A History of the Development of New Zealand Accounting Standards for Small and Medium Enterprises and the Future Prospects of IFRS for SMEs

A Dissertation submitted to the Auckland University of Technology in fulfilment of the requirements for the Degree of Master of Business

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ATTESTATION OF AUTHORSHIP

I hereby declare that this submission is my own work and that, to the best of my knowledge and belief, it contains no material previously published or written by another person (except where explicitly defined in the acknowledgement), nor material which to a substantial extent has been submitted for the award of any other degree or diploma of a university or other institution of higher learning.

Signed...

Date ……………………………………

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ABSTRACT

With attempts to standardise accounting standards applicable to reporting entities, the International Accounting Standard Board issued the International Financial Reporting Standards (IFRS) for small and medium sized enterprises (SMEs). IFRS for SMEs aims at reducing the compliance costs for smaller enterprises. This thesis examines the controversies and the reasons that the New Zealand accounting standards body may or may not adopt IFRS for SMEs by providing an account of what was occurring during the period of development, and comments on the appropriateness of its adoption in New Zealand.

Historical narrative inquiry methodology is used in this research to investigate issues related to accounting standards for SMEs using the structured framework based on Porter (1981). The thesis is based on documentary evidence found by analysing the historical development of accounting standards for SMEs. The historical narrative inquiry model developed by Colby (2008) is used to structure the research.

The historical development of accounting standards in New Zealand shows that IFRS for SMEs is what the business community is waiting for to enhance the confidence of users on SMEs' accounts. The Framework for Differential Reporting is cost burdensome for SMEs.

Since the IFRS for SMEs has not actually been adopted in New Zealand, interviews with business owners are eliminated. The appropriateness of the IFRS for SMEs within New Zealand business tiers is mainly considered.

The contribution of this thesis is that it documents the development of the accounting standards and offers understanding of the future prospects of the IFRS for SMEs in New Zealand.

Chapter One

Introduction

Chapter one starts with the background introduction of the published international financial reporting standards. There are two sets of financial reporting standards: international financial reporting standards (IFRS) and international financial reporting standards for small and medium-sized entities (IFRS for SMEs). From the background introduction, the research question is drawn. The research adopts the historical narrative inquiry methodology to conduct the research.

1.1 Background

Given a set of transactions from which accountants have to prepare financial statements, accountants in different countries or even in a same country will not produce identical financial statements (Nobes & Parker, 2008). There are several reasons for this. Accountants may follow the same set of rules, but no set of rules seems to cover every eventuality. There is also room for professional judgement. Professional judgements commonly depend on the accountants' environment or the accountants' countries. In addition, accounting rules are different between countries and even among companies. Multinational enterprises operate in more than one country and they may find it hard to produce transparent and consistent financial statements. In other words, it is hard for multinational enterprises to know what set of standards they should comply with. Investors may find it hard to make investment decisions when they cannot compare efficiently financial statements prepared by overseas companies (Nobes & Parker, 2008). Having one set of financial reporting standards would facilitate investors' understanding of financial reporting prepared across borders and make the financial statements' comparison easier. In fact, each jurisdiction has its own national sets of standards which are the most appropriate for that country's environment and no country seems to have the same set of standards as another. After a long process, which started with the issue of an exposure draft of proposed IFRS which aimed to seek comments throughout the world, the International Accounting Standards Board (IASB) has finally published a set of international financial reporting standards called IFRS. The IFRS are built on the principle-based framework and aim to overcome the rule-based approach of the existing system such as Generally Accepted Accounting Practice (GAAP) in the United States of America. In New Zealand, the Financial Reporting Act 1993 defines GAAP as the compliance with the applicable financial reporting standards and accounting policies that are appropriate to the circumstances of the reporting entity and have authoritative support within the accounting profession.

The main objective of the IASB is to establish a single set of globally accepted standards which will provide high quality, transparent, comparable and understandable information to capital market and other users (IASB, 2002). IFRS was designed for all profit-oriented entities that provide information to external users who have limited access to information for their investment decisions (Perry & Crook, 2007a). The European Union (EU) Parliament was the first regulatory body in the world to require its listed companies to prepare consolidated accounts in accordance with IFRS on or after January 2005. In New Zealand, reporting entities had the option to adopt IFRS from 1 January 2005 voluntarily and adoption became compulsory on or after 1 January 2007. IFRS is applicable to large listed companies as well as to SMEs. However, the extensive and complex requirements of IFRS may create burdens for SMEs. There has been debate about whether or not the benefits of IFRS adoption outweigh the costs for SMEs.

1.2 Debate on IFRS for SMEs

IFRS for SMEs, released in July 2009, is a set of international standards designed particularly for SMEs. IFRS for SMEs is a globally accepted set of standards aiming to serve entities with around 50 employees or less. Different countries have different definitions of SMEs and definitions of SMEs are classified into quantitative and qualitative characteristics. Quantitative characteristics of SMEs’ definition are commonly based on a number of criteria which include turnovers, total assets, and number of employees (see Table 1.1 below).

Table 1.1: Quantitative characteristics of definition of SMEs

Countries	**Number of SMEs within a country**	**Medium-sized entities**	**Small-sized entities**
European Union And United Kingdom	98% (United Nations Committee on Trade and Development, 2000)	Employees<250	Employees<50
Australia	99% (APEC, 2009)	Employees: 20-200	Employees: 5-19
New Zealand	97.1% (Ministry of Economic Development, 2009)	Employees: 6-19	Employees: 0-5

Source: Author (2010)

The implication of IFRS for SMEs in New Zealand is significant as 97.1% of business entities are SMEs (Ministry of Economic Development (MED), 2009a). According to the United Nations Committee of Trade and Development (UNCTAD), SMEs make up 98% of the business community in EU (UNCTAD, 2000) and 99% in Australia (APEC, 2009). IFRS for SMEs may only be suitable for small, not medium-sized companies in the EU. IFRS for SMEs may serve medium-sized companies well, but it may be a burden for micro-sized companies in New Zealand. Each country has its own national set of standards for SMEs and IFRS for SMEs may serve only either medium or small entities.

In the United Kingdom, there is a distinction between the two levels of SMEs: level 3 for small or micro-owner–manager and level 2 for larger ones. Each level is underpinned by a set of guidelines (UNCTAD, 2000). The definition of SMEs used in the EU as a whole and in particular the United Kingdom describes a “small” business as an enterprise with fewer than 50 employees and “medium” one as having fewer than 250 employees. In Australia, the range for small business is from five to 19 employees while a medium-sized entity is from 20 to 200 employees (MED, 2006). New Zealand has quite a broad range of SMEs (see Table 1.2 below) and the Ministry of Economic Development (MED) defines SMEs as enterprises with zero to 19 people (2009a). This shows that the relative size of New Zealand SMEs is a lot smaller than those in the United Kingdom or Australia.

Table 1.2: Number of enterprises by size (MED, 2009a, p.8)

New Zealand is predominantly a nation of small businesses.

Employee Sized Group	Number of enterprises	Percentage of all enterprises	Cumulative percentage
0	319,463	67.8%	67.8%
1-5	100,459	21.3%	89.1%
6-9	20,526	4.4%	93.5%
10-19	16,771	3.6%	97.1%
20-49	9,104	2.0%	99.0%
50-99	2,579	0.6%	99.5%
100-499	1,859	0.4%	99.9%
500+	340	0.1%	100%
Total	471,101	100%	-

Table 1.3: Qualitative characteristics of definition of SMEs (MED, 2004, p. 3)

While SMEs are diverse, typically an SME may:

- have begun spontaneously from just one idea or new product and may continue to be an incubator for innovative ideas and products
- have an owner/manager with little formal business experience or few generic business skills
- have begun because the founder/owner has a particular technical expertise
- comprise the founder/owner and up to four employees (often with an unpaid family member providing administrative support)
- have the owner as the only person in a managerial position, and no board or formal governance arrangements
- operate on trust, rather than on systems and contracts
- have a tight family-like culture where the values of the owner are strongly shared by the staff and workplace practices are flexible and suited to individual employees' needs
- focus on a small range of products or services sold mainly on the local domestic market
- have all personal assets, including the owner's home, committed as security for the business
- acknowledge the owner's time as one of its scarcest and most valuable assets
- operate flexibly, on a "reasonable person" basis, rather than on an informed and strict observance of regulations
- have a vision and outlook that is bounded by the horizons, skills and experience of the founder/owner, the pressures of day-to-day management and tight resource constraints (i.e., a tactical rather than a strategic approach)
- endeavour to operate independently of other businesses and institutions and to favour self-help over seeking advice
- not be aware of the regulations to which it is expected to adhere
- in provincial areas, be a key part of the social fabric of the community
- close within three years of its inception, not infrequently in circumstances that could easily have been prevented.

SMEs have several qualitative characteristics which are different from large companies. The Small Business Advisory listed typical characteristics of New Zealand SMEs in its

2004 Annual Reports. These qualitative features of SMEs which have 20 employees or fewer (MED, 2004, section 2, p. 3)

Quantitative characteristics are commonly used to define SMEs as stated in Table 1.1.

The New Zealand accounting standards board has not adopted the set of standards IFRS for SMEs as yet. As a result, in 2008 the Minister of Commerce announced that his department would review the financial reporting framework which sets financial reporting requirements for SMEs. According to the Accounting Standards Review Board (ASRB), the outcome of the government's financial reporting reform proposal has been a recommendation that IFRS will be applicable only to entities having public accountability, economic significance and separation of owner and manager roles (ASRB, 2009). In fact, there has also been a series of New Zealand-based studies such as BusinessNZ/KPMG, 2004: Chamber of Commerce, 2003, suggesting compliance with IFRS remains a significant constraint and cost to business (cited in Judge, 2006). Business events in SMEs are often far less complicated than those in the listed companies (see Haller, 2003 for SMEs' reservations about IFRS).

