a new government standard setting agency. Further issues being considered are whether to remove preparation requirements for small and medium companies, and how to rationalise the reporting requirements in the non-profit sector. Legislation to implement the review is intended to be introduced into Parliament in 2011.

Following the collapse of a significant number of corporations internationally, many governments concluded that self-regulation of the audit profession was no longer appropriate and introduced government regulation, independent oversight or a combination of the two. New Zealand currently relies on self-regulation, but in light of the risk that New Zealand auditors are de-recognised overseas, decisions have been taken to strengthen auditor regulation. Audit standards will be set by a government regulator, and there will be government oversight of the licensing of auditors. The reforms are due to be implemented in 2011.

### **6.3.3 Financial Crisis**

The move to a consolidated financial sector regulator for capital markets draws on the lessons from the financial crisis and aims to restore investor confidence in financial markets.

In addition a review being led by the Ministry of Economic Development aims to ensure that securities regulation keeps up with changes in the financial environment. A key part of the review will be to take into account lessons from the international credit crisis and to stay closely linked into international regulatory developments. The review encompasses the application of securities legislation, the form and content of required disclosure, supervisory and regulatory controls, and compliance with international principles.

## Key Corporate Governance Rules and Practices in New Zealand

Element	Yes	No	Source(s) of Rule	Comments
<b>RIGHTS OF SHAREHOLDERS</b>				
1. Do shareholders add items to the agenda for shareholders' meetings?	X		CL	
2. Do shareholders ask questions of directors at shareholders' meetings and do they receive answers?	X		GP	
3. Must company transactions with its insiders be on a non-preferential basis?	X		CL	Companies may avoid a transaction in which a director is interested unless the company has received fair value for it.
4. Is a super majority vote required for major company acts affecting shareholder rights?	X		CL	75% majority required.
<b>COMPOSITION AND ROLE OF BOARDS OF DIRECTORS</b>				
5. Must boards have independent directors? What percentage?	X		SLR	One third of directors (rounded down to the nearest whole number) must be independent.
6. Do independent directors have significant influence over (a) internal and external audit and (b) executive compensation?	X		CGC, SLR	This is contained in the principles issued by the Securities Commission.
7. Do independent directors decide what information the board receives from management?		X		
8. Are the chairman of the board and chief executive officer different persons in the majority of listed companies?	X		GP	
9. Are all board members elected annually?		X		
10. Does the board oversee enforcement of a company code of conduct?		X	CGC	This is contained in the principles issued by the Securities Commission.
<b>TRANSPARENCY AND DISCLOSURE OF INFORMATION</b>				
11. Do financial statements comply with IFRS International Financial Reporting Standards (IFRS)?	X		Financial reporting law	The Accounting Standards Review Board requires issuers to comply with IFRS.
12. Are the identities of the five largest shareholders disclosed?	X		CL	
13. Is compensation of company executive officers disclosed?	X		CL	The number of employees in brackets of \$10,000 receiving remuneration above a threshold of \$100,000 per annum must be disclosed.
14. Are extraordinary corporate events disclosed?	X		CL	Major transactions must be disclosed to shareholders and approved by special resolution, i.e. 75% majority.
15. Are risk factors disclosed in securities offering materials?	X		SL	
16. Are transactions of a company with its insiders disclosed?	X		CL	Directors must disclose their interest in any transaction with the company.

Note: CL – company law; SL – securities law; CGC – corporate governance code; SLR – stock exchange listing requirement, GP – general practice but not obligatory