



# Are financial reports meeting user needs?

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**INFORMATION AND ASSURANCE NEEDS OF USERS  
OF TIER 2 FOR-PROFIT ENTITY FINANCIAL REPORTS**

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RESEARCH SUMMARY // DECEMBER 2017



**EXTERNAL REPORTING BOARD**  
*Te Kāwai Ārahi Pūrongo Mōwaho*

# Introduction

## THE EXTERNAL REPORTING BOARD (XRB)

### The External Reporting Board (XRB) is responsible for financial reporting strategy and for accounting and auditing & assurance standard setting in New Zealand.

Our aim is to help engender trust and confidence in New Zealand organisations' external reporting, to assist them to compete internationally and to enhance their accountability to stakeholders.

As part of our role in helping to ensure New Zealand is a reputable market, trusted by investors and other stakeholders, we have commissioned research into the usefulness of the financial reports produced by Tier 2 for-profit entities. This research follows our 2016 report which investigated the usefulness of the financial reports produced by for-profit entities operating in New Zealand's domestic capital markets (Tier 1 for-profit entities).

Go to [xrb.govt.nz/information-hub](http://xrb.govt.nz/information-hub) to read the full research reports.

### What is a Tier 2 entity?

A large for-profit entity which is required to prepare general purpose financial reports (GPFR) and which does not have public accountability.

(Large = revenue over \$30 million or assets over \$60 million)

(An entity with public accountability is a Tier 1 entity)

We estimate there are currently more than 2,000 Tier 2 for-profit entities in New Zealand\*

\* Determining the number of businesses in this group is difficult as there is no central depository for Tier 2 entities' financial statements. The law also allows some to opt in or out of reporting. Our estimates are calculated from data from Statistics New Zealand, the Financial Markets Authority, the Companies Office and the Office of the Auditor-General.

### THE AIM OF THE RESEARCH IS TO



#### Determine

the number of Tier 2 for-profit entities in New Zealand



#### Understand

the common information and assurance needs of users of financial reports produced by large New Zealand for-profit entities

### WHO ARE THE USERS OF THESE FINANCIAL REPORTS AND WHAT ARE THEIR KEY INTERESTS?



#### Shareholders

(owners/managers)

For equity investment, to monitor management, to monitor governance



#### Lenders

(e.g. banks)

For lending purposes, to monitor management



#### Advisors

(e.g. accountants/consultants)

To monitor management and governance



#### Regulators

(e.g. tax authorities)

To monitor regulatory compliance, including compliance with tax legislation

# Research implications

## FINANCIAL REPORTING SHOULD CONTINUE TO EVOLVE

Financial reports are a well-used and trusted source of information. However, they should continue to evolve. Suggested improvements from the users of Tier 2 reports include:

### Simplify

abc

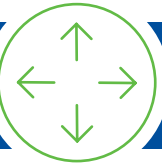
Reduce the length and complexity of financial statements, particularly disclosures such as financial instruments and hedging

### Improve



- Improve disclosures on financial risk management to be more specific to the business
- Clarify narratives on related party transactions and contingent liabilities
- Detailed segmental reporting

### Expand



- Provide further narratives on:
- Financial performance and position (and provide summary financial information)
  - Business strategies and future prospects

Overall the findings of this research are consistent with our earlier research into the usefulness of the financial reports produced by for-profit entities (Tier 1) operating in New Zealand domestic capital markets. Both groups of users find financial statements useful and they trust them. However, both groups also want to see financial reports continue to evolve and improve, and where possible to be shorter and simpler.

# Importance of the research for the XRB

This is the first comprehensive study into the needs of users of Tier 2 for-profit entity financial reports in New Zealand.

1

The research will be used to drive discussion and debate around Tier 2 accounting requirements in New Zealand.

2

This research will help inform the amendments to the Reduced Disclosure Regime requirements for Tier 2 for-profit entities which the XRB is currently working on, in conjunction with the Australian Accounting Standards Board.

3

This research will also inform our post implementation review of the Accounting Standards Framework (and Tier Structure), which will take place in 2019-2020.

We look forward to hearing more from users of financial reports. If you have a view, please get in touch.