There is also an ongoing debate of the appropriateness of IFRS for SMEs relating to the content that is required. For example the Statement of Cash Flow is exempted for qualifying companies in New Zealand in accordance with the Framework for Differential Report (Whittington, 2007). This is the current standard that applies in New Zealand to some SMEs that qualify for differential reporting exemptions. The Framework for Differential Reporting also serves as a guide for standards setters in setting up differential reporting exemptions in financial reporting standards in New Zealand currently (Institute of Chartered Accountants of New Zealand (ICANZ), 1994). According to the United Nations Committee on Trade and Development, there is little evidence underpinning the necessity for preparing the statement of cash flow for small-sized enterprises (UNCTAD, 2002, para.62). However, according to the International Accounting Standards Board, SMEs are required to prepare a Statement of Cash Flow according to IFRS for SMEs (IASB, 2009b). The European Parliament found that the standards for SMEs are too complicated (Mackintosh, 2008). The New Zealand accounting body could adopt IFRS for SMEs as we have done with our existing IFRS for listed companies or they could continue with the current Framework for Differential Reporting. Given the international nature of IFRS and comparability between countries and the history and debates around this standard, the research aims to examine the development of New Zealand accounting standards for SMEs and respond to the research question of "How appropriate is it for New Zealand to adopt the IFRS for SMEs?"

It appears to be a great advantage for developing countries where setting up a comparable set of quality accounting standards may be beyond their knowledge. It is also beneficial for countries which already have national sets of accounting standards to standardise them to ensure international comparison.

1.3 Conclusion

In conclusion, in an attempt to standardise national standards globally to one set of accounting standards applicable worldwide, the IASB issued IFRS for SMEs. SMEs occupy a large proportion of the business community in many countries. Debates have taken place in many countries to discuss if IFRS for SMEs is appropriate for SMEs given there are different definitions of SMEs between countries. The majority of New Zealand businesses are SMEs. Therefore, it is essential for New Zealand to consider the appropriateness of IFRS for SMEs. This issue will drive the present research using a historical narrative inquiry methodology. The research is structured according to the historical narrative inquiry model developed by Sherri Colby (2008). Due to the nature of this methodology, each chapter is located in a chronological order; and the literature review is not contained in a separate chapter but across chapters. The theories of regulation which include the public interest theory, signalling theory, capture theory, and the agency theory are used to strengthen the discussion on whether New Zealand should regulate IFRS for SMEs if adopted. Therefore, these theories are discussed in Chapter 7 where discussion of regulation is located.

Structure of the Thesis

This introductory chapter describes the background of the research and identifies the key questions the research is aimed to address.

Chapter Two identifies and justifies the choice of methodologies adopted in this research. The purpose of this chapter is to present a review of the literature concerned with the application of the historical narrative methodology. The chapter also introduce a historical narrative inquiry model developed by Sherri Colby which is found useful to structure the research.

Chapter Three is indicated to explore the development of sector-neutral standards which includes a discussion of the structure of the profession's responsibilities and standard setting functions in New Zealand.

Chapter Four considers the impacts of the sector-neutral approach to the Conceptual Framework, impacts on setting on terminology, and impacts on setting on the timeliness of the due process.

Chapter Five is aimed to examine the development of the Framework for Differential Reporting and its application to SMEs in New Zealand.

Chapter Six describes characteristics of the IFRS for SMEs and compare with the Framework for Differential Reporting. The comparison is made to address the usefulness of the IFRS for SMEs and its appropriateness to business entities in New Zealand.

Chapter Seven draws attentions of readers to the review of the Framework for Financial Reporting which sets financial reporting obligations for businesses in New Zealand. The chapter is aimed to discuss whether SMEs should be required to prepare general purpose financial reports. Theories of regulations are used to strengthening the discussion.

Finally, recommendation and conclusion are found in Chapter Eight. This chapter also address limitations of this research.

Chapter Two

Research Methodology

2.1 Introduction

The primary purpose of this chapter is to identify and justify the choice of methodologies used to address the research question: “What was occurring during the period of the development of New Zealand accounting standards for SMEs and how appropriate is it for New Zealand to adopt IFRS for SMEs?”

Historical narrative inquiry methodology was employed for this research. This chapter presents a review of the literature concerned with the application of the historical narrative inquiry methodology in accounting. Framework of Porter (1981) and historical narrative inquiry model developed by Colby (2008) were selected to conduct this research.

The historical narrative inquiry model offers a procedural knowledge of the historical investigations. The procedural knowledge process includes the following elements: attracting the interest/ attention of the researcher in past events (contextual beginnings); stimulating in-depth thinking (in-depth questioning); developing the skills of collecting and interpreting secondary documents (secondary source analysis); forming the historical perspectives based upon evidence collected (researcher’s authorship); and argument formation and future prospect (philosophical/argumentative reflection).

“Historical narrative inquiry is a cyclical process involving inquiry, investigation, and interpretation—that is the restructuring of existing narratives and organising of a new account” (Colby, 2008, p. 65). According to Porter (1981), even though explanatory narrative process is inherently subjective, application of his model enables historians focussing on a scheme of investigation having general applicability. Porter (1981) also argues:

> The narrative account is therefore comparable to and reflective of the actual past, though it is never the same as the past. And because history is a public inquiry (rather than private, as in fiction), the account can be judged and corrected by other historians. (p. 53)

The framework of Porter (1981) offers instructions as to how materials or historical events should be selected and organised. According to Porter (1981), the historical events should be analysed and perceived within the contexts in which they occurred.

This chapter comprises four sections. This chapter firstly introduces the original model of the historical narrative inquiry developed by Dr Colby (2008). Secondly, an explanation as to why the model is modified to fit to this research and the contribution of the model to the research are provided. Thirdly, Porter's framework and some related literature are discussed. Lastly, there is a description of data used in this study.

2.2 Research Method

2.2.1 Colby's historical narrative inquiry original model

Background

Dr Sherri Colby developed the historical narrative inquiry model to assist history education. The model aims to help students to develop interest/attention to the past; procedural knowledge of doing history; skills of analysing and evaluating original historical documents; interpretative skills for historical narratives; reconstruction of historical perspectives based on evidence collected; and student-authored historical narrative and argumentative essays based on the articulation of historical perspectives (Colby, 2008).

The model includes six steps: contextual readings; inquiry; secondary document collecting; document analysis; historical rebuilding; and argument formation. The model is the fruition of her interpretation of the following concepts (Colby, 2008, p. 60):

i. Historical thinking (the nature of cognition in history)
ii. Historical empathy (the ability to perceive history from the perspectives of those in the past)
iii. Disciplined inquiry (the nature of historical investigation and the historian's craft)
iv. Historical theory (the acceptance and recognition of narrative—with its linguistic, literary, stylistic and structural influences—as the communicator of past events)

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2.2.2 Modified historical narrative inquiry model and its contribution

Background

According to Dr Colby (2008), students do not seem to think critically about historical events. Therefore, the “authentic historical documents” are used to advance the students’ interpretative skills by comparing their analysis of secondary documents with the analysis of the “authentic primary documents”. According to Colby (2008, p. 60), “the integration of primary documents into the curriculum offers resuscitative prospects for the teaching of history through authentic accounts of historical events and through the teaching of history as an intellectual process.”

Dr Colby’s model comprises steps which appears to flow logically from the beginning stage to the conclusion of what happened in the past. Therefore, this model was selected to structure the study and each individual chapter within the research. The students’ learning outcome at each stage of the original model is modified to relate to the research topic. The researcher plays the role of a student and follows the instructions of the model from the first step of identifying an interest or curiosity of the past to the final step or conclusion.

The whole purpose of this study is to examine the development of New Zealand accounting standards for SMEs based on publicly available documents. Publicly available documents are classified into two categories: primary documents and secondary documents. Primary documents are authentically generated at source without any comments from stakeholders whereas secondary documents comprise of comments or viewpoints of relevant stakeholders.

Even though the study is not aiming to generate raw data, the publicly available documents appear to be valid for the purpose of narrating historical events. There are two approaches to acknowledge historical events within the historical research vein: traditional and modern. The similarity between these two approaches is the attempt to respond to unanswered questions about the past. The distinction between these two approaches is the way the facts are acknowledged. The traditional approach focuses highly on the past events and seems to present facts in a more objective manner, while the modern approach recognises the subjectivity within the way the facts are presented and is more likely to adopt the work's predisposition to perspectives.

The new (modern) approach relies largely on the traditional historical approach to generate much of the raw data and examine the reliability of the facts (past events) (Funnell, 1996, 1998). According to Previts, Parker, and Coffman (1990), the expectation for explanation and causal analysis may be raised as the new approach is selected:

> The historian searches for patterns of development and attempts to proceed from a determination (what happened) to a contingency (how it happened) basis. Facts are necessarily selected and organised through a judgmental process constrained by time and are provisional according to the historian's perception of the contextual variables of the period studied.
>
> History may not reveal the cause of an event as a certainty, but it can indicate probable factors affecting the event. The historian's assessment of the influence of contextual factors rests not on possibility or probability alone but also on adjusted plausibility. Indeed, the term cause is generally avoided when historical propositions cannot be empirically confirmed or refuted. (p. 8-9)

The facts are provisional to the contextual variables of the period studied. This research utilises the new historical approach as it emphasises the interpretation of publicly available documents to address the intellectual contribution to the subject matter, rather than to examine the reliability of the raw data.

New Zealand has been using the sector-neutral approach to standards setting and it is claimed to work well for New Zealand. In particular, New Zealand has attempted to sector-neutralise the IFRS (Perry, 2006). The research adopts the modern approach which requires explanation to show causal relationships between what events happened in the past. The historical narrative inquiry model of Colby (2008) also aims to enhance the interpretation skills of history students. Therefore, to answer to the research question: “What was occurring during the period of development of New Zealand accounting standards for SMEs and how appropriate is it for New Zealand to adopt the IFRS for SMEs?”, the research is structured in accordance with Colby’s model with certain modification to address causal relationships therein. These modifications are covered in Chapter 3 and Chapter 4, when coming to describe the development of New Zealand accounting standards for SMEs. The research firstly attempts to explain what caused the emergence of the sector-neutral approach in New Zealand and its impacts on New Zealand when trying to harmonise to or adopt international accounting standards. These causes form a typical feature (sector-neutrality) of accounting standards in New Zealand and they also contribute to form the final decision about the appropriateness of IFRS for SMEs in New Zealand. The overall research not only shows the development of accounting standards, but also describes the causal relationship. In addition, Chapter 7 discusses the revision of the Framework for Financial Reporting which is ongoing. In short, these three chapters primarily use secondary documents which include the comments or viewpoints of relevant stakeholders. Therefore, the structure of these chapters does not include the stage four: primary document analysis (see Figure 2.3 below). Chapter 5 and Chapter 6 analyse the authentic primary documents which were generated at source and make a comparison with secondary documents’ analysis. Therefore, these two chapters include the six stages of the model (see Figure 2.2 below).

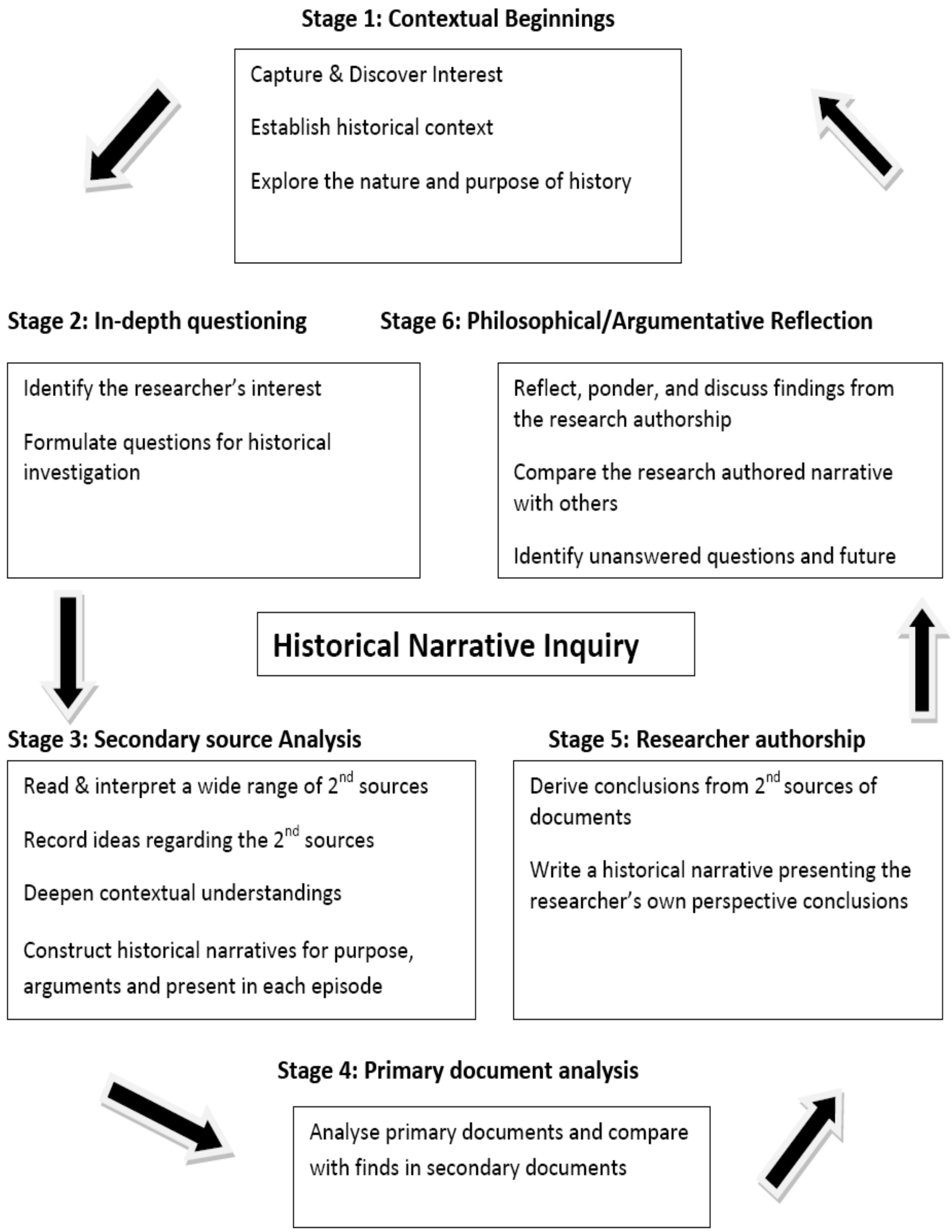
Using the publicly available documents to conduct the qualitative research is quite common (Bryman & Bell, 2007). Orton (1997) acknowledges the utility of publicly available documents to analyse events as “organisational post mortem” research. Reports of public inquiries are used by Turner (1994) when he conducts the research on the preconditions of the fire at the Summerland Leisure Centre, Douglas, Isle of Man in 1973. Gephart (1993) also conducted research on “naturally occurring retrospective and archival qualitative data including public inquiry transcripts and proceedings newspaper reports and corporate and government documents” (cited in Bryman & Bell, 2007, p. 565). Therefore, the secondary documents used in this study are valid.

Contribution

The model structures the study in such a logical and meaningful way. It seems to create an on-growing interest for the researcher and the readers from the beginning stage to the result-finding step. The model is also used to structure each chapter to express a clear and logical flow of the topic in each chapter. The finding within each chapter contributes to the overall findings of the research.

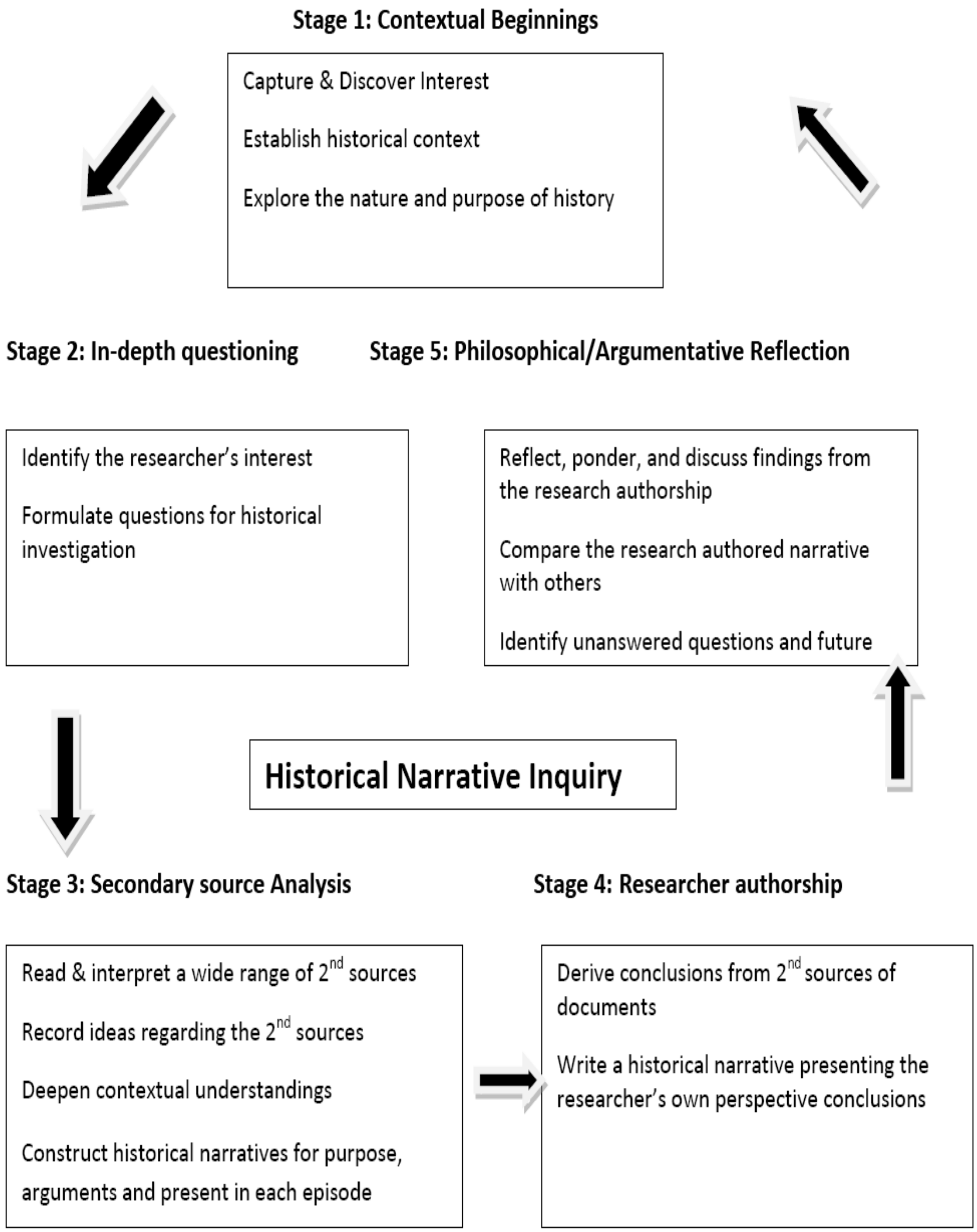
Modified Models

Colby's (2008) model mainly serves to educate history students. Therefore, Colby establishes learning outcomes for each stage of the model. This research adopts Colby's model because it assists readers to follow the stages the researcher took. The research thus appears to be clearer and more logical. Instead of showing the learning outcome as Colby does, the work of the researcher at each stage is outlined. Below are two figures which effectively serve to structure the chapters of the research.