# Key findings – Tier 2 for-profit reporting

## FINANCIAL REPORTS ARE WELL USED

**60%**

use financial reports

Users are predominately **shareholders** (77% use financial reports) and **regulators** (100% use financial reports)



**40%**

do not use financial reports

Particularly **lenders** who can request special purpose reports, and **advisors** who have access to greater management information

## CORPORATE FINANCIAL STATEMENTS ARE THE MOST VALUABLE SOURCE OF INFORMATION



### Corporate financial statements

rated by all user groups as the most valuable source of information, with the exception of lenders



### Management commentary and analysis

rated the most valuable by lenders and the second most valuable source of information by all other user groups

### Valued additional information



Narratives that explain the entity's performance and financial position



Information on business strategies and prospects for future financial years

## ALL FINANCIAL STATEMENTS ARE VALUED

### Most useful

Statement of financial position  
Statement of profit or loss

### Least useful

Statement of changes in equity

For many, the Notes to the financial statements are found to be too complex and lengthy, and many people do not use them.

## THE MAJORITY OF USERS DO NOT REQUIRE MORE INFORMATION

**62%** of users do not require additional information

### HOWEVER



**Regulators** would value more detail on related party transactions



**Shareholders** would value more information on company strategy and enhanced segment reporting



**Lenders** would value details of loan repayments and a clearer discussion on contingent liabilities

# Assurance

## WHAT ARE THE DIFFERENT FORMS OF ASSURANCE?

### ASSURANCE

All respondents understood the different forms of the engagements.

### NON-ASSURANCE

#### Audit



An audit engagement is where an independent auditor provides an opinion as to whether the financial statements are prepared in accordance with an applicable financial reporting framework.

#### Review



A review engagement is less thorough and detailed than an audit. The reviewer provides a conclusion as to whether anything has come to their attention to indicate that the financial statements have not been prepared in all material respects, in accordance with an applicable financial reporting framework.

#### Agreed-upon procedures



Agreed-upon procedures are **non-assurance engagements** that provide factual findings on very specific and mutually agreed matters and procedures.

## THERE IS DEMAND FOR VOLUNTARY AUDITS

Much of the demand arises from conflicts between owners and creditors.

51%

of financial statements used by respondents **are** independently audited or reviewed



7%

of users indicate the entities they have an interest in do not prepare financial statements

31%

of financial statements used by respondents **are not** independently audited or reviewed

11%

of financial statements used by respondents are subject to an agreed-upon procedure engagement

## ALL AUDIENCES VALUE THE CREDIBILITY PROVIDED BY ASSURANCE ENGAGEMENTS



#### Shareholders:

- value checks on the adequacy of internal controls



#### Lenders:

- value warnings of going concern issues
- value protection against fraud



#### Advisors:

- value credibility of information



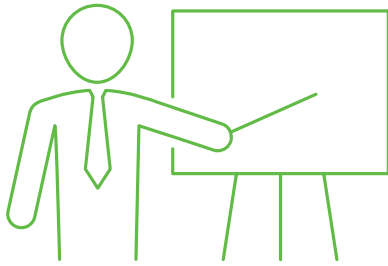
#### Regulators:

- value checks on adequacy of internal controls
- value checks on compliance with legislation and constitution

# Methodology

## RESEARCH TEAM

The research was commissioned by the XRB to better understand the needs of users of financial reports in New Zealand.



### The team at Massey University included:

- Professor Fawzi Laswad
- Dr Warwick Stent
- Dr Nives Botica Redmayne
- Dr Lei Cai
- Dr Dimu Ehalaiye

## RESEARCH METHODOLOGY

**Detailed literature review** of international research  
**Online survey of 79 respondents** and 5 in-depth interviews

## PROFILE OF RESPONDENTS



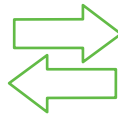
### Shareholders

**13** Responses  
**1** Interview



### Lenders

**27** Responses  
**1** Interview



### Advisors

**21** Responses  
**1** Interview



### Regulators

**7** Responses  
**2** Interviews



### Other

**11** Responses

All respondents had above average levels of knowledge, skills, and experience in reading, understanding and analysing financial statements.

Contact us at [xrb.govt.nz](http://xrb.govt.nz) or (04) 550 2030



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