Source: Adapted from Colby (2008)

Figure 2.2: Six stage historical narrative inquiry model.



Source: Adapted from Colby (2008)

Figure 2.3: Five-stage historical narrative inquiry model

Stage 1: Contextual beginning

a. Capture and discover interest

To globalise the financial reporting standards, the IASB has issued IFRS. IFRS is used for consolidated accounts by listed entities. New Zealand has adopted IFRS. In July 2009, the IASB issued IFRS for SMEs which are aimed to serve unlisted entities. New Zealand has not decided whether the IFRS for SMEs will be adopted.

b. Establish historical context

The majority of New Zealand businesses are SMEs. SMEs currently comply with the Framework for Differential Reporting. New Zealand has used the sector-neutral approach for standards setting since 1992. Therefore, the study examines the period from 1992 (sector-neutral approach started) to 2009 (when the IFRS for SMEs was issued).

c. Explore the nature and the purpose of history

The nature and purpose of history seems to place an important role in forming future expectations. Therefore, it appears to be essential to examine the historical development of New Zealand accounting standards for SMEs.

Stage 2: In-depth questioning

a. Identify the researcher's interest

The researcher is interested in discovering if New Zealand is going to adopt IFRS for SMEs.

b. Formulate questions for historical investigation

The research question "What was occurring during the period of development of New Zealand accounting standards for SMEs and how appropriate is it for New Zealand to adopt IFRS for SMEs?" is formulated for the historical investigation.

Stage 3: Secondary source analysis

Secondary documents used in this research are publicly available documents. They include interpretations and viewpoints of authors.

Contextual understanding is deepened by the analysis of the secondary documents. The historical development of the New Zealand accounting standards is visualised by the interpretation of a series of accounting events. In the stage of secondary source analysis, each step within this stage is not clearly differentiated but is linked together to construct a historical narrative for the argument's purpose.

a. Read and interpret a wide range of the secondary sources

As mentioned above, the research is not aimed at generating raw data or examining the reliability of facts, but to interpret past events with intellectual analysis.

The historical events this research is looking for are: the development of the New Zealand accounting bodies and the standards setters; the emergence and development of accounting standards for SMEs in New Zealand; the occurrence and development of the New Zealand Framework for Differential Reporting; the development of the Financial Reporting Framework; and Feedback from the Exposure Draft of IFRS for SMEs and the official IFRS for SMEs generated in July 2009. The events are arranged into periods of development (see Table 2.1 below).

Table 2.1: Accounting events (in chronological order)

Year	Description	References
1991	Proposed Framework for Financial Reporting	Bradbury & Baskerville, 2007
1992	The Accounting Research and Standards Board (ARSB) was dissolved and replaced with two boards: the Professional Practice Board to issue auditing standards; and the Financial Reporting Standards Board (FRSB) to publish financial reporting standards and interpretations or technical guidance as necessary; still entirely funded by the New Zealand Society of Accountants.	Simpkins, 1993
1993	Established the Financial Reporting Act 1993	Baskerville, 2005
1994	The Financial Reporting Act was passed and the Accounting Standards Review Board (ASRB) was established	Zijl & Bradbury, 2005
2002	ASRB decided that both public and private sectors must adopt the IFRSs by January 2007. Not for profit entities including public sector entities comply with the IFRSs and any standards specific to them.	ASRB, 2007
2005	Reporting entities were given option to adopt IFRSs early	ASRB, 2007
2007	The IFRS was replaced by the NZ IFRSs and all reporting entities must adopt the NZ IFRSs The FRSB decided to postpone mandatory adoption of NZ IFRSs for certain small entities that meet specific criteria. The Financial Reporting Act 1993 requires companies, other than exempt companies to prepare financial statements complying with GAAP.	ASRB, 2007
2008	The government commenced the review of the financial reporting requirements applicable to SMEs under the Financial Reporting Act 1993	ASRB, 2009
2009	The IFRS for SMEs was issued	IASB, 2009b

The data are collected from a large range of sources: reports and journal articles from New Zealand Institute of Chartered Accountants; Press Release from IASB New Zealand public domain, journal articles about the SMEs from the AUT library and database, *New Zealand Herald* articles, press releases and reports from the website of the MED, the IFRS for SMEs generated by the IASB. Data are also collected from conferences and seminars that the researcher attended (see Table 2.2 below).

Table 2.2: Data collection: Accounting Conferences

Month/Year	Topics	Place	Presenters
November 2009	Auckland Regional Accounting Conference (ARA)	The University of Auckland	Liz Hickey (Adjunct Professor, Department of Accounting and Finance, the University of Auckland)
January 2010	The Financial Reporting Reforms 2009	Unitec	Joanna Perry (Chairman of Financial Reporting Standards Board)
March 2010	Meeting with partners in PriceWaterHouseCooper (PwC)	PwC, Auckland Office	Jason Kearns (a partner, PwC, Auckland)
April 2010	NZ IFRS Update for SMEs	New Zealand Institute of Chartered Accountants	Brendan Lyon (a partner, Deloitte, Auckland) and Victoria Turner (Senior Manager, Deloitte, Auckland)

Source: Author (2010)

b. *Record of ideas regarding the secondary sources*

In each chapter, opinions (what people conceive about the past events) of different stakeholders (such as business owners, accounting practitioners, financial reporting standards board, etc) are recorded to deepen understandings of the historical context and to construct a historical narrative for the argument.

Table 2.3: Involved stakeholders considered

Stakeholders	Descriptions
Accounting Practitioners	Users of financial reporting standards
Accounting Academics	Who provide opinions from education's perspective
Standard setters	Setters of financial reporting standards
Business owners	Whose entities comply with the standard

Source: Author (2010)

Stage 4: Primary document analysis

Primary documents used in this research are the IFRS for SMEs issued by the IASB and the Framework for Differential Reporting issued by the New Zealand Financial Reporting Standard Board. They are analysed and compared with the analysis from secondary documents. Results of the comparison are reflected in stage 5.

Stage 5: Researcher authorship

The findings from Chapter 3 and Chapter 4 (if any) contribute to the researcher's conclusions from the researcher's own perspective. Eventually, the conclusions and arguments in each chapter are combined to form an overall conclusion for the research. The historical narrative is then presented with the intellectual contribution of the research. Carnegie and Napier (1996, p. 14) have suggested that narrative history may be little more than a chronology of events for the purpose of documenting the past (history): "narrative history may gain strength from the verve with which the facts are communicated, the story is told. The literary style with which history is narrated helps to lend credibility to the date and events uncovered". Moreover, materials of the story are presented in a chronologically sequential order which creates a coherent story with a single content (Stone, 1979).

Stage 6: Philosophical/ argumentative reflection

Similar to stage 5, the findings from the research authorship are discussed and posed against the opinions of stakeholders to identify research questions for future study.

2.2.3. Porter's framework

This chapter presents a review of the literature concerned with historical studies in accounting. Application of the historical narrative inquiry methodology in the accounting domain is supported by the literature. Porter (1981) is referred to as the authority for historical research in the accounting field.

Porter's methodology suggests how to select and process the evidential materials and how to organise their presentation for analysis. Therefore it fits in stages 3 and 4 of the historical narrative inquiry model. Funnell (1998) recites Porter's (1981) argument that the pattern and structure of life form the historical narrative. In addition, events occur in sequence provide meaning for events which happened previously or subsequently and the written narrative is also referred to as a work of history. Porter's statement below is quite often cited in the literature, such as Poullaos (1994) and Funnell (1998):

> the means to order the individual events which are proposed to constitute the facts of history, thereby making them comprehensible by identifying the whole to which they contribute. The ordering process operates by linking diverse happenings along a temporal dimension and by identifying the effects one event has on another, and it serves to cohere human actions and the events that affect human life into a temporary gestalt (Porter, 1981, p. 57)

To have a comprehensive picture of the contextual situation, the construction of Porter's model requires historical events to be carefully defined and represented chronologically. The duration of an event and durations around an event are also carefully selected as they determine the level of abstraction appropriate for the research. By looking at historical events, we would be able to examine the development of accounting standards for SMEs and their impact on other accounting events. This would form a basis for judgments on how suitable IFRS for SMEs is for New Zealand. The chronology of development of accounting standards for SMEs is from 1992 when the first standard relating to SMEs came out, to when the new IFRS for SMEs were published by the IASB in July 2009.

In historical narrative inquiry according to Porter (1981) each historical event is considered in the context in which it occurred, firstly to understand an overall picture and lastly to appreciate how the context formed characteristics of the event. Therefore, according to Porter's model, context and events are closely linked to each other and events make more sense within a context. Carnegie and Napier (1996) state:

> We believe that accounting history is enhanced by locating our narratives within an understanding of the specific context in which the object of our research emerges and operates, that we all write, implicitly if not explicitly, to a paradigm. However, the degree with which this needs to be emphasised depends on the particular subject matter of our research. We also believe that historical research in accounting gains its strength from its firm basis in the 'archive' (p. 8)

To investigate and explain the granting of the Royal Charter to the Institute of Chartered Accountants in Australia in 1928 for the 40-year effort, Poullaos (1994) combines the narrative explanation based on Porter (1981) with the literature on the sociology of the professions. He first analysed the development in accountancy using the historical analysis approach. According to Poullaos (1994), the historical narrative approach "incorporating the results of a detailed sequential analysis of a number of related, but unique, events" may result in the high level of comprehensible explanation. Porter's historical events appeared to be unique and non-recurring. Poullaos' demonstration of bringing the theory to practice by using narrative to comprehend past events in accountancy was found to be useful for subsequently interpreting and applying Porter (1981).

It was the first time Poullaos used Porter's framework to examine past accounting events. He found it useful, so it is expected to work well in this research. In regard to this research, both international and national (New Zealand) accounting standards setting environments are considered. The selected historical events may include economical, political, and social. These events are selected at different periods of time to show the transition and development of the standards relating to SMEs. Furthermore, they will be organised and structured in a chronologically sequential order which creates a single-content, coherent story as suggested by Porter's model.

This study is constructed in such a way that it aims to "live" what has happened in the past by interpreting publicly available documents. This would form a solid basis for the conclusion and future expectations. The historical narrative inquiry model serves as a map which is interlinked with Porter's framework to drive through the research.

There may be some other methodologies which may fit well to this type of research. The historical evidence comprises past events which are related to one another.

2.2.4 Data analysis

As mentioned above, the research is not aimed at generating raw data or examining the reliability of facts, but interpreting past events with intellectual analysis. There is quite a wide range of publicly available documents relevant to the study (discussed in stage three of Colby's model). The key "tool" used to analyse the data is interpretation skill. Each chapter discusses a topic. Relevant data are analysed and interpreted to address the research questions in each chapter. Each chapter is structured in accordance with Colby's model. Research questions of each chapter are sub-questions aimed to clarify and to support the overall research question.

Porter's framework interacts with Colby's model. Porter's framework is mainly used in selecting past accounting events, analysing and locating them in chronological order. Colby's model concentrates on how to provide insights to readers in a logical manner.

In conclusion, the research is designed in chronological order to facilitate readers' understanding of a dynamic flow of important events as they occurred. It also helps to make sense as to why the events happened at a particular time and show the relationship between the events. The chronological development of events illustrates a more comprehensive picture of the past that led to the current state of affairs in accounting standards in New Zealand. Each chapter's time line highlights the relationship between events to allow readers to continually reinforce the past and present. Therefore, the literature review is not located in a separate chapter, but spread through each chapter. Porter's framework and Colby's model are the key tools selected to conduct this research.

Chapter Three

The Development of Sector-Neutral Standards in New Zealand

3.1 Introduction

The publicly available documents related to the events under examination have been collected. The first event is the emergence of sector-neutral standard setting in New Zealand. The events which are associated with the emergence of the sector-neutral standards are arranged in the order in which the events occurred. The analysis starts with the interpretation of collected documents and records of stakeholders' opinions about the events. Each chapter is designed using the structure and model of historical narrative inquiry. Each chapter contains the five stages of the historical narrative inquiry model. This chapter introduces the structure of the profession's responsibilities and standard setting functions. It sets the scene for the standard setting process in New Zealand.

3.2 Historical Narrative Inquiry Model

The structure of the profession's responsibilities and standard setting functions in New Zealand are discussed. This chapter is structured in accordance with Figure 2.3 (the five-stage historical narrative inquiry model).

3.2.1 Stage 1: Contextual Beginnings

In 1946, New Zealand financial reporting regulation began with the New Zealand Society of Accountants (the NZSA) (Zijl and Bradbury, 2005) and at the same time the Australian Institute issued quite similar 'Recommendations on Accounting Principles' largely based on the 'Recommendations' of the English Institute. In 1974, the NZSA became an associate member of the International Accounting Standards Committee (the IASC) during which time local standards still had precedence but any difference from the requirements of IASC was specially acknowledged (Bradbury, 1998). In 1974, the NZSA issued Statements of Standard Accounting Practice (SSAPs). In 1980, the NZSA created an Accounting Research and Standards Board (the ARSB). The ARSB's function was to prepare accounting standards. The standards of public benefit entities are separately developed from those of the private sector entities. The public benefit entities are private not-for-profit entities (such as charities, sports clubs, etc) and service-oriented public sector entities (such as central government, government departments, local authorities, etc). Private sector entities are commercial or for-profit entities.

In November 1992, the ARSB was dissolved and replaced by two boards: the Professional Practices Board which issues auditing standards; and the Financial Reporting Standards Board (FRSB) which publishes financial reporting standards and interpretations or technical guidance. (Simpkins, 1993)

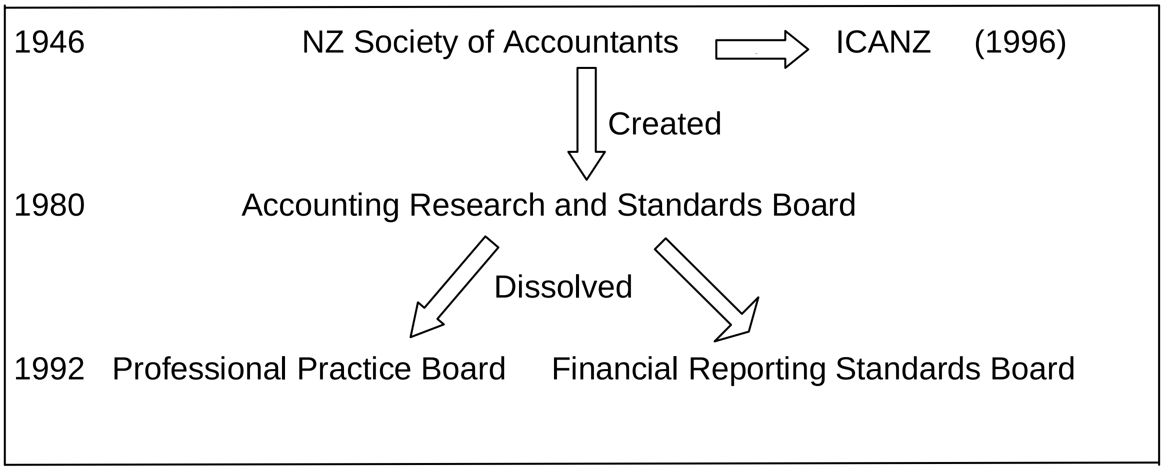
In 1992, Financial Reporting Standards (FRSs) was the new term for standards. In 1993, there were five SSAPs and five FRSs on issue. The standards are used to prepare financial statements for external users. As stated in the Public Finance Act 1989, the standards are linked to the state sector (Zijl & Bradbury, 2005).

The NZSA was the only body for accounting standards setting in New Zealand. The NZSA changed its name to the Institute of Chartered Accountants of New Zealand (ICANZ) in 1996. According to the Institute of Chartered Accountants of New Zealand Act 1996 (ICANZ, 1996, section 5, p. 2), the functions of the ICANZ are:

a) to promote quality, expertise and integrity in the profession of accountancy by its members in New Zealand:
b) to promote, control and regulate the profession of accountancy by its members in New Zealand:
c) to promote the training, education and examination of persons practising, or intending to practise, the profession of accountancy in New Zealand or elsewhere:

d) Any other functions that are conferred on it by the rules.

The development of New Zealand standard setting bodies can be summarised as follows:



Source: Author (2010)

Figure 3.1: The development of the standard setting bodies in New Zealand

In 1994, the government appointed the Accounting Standards Review Board (ASRB). The ASRB is a statutory body that is independent from the accounting profession. Its responsibility is to review and approve the FRSs which are submitted by the FRSB. Even though the standards continued to be developed by the FRSB, the ASRB approves standards submitted to them by the accounting profession and provides legal backing to the standards as established under the Financial Reporting Act 1993.

3.2.2 Stage 2: In-depth questions

What is sector neutrality? Why does New Zealand adopt the sector-neutral standards approach? How important are sector-neutral standards in New Zealand?

3.2.3 Stage 3: Secondary sources analysis

Sector neutrality is defined as the way economic transactions are treated regardless of the type of entities undertaking them. The treatment of economic transactions is the same regardless of whether they occurred in for-profit entities or public-benefit entities. Also under this approach, only one standard setting board is responsible for developing the accounting standards.

The neutrality in New Zealand developed in conjunction with the commercial reforms of the public sector. Slow economic growth and high debt were major issues which the newly elected Labour Government faced in 1984. Government expenditure was 39% of GDP. Major commercial operations of the government were corporatised and required to be operated successfully as businesses (see Boston, Martin, Pallot, & Walsh, 1991; and Scott, Ball, & Dale, 1997 for full discussion on these economic reforms). Within this climate of economic and political reform, the Minister of Justice initiated a comprehensive review of legislation. The commercial legislation, which promotes the corporate body form for organising the aggregation and use of capital, was seen to be central to the goal of an efficient economy (Boston et al., 1991; McCulloch & Ball, 1992).

The reform of the public sector was operationalised in two pieces of legislation: the State Sector Act 1988 which established accountability and service performance of government departments; and the Public Finance Act 1989 which allowed departments to operate their own bank accounts and required accrual-based accounting systems to be used. Accrual accounting was only one of the elements seen in a comprehensive programme of the public sector financial management reform. Other elements included the distinction between outputs and outcomes; control over input resources; and the distinction between purchase and ownership interests (Miah, 1991; Hay, 1992; McCulloch & Ball, 1992). These legislative reforms in the public sector were successful and largely influenced by the developments in the public sector accounting by the NZSA. The Audit Office and Treasury were concerned about the quality of financial information provided by government departments (Hay, 2001). Therefore the financial accounting reforms in the public sector began earlier than the commercial reforms. In

1978, the Controller and Auditor General issued a report which was primarily influential. The report described financial management in the public sector as “mediocre”; and accountability was described as “inadequate” (Hay, 2001).

In 1992, the FRSB adopted the sector-neutral approach to standard setting. It has been acknowledged that the sector-neutral approach has benefited New Zealand Financial Reporting Standards (FRSs) (Lee & Teixeira, 2004). Therefore, if the New Zealand standards setting body has to move away from the sector-neutral approach at some stage, it would possibly be as a result of political and historical reasons, not because of a flaw in the sector-neutral concepts (Lee & Teixeira, 2004). However, the sector-neutral concepts may not work efficiently. Assets are assets and liabilities are liabilities regardless of the sectors the entity belongs to. For example: cash is a current asset. Furniture is a non-current asset. Loans are long-term liabilities. These elements are the same in profit-oriented entities and public-benefit entities. Warren (2004) has demonstrated that many academics have argued about the recognition and measurement of assets and liabilities. The definition of an asset: “An asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity” (IFRS for SMEs, 2009, s2.15(a)). “The future economic benefit of an asset is its potential to contribute, directly or indirectly, to the flow of cash and cash equivalents to the entity. Those cash flows may come from using the asset or from disposing of it” (IFRS for SMEs, 2009, s2.17). Some argue that the public-benefit entities work for the public benefit, and the future economic benefits of the assets are public good benefits which are not cash convertible. Therefore, the definition of assets may not be satisfied. Similarly, “for a liability to exist and be reported, an entity must have little discretion to avoid a future economic sacrifice for a present obligation” (Warren, 2004, p. 28).

Many attempts to add further recognition, measurement and disclosure requirements to IFRS to be used for public benefit entities have been made (key changes to standards setting are summarised in Table 3 above). “The consequence of imposing additional measurement and recognition requirements would be that the entities subject to the requirements could no longer claim to be complying with IFRS" (Zijl & Bradbury, 2005, p. 11).

3.2.4 Stage 4: Research authorship

The emergence of sector neutrality in New Zealand resulted from the reforms of the New Zealand government in 1984. The adoption of sector neutrality could be considered as progress for the New Zealand accounting standards development. Sector neutral standards may have been appropriate at that time when the nature of transactions and their business contexts were similar among sectors. Accounting issues occurring in public-benefit entities may find solutions in the profit sector. In other words, solutions generated in the profit-oriented environment may have been a sector-neutral solution.

Transactions of each sector may grow more complicated along with the sector development over time. It is essential to consider the context when the transaction occurred. This may result in a unique aspect requiring a solution in each sector. A single set of financial reporting standards for each sector appears to be practical to capture and monitor business events by restructuring disclosure requirements. The relationship between performance information and accountability is more likely to be emphasised in the standards for each sector.

3.2.5 Stage 5: Philosophical/argumentative reflection

The contribution of New Zealand in the international standard setting process (which has enhanced New Zealand's international reputation as a standard setter), has mainly resulted from the benefits of taking a sector-neutral approach in the development of FRS (Lee & Teixeira, 2004). However, to ensure the New Zealand financial reports are comparable to those in different countries, they have to be prepared on the same basis. IFRS is uniquely developed for profit-oriented entities. IFRS for SMEs are a simplified version of IFRS, thus they serve small and medium for-profit entities. If New Zealand financial reporting standards are standardised to the international level, the New Zealand sector-neutral approach may be at risk. Its appropriateness to today's global trends is what needs to be examined. IFRS, which is designed for for-profit entities, have been settled and adopted in many countries, including New Zealand. If New Zealand chooses to maintain the sector-neutral approach, IFRS may have to be adjusted to accommodate the public-benefit entities. New Zealand and Australia are the two countries committed to sector neutrality in setting the FRSs. It may be essential for New Zealand to work jointly on this issue with Australia. To assist the New Zealand standard setters in making decisions and to add to the body of knowledge, it is important to examine the impacts of sector-neutral accounting standards on the Conceptual Framework, impacts on setting on terminology and impacts on setting on the timeliness of the due process which are discussed in the following chapter.

Table 3.1 Stakeholders' opinions (evidence collected)

Year	Stakeholders	Opinions	Sources (Title)	Pages
2004	Chartered Accountant	Quality of the FRSs in New Zealand is widely acknowledged. In fact, the FRSs have benefited from adopting a sector neutral approach	"Implications of IFRS for sector-neutral standard setting" Simon Lee and Alan Teixeira	21
2004	Chartered Accountant	New Zealand sector-neutrality is at a crossroad. New Zealand should maintain sector neutral standards because of the benefits to New Zealand. New Zealand institutional structures are well designed to synthesize international materials to generate a single set of standards neutral to both sectors and approve these standards as New Zealand regulation.	"At the crossroads" Ken Warren	26 28
2005	Accounting Academics	Imposing additional disclosures and requirements to the IFRS were expected to be useful as it could be applied in both sectors, but the entities subject to the requirements could no longer claim to be complying with IFRS. Such requirements will therefore, be restricted to apply only to public benefit entities. Therefore, it may be the end of sector-neutral standards in New Zealand	"Due Process and the Adoption of IFRS in New Zealand" Tony van Zijl and Michael Bradbury	11

Chapter Four

Impacts of Sector Neutral Accounting Standards

4.1 Introduction

In Chapter three, the development of sector-neutral standards setting in New Zealand was discussed. This included what drove the emergence of the sector neutrality and briefly contrasted the usefulness and drawbacks of sector-neutral standards in New Zealand. Therefore, this chapter discusses the impacts of the sector-neutral approach to the Conceptual Framework, impacts on setting on terminology, and impacts on setting on the timeliness of the due process.

4.2 Historical Narrative Inquiry Model

The impacts of sector-neutral accounting standards are discussed. This chapter is structured in accordance with Figure 2.3 (the five-stage historical narrative inquiry model).

4.2.1 Stage 1: Contextual beginnings

New Zealand is one of the early jurisdictions to adopt IFRS. The reporting entities in New Zealand were able to voluntarily adopt IFRS in 1 January 2005. The adoption became mandatory on 1 January 2007. The evidence collected in the prior chapter shows that the adoption of IFRS may put the sector-neutral standards at risk. IFRS is designed for profit-oriented entities only, not for all sectors (MED, 2005). If IFRS is modified to accommodate the Public Benefit Entities, IFRS will no longer be “pure IFRS” designed by the IASB and adopted globally. In addition, entities that comply with the “modified IFRS” may not be claimed as complying with IFRS. New Zealand is still maintaining both IFRS and the neutral-sector standards. If New Zealand decided to adopt IFRS for SMEs, would New Zealand maintain three sets of standards? IFRS for SMEs is a simplified version of the full IFRS. It is essential to understand the differences between the neutral-sector standards and international standards.

4.2.2 Stage 2: In-depth questions

What are the differences between the sector-neutral standards and the international accounting standards? What are the impacts of the sector-neutral standards on the globalisation objective? What is the future of the sector-neutral standards in New Zealand?

4.2.3 Stage 3: Secondary resource analysis

As discussed in the previous chapter, the sector-neutral approach has been adopted in financial reporting standards setting by New Zealand and Australia. Overall, it is a single set of financial reporting standards applicable to all entities regardless of the type of sectors they belong to. It is essential for the sector-neutral standards to be appropriate for users in different sectors. Therefore, it is fair to say that the development of the sector-neutral standards is driven by the needs of all users.

The adoption of the sector-neutral approach has some impacts on the Conceptual Framework, the Terminology, and the Due Process aiming to serve all the sectors.

Impacts of sector-neutral standards on the Conceptual Framework

A change in the objectives of reporting was one of major impacts of the sector-neutral standards. The “stewardship” role of financial reporting was replaced by the “accountability” role (Bradbury & Baskerville, 2007). Financial reporting is not only oriented toward the stewardship function of the accounting information suppliers but it is also a performance measure against the goal assigned to the accounting information suppliers based on the underlying accountability relationship. The accountability relationship exists both inside and outside an organisation. Within an organisation, employees are accountable to their respective managers depending on the organisational hierarchy of authority and responsibility. An organisation is also responsible to shareholders, creditors, governments, customers and society (Ijiri, 1983). In short, financial reporting may no longer be prepared to serve managers' functions only, but it is prepared to serve the public in general. Due to the objective changes of the financial reporting, the conceptual framework is also influenced.

Technically, the conceptual framework of accounting can either be accountability-based or decision-based. When a conceptual framework of accounting is established on an accountability basis, the focus is placed on the relationship between the suppliers and the users of the accounting information. The objective of accounting is to provide flows of fair information to the information users. The accountability-based conceptual framework acknowledges the right of the users to receive business reports and to inspect accounting records in the case of specified irregularities occurring. On the other hand, the accountability-based conceptual framework also recognises a desire to protect the privacy of information providers. Eventually, the users are ensured that the information they receive is free from bias and the information providers are also protected from the costs incurred by bias or misrepresentation. In the accountability-based conceptual framework, the interests of the two parties are carefully weighed (Ijiri, 1983).

In the decision-based framework, the focus is on the decision makers and the interest of the information providers is not considered. The objective of accounting reporting is to provide useful information for economic decisions. More information including subjective information is preferred as long as it is useful for decision makers. Attention of the accounting information suppliers is not focussed on how the business performance is recorded and reported. Conversely, in the accountability-based framework, discretion is used in recording and reporting the business activities to provide the best performance picture possible (Ijiri, 1983).

The accountability concept is used as a basis in the New Zealand Framework and it is defined in the Statement of Concepts for General Purpose Financial Reporting as follows: "Accountability is the requirement for one party to account to another party for its performance over a given period: for example, directors are accountable to shareholders, and Parliament holds Ministers to account" (ICANZ, 1993, Para 3.3)

The notion of "accountability" is more fully explained, together with the notion of "governing body" in the Framework for Differential Reporting. The differential reporting regime was first introduced in 1994 with the purpose of providing some concessions or exemptions for qualified entities from some of the financial reporting requirements. The Framework for Differential Reporting sets out some criteria for identifying which entities are eligible for exemptions. The criteria are regularly reviewed to adapt to changes in the business environment. It was first introduced in 1994 and revisions were made in 1997, 2002 and 2005.

According to the New Zealand Framework, any entity holding public accountability status or any entity in which there is separation of the owners and the governing body has to prepare general purpose financial statements (GPFSs). The GPFSs are defined in the New Zealand Framework as those which are "prepared and presented at least annually and are directed toward the common information needs of a wide range of users" (paragraph 6). The users of financial statements include present and potential investors, employees, lenders, suppliers and other trade creditors, customers, governments, their agencies, the public, funders, financial supporters and elected or appointed representatives (paragraphs 9 and 9.1). The obligation of producing the GPFSs might be established by statute or by the entity's founding documents. In addition, the Code of Ethics of the New Zealand Institute of Chartered Accountants imposes on its members a professional responsibility for the preparation or presentation of GPFSs to "take all reasonable steps within their power to ensure that GAAP is complied with" (paragraph 103).

The New Zealand Framework was revised in 2005 to assist SMEs including "clubs, incorporated societies, public sector bodies as well as companies" in their adoption of the IFRS. The users of the financial statements in the New Zealand Framework now include "taxpayers, donors and representative groups" (Bradbury & Baskerville, 2007, p. 13). More information was suggested to supplement "traditional" information reporting.

To provide a fair flow of information to users of all sectors, the New Zealand GAAP recommends (not requires) a statement of service performance to provide both financial and non-financial measures to meet financial reporting objectives. The qualitative characteristics and the assumptions underlying the preparation of the GPFSs remain unchanged except for the term “service potential”. The service potential term was included in the definitions of financial elements (Bradbury & Baskerville, 2007, p. 13).

Impacts of sector-neutral standards setting on terminology

Accounting language in both private and public sectors are altered and expanded under the sector-neutral accounting standards. For example: in terms of financial statements: “financial performance” replaced “income statement”; “financial position” replaced “balance sheet”; in terms of financial statement items: “financial surplus” replaced “profit”; and other terms used in accounting standards: “fairly present” and “fairly reflect” replaced “true and fair view”, and “governing body” replaced “director” (Bradbury & Baskerville, 2007, p. 13).

International Accounting Standards 1: Presentation of Financial Statements notes that the terminology used in the standards is suitable for both profit-oriented entities and public-sector entities. If public-benefit entities wish to use the standards, they “...may need to amend the descriptions used for particular line items in the financial statements and for the financial statement themselves.” (IAS 1.5). In my opinion, it would be confusing if each country or each business entity named this differently in their financial statements. Due to the increasing number of international business transactions within the business community, it is essential for the financial statements to be understood by global users.

Impacts of sector-neutral standard setting on the timeliness of Due Process

Additional public sector issues would increase the time taken for the process of developing exposure drafts, reviewing responses and ensuring the approved Financial Reporting Standards (FRSs) meet with constituency compliance. Herz (2003) calculated the time taken from the stage of developing an exposure draft to the final stage of approving a standard. He also compared the time for due process before and after the sector-neutral approach was adopted (before and after 1992). Evidence is provided in Appendix 1 which shows that it takes a considerably longer time for a standard to be processed and approved after 1992. For example: accounting for provisions, contingent liabilities and contingent assets took 66 months for completion of due process whereas before 1992 they took only 21 months. Accounting for investments in associates took 40 months for completion of due process whereas before 1992 they took only 20 months.

As mentioned above, New Zealand has attempted to modify the IFRS to accommodate public sector entities. Additional requirements for measurement and disclosure would be included in the IFRS. It would be a new challenge for the New Zealand standard setter, as Joanna Perry (2006) states, "Over the past few years the focus of the FRSB has been on developing the New Zealand equivalent to the IFRS. In doing so a lot of work was done to ensure that the NZ IFRS could be applied by public benefit entities". The adoption of the IFRS creates a challenging environment for New Zealand in a number of aspects. Perry (2006) outlines the issues in this area:

- ensuring the standards provide relevant information to users of general purpose financial reports of Public Benefit Entities;
- integrating requirements and guidance for Public Benefit Entities into standards developed for profit oriented entities from a broad range of international and domestically developed materials;
- ensuring adequate attention is given to addressing financial reporting issues facing Public Benefit Entities;
- ensuring that Public Benefit Entities constituents understand the potential implications of proposed domestic equivalents of IFRS and have the opportunity to comment on them from an informed perspective;
- implementing a credible and reliable process to achieve the above.

4.2.4 Stage 4 Research authorship

New Zealand adopted the sector-neutral approach to construct a single set of standards applicable to all sectors. Joanna Perry (2006) and Lee & Teixeira (2004) find that the sector-neutral approach serves quite well the standard setting in New Zealand and there are no flaws in the current approach. The benefits of the sector-neutral approach are undeniable as discussed in Chapter three. This approach worked well before the IFRS was adopted in New Zealand. The overall objective of adopting the IFRS is to achieve a transparent, consistent and high quality global set of standards. By doing so, investors would understand financial statements prepared across borders. The IFRS is adopted and harmonised in many jurisdictions as briefly mentioned in Chapter one. "In New Zealand our preference is to continue with the existing approach, enhanced as appropriate to address the needs of users of [Public Benefit Entities] financial statements" (Perry, 2006, p. 4). To maintain the sector-neutral approach, New Zealand may have to modify the IFRS or include additional requirements for measurements. By doing so, the IFRS in New Zealand may differ from other jurisdictions and may be a too "heavy" single set of sector-neutral standards. Having said that, it is also important for New Zealand to consider its ability to develop a set of sector-neutral standards by including all the users' needs and maintain the "pureness" of the IFRS applicable to profit-oriented entities.

Australia and New Zealand are two countries using the sector-neutral approach for standard setting. It appears to be a significant challenge for New Zealand and Australia to develop sector-neutral standards and be consistent with the other jurisdictions. The challenges of the sector-neutral approach may be how to include all users' needs in the set of standards and how reliable the standards would be. In my opinion it would not be difficult for New Zealand to develop a separate set of standards for public benefit entities. It may be even easier than attempting to aggregate standards of different sectors into one set of standards. If each sector has its own set of standards, the needs of all users are more highly likely to be comprehended. Furthermore, it would be easier for ICANZ to monitor the situation to ensure the standards serve its aim. On the other hand, the IFRS is also purely used as they are designed for.

4.2.5 Stage 5 Philosophical/argumentative reflection

It is fair to acknowledge that the compliance costs would be increased if multiple sets of standards are maintained. The barriers would also occur for accountants to work across sectors. Perry (2006) also states, "In New Zealand, the not-for profit sector is already finding it particularly difficult to attract qualified accountants and auditors, and any additional barriers to movement of accountants between sectors is likely to exacerbate this" (p. 4). New Zealand has used the sector-neutral approach since 1992. The emergence of the IFRS and the IFRS for SMEs may signal a transition time for New Zealand to move away from sector-neutral standards and restructure accounting forces to balance the needs of sectors. The attention is possibly mainly placed on the for-profit sector. Not much attention is on the not-for-profit sector as Joanna Perry states. Since business activities are getting more complicated, it may be a time for New Zealand and Australia to develop in-depth standards for each sector and move away from sector-neutral standards. To have more accountants in the not-for-profit sector, it may be worthwhile to focus more on the education of the not-for-profit accounting.

Table 4.1 Stakeholders' Opinions (evidence collected)

Year	Stakeholders	Opinions	Sources	Pages
1983	Accounting Academics	The accountability based conceptual framework weights the interest of both accounting information supplier and users. It also ensures the information provided is fair and free from bias	On the Accountability-Based Conceptual Framework of Accounting Iriji, Y	75, 76
2004	Chartered Accountants	Move away from the sector-neutral standards may be for political reasons, not a flaw in the sector-neutral concept.	Implications of IFRS for sector-neutral standards setting Lee, S & Teixeira, A	21
2006	Chartered Accountants	Sector-neutral approach remains the most effective and efficient approach. With the adoption of IFRS, the standard setting environment is more challenging	Comments on the Review of the Policy of Sector Neutral Accounting Standards Setting in Australia Perry, J	2
2007	Chartered Accountants	NZ standard setters are currently struggling to maintain sector neutrality in financial reporting because the IFRSs are primarily developed for profit-oriented entities	Sector-neutral Accounting Standards: A Ten-year Experiment Bradbury, M & Baskerville, R	1

Chapter Five

Development of Framework for Differential Reporting

5.1 Introduction

As mentioned before, the sector-neutral accounting approach has been used for standard setting in New Zealand and Australia since 1992. The sector-neutral standards are applicable to all profit-oriented entities and the public-benefit entities. Before New Zealand adopted the IFRS, the NZ FRSs were the first set of sector-neutral standards. In 2002, the ASRB announced that New Zealand was going to adopt the IFRS. Since New Zealand adopted the sector-neutral approach, New Zealand has been attempting to develop a set of sector-neutral standards based on the IFRS, called NZ IFRS. All entities, except for exempt companies, have to comply with the NZ FRSs (before the adoption of IFRS) and NZ IFRS. Since the major part of the New Zealand business community is SMEs, to fully comply with the NZ FRSs or the NZ IFRS appears possibly burdensome for the SMEs. Therefore, in 1994, the Framework for Differential Reporting for entities applying NZ FRSs was established to provide some exemptions from some of financial reporting requirements for entities that meet certain requirements. After New Zealand adopted the IFRS, the Framework for Differential Reporting was “rolled over” and applied to entities applying New Zealand equivalent to NZ IFRS. The whole purpose of the research is to respond to the research question “Should New Zealand adopt the IFRS for SMEs?” The IFRS for SMEs is designed for profit-oriented entities. Therefore, from Chapter five onward, the focus is mainly placed on the for-profit sector aspect.

This chapter aims to discuss the characteristics of SMEs and the development of the Framework for Differential Reporting by using the historical narrative inquiry model.

5.2 Historical Narrative Inquiry Model

This chapter aims to discuss the development of the Framework for Differential Reporting in New Zealand. Figure 2.2 (the six-stage historical narrative inquiry model) is employed to structure this chapter.

5.2.1 Stage 1: Contextual beginnings

SMEs have a significant effect on the New Zealand economy. They total 97.1% of New Zealand business entities, account for 40.7% of the economy's total output and for 30.7% of employees in New Zealand (MED, 2009a). No reliable figures for survivability of NZ SMEs are available. Originally, Statistics New Zealand used data on entries and exits from the business frame to determine a survival rate (Statistics New Zealand, 2006). This has led to the conclusion that "four out of five new firms fail within the first five years" (Berryman, cited in Cameron & Massey, 1999). According to John and Heleas (2000), the business environment where SMEs operate is quite uncertain due to the small number of customers and suppliers and their inability to drive prices. Because owners recognise that they cannot control prices, they concentrate on maximizing other values such as customer satisfaction. Apart from the challenge of pricing, SMEs have little certainty as to how the business will fare in the future. It is not easy to know if the SMEs are doing well as related financial and non-financial information is not always available to the general public (Baskerville & Cordery, 2006).

There are a number of criteria or thresholds used to define and differentiate SMEs from other business sizes. These criteria include: the number of employees; the turnover; the ownership structure; the management style; and the location of markets. These criteria are commonly used in many countries and some employ a combination of these measures.

Statistics New Zealand defines SMEs as entities with 19 or fewer employees (MED, 2006, p. 5). According to John and Heleas (2000), 85% of New Zealand companies employ five or fewer employees. Since 2003, some changes have been made on the measure of the full-time equivalent employee (FTE) count and employee count (EC).

The FTE measure comprises “paid employees and working proprietors who did not pay themselves a salary or wage”. “The EC measure covers paid employees but does not include working proprietors other than those who pay themselves a salary or wage” (MED, 2007, p. 6).

Since SMEs play an important role in the New Zealand economy, financial reporting standards for these have come to the attention of the standard setter and the regulators. In New Zealand, the Framework for Differential Reporting was established to provide some concessions or exemptions of financial reporting requirements for SMEs. At the international level, the IASB issues the IFRS for SMEs to relieve the SMEs from complying with the full IFRS on the one hand and it also aims to enhance the reporting standards of SMEs to a higher quality. However, New Zealand is still in the process of considering if they should adopt the IFRS for SMEs. It is also the question that this research aims to answer.

5.2.2 Stage 2: In-depth questions

Before New Zealand adopted the IFRS, the NZ FRSs was the first set of sector neutral standards. Since 2005, New Zealand has been attempting to develop a set sector-neutral standards based on the IFRS, called the NZ IFRS. The question is what is the reflection of these changes to the Framework for Differential Reporting? In other words, what is the historical development of the Framework for Differential Reporting?

5.2.3 Stage 3: Secondary resource analysis

Framework for Differential Reporting for entities applying NZ FRSs

As mentioned above, the majority of New Zealand companies are small and medium-sized entities and they have to prepare either special purpose financial reports or GPFSs. The Framework for Differential Reporting was established to provide some concessions for entities which are required to prepare GPFSs that comply with NZ GAAP. There are some criteria established to consider if an entity qualifies for the differential reporting (discussed in stage 4 below).

In February 1994, the Framework for Differential Reporting was first promulgated. During the subsequent year, the FRSB received requests for clarification and ruling on the implementation of some aspects of the Framework. When the issues were noticed, all the Institute members were called on to notify the Institute of any problems countering the practical implementation of the Framework. To ensure the smooth operation of the system, several refinements were made after that by the FRSB which has been given authoritative support within the accounting profession in New Zealand by the ASRB.

The FRSB has utilised the “top-down approach” to design the Framework for Differential Reporting. According to the top-down approach, the FRSB first produces a comprehensive set of standards applicable to non-qualifying entities. Lastly, the FRSB eliminates any irrelevant standards which are not applicable to entities which qualify for certain exemptions. In the United Kingdom, the “bottom-up” approach was adopted when an exposure draft for the proposed United Kingdom financial reporting standards for small entities was issued. The bottom-up approach also aimed to relieve small entities from some reporting requirements (Baskerville & Simpkins, 1997). As stated in section 4.22 of the Framework for Differential Reporting:

> closely held entities where the parent or ultimate controlling entity has the coercive power to tax, rate or levy to obtain public funds is not permitted to use a lack of separation between the owners and governing body as the basis for qualifying for differential reporting exemption.

The size criteria set in the Framework for Differential Reporting are regularly reviewed and entities which were previously “large” are able to apply the revised size criteria. In 1994, the revenue threshold was $2.5 million; the total assets threshold was $1.5 million. In 1997, the revenue threshold was $5 million; the total assets threshold was $2.5 million, employees were fewer than 20. Therefore, the number of entities which qualified for the exemptions set in the Framework for Differential Reporting possibly increased (Baskerville & Simpkins, 1997).

Framework for Differential Reporting for Entities Applying the NZ Equivalents to IFRS

The NZ IFRS have largely been adopted by large issuers, subsidiaries of overseas companies complying with IFRS and the public sector (ASRB, 2007). The FRSB found it necessary to have a Framework for Differential Reporting for entities applying the NZ IFRS. At the same time, the IASB was developing the IFRS for SMEs. Therefore, the FASB found it unwise to invest much time and money to develop a new approach for differential reporting concessions, given the existing Framework for Differential Reporting satisfies the objective of reducing compliance costs for a large number of entities. (Warren, Fisher, & Scott, 2004)

The Framework for Differential Reporting for Entities Applying the NZ IFRS was developed on the basis of the Framework for Differential Reporting for entities applying NZ FRSs established in 1994. While waiting for the outcome of international developments on the IFRS for SMEs, the differential reporting regime provides relief for qualifying entities. It provides some concessions for entities applying NZ IFRS. No comprehensive review has been made of this Framework. The Framework for Differential Reporting for Entities Applying the NZ IFRS was considered a short-term and interim measure. As a result, the majority of the concessions under NZ FRSs were carried forward to NZ IFRS. The differential reporting concessions can be termed mainly “roll over”. There are three broad assumptions about the costs and benefits of complying with financial reporting standards which have been used without re-examination since the initial Framework was developed in 1994. However, there were some proposed changes as discussed in the article “Differential reporting—FRSB issues Exposure Draft” (Warren, 2004). Based on the feedback received from constituents on ED-74: Related Party Disclosures (May 1994) and ED-91: Related Party Disclosures (April 2002), FRSB finds it is necessary to fully comply with NZ IAS 24 Related Party Disclosures. Therefore, it is in the proposal of the FRSB (except for the requirement of paragraph 16) which is to disclose key management personnel compensation in total and by category. As suggested from several submissions received on the Exposure Draft, users of the financial statements find the disclosure of full related-party information important and exemption from the proposed standard should be removed (Hannif, 2004).

5.2.4 Stage 4: Primary Document Analysis

Framework for Differential Reporting for entities applying NZ FRSs

The FRSB firstly prescribes comprehensive requirements (Appendix 3) for large companies and then eliminates irrelevant requirements for smaller entities. In other words, qualifying entities are granted “full exemptions” from some financial reporting requirements which are shown below and the qualifying entities are also granted “partial exemptions” (Appendix 4).

Table 5.1: Full exemptions from the NZ FRSs

Standards	**Descriptions**
FRS-10	Statement of Cash Flows
SSAP-12	Accounting for Income Tax
SSAP-23	Financial Reporting for Segments
FRS-31	Disclosure of Information About Financial Instruments

Source: Adapted from the Framework for Differential Reporting

The Framework for Differential Reporting was developed on the basis of the following assumptions outlined in s 3.3 of the Framework for Differential Reporting:

a) compliance with financial reporting standards creates costs (usually for the reporting entity) and benefits (usually for users of the financial reports);
b) compliance should be required only when the benefits of compliance exceed the costs;
c) financial reporting standards will be more accepted if they apply only where benefits are generally agreed to exceed costs.

Costs and benefits are used as criteria to differentiate if an entity has qualified for differential reporting exemptions. Since costs and benefits of financial reporting requirements are not easy to measure, the Framework for Differential Reporting adopt surrogates based on the following broad assumptions (s 4.14):

a) More benefits are derived from the [GPFSs] of entities with public accountability because reports of such entities are likely to have more users
b) There is generally no accountability requirement when all of the owners of an entity are also members of its governing body. However, where the owner and the governing body of an entity are different, an accountability requirement arises. In this case, the value of the entity's GPFSs to users may be expected to increase, and greater benefit is likely to be derived.
c) In general, the larger the entity, the more extensive the group of users benefiting from the information provided in its [GPFSs], and the greater the benefit likely to be derived.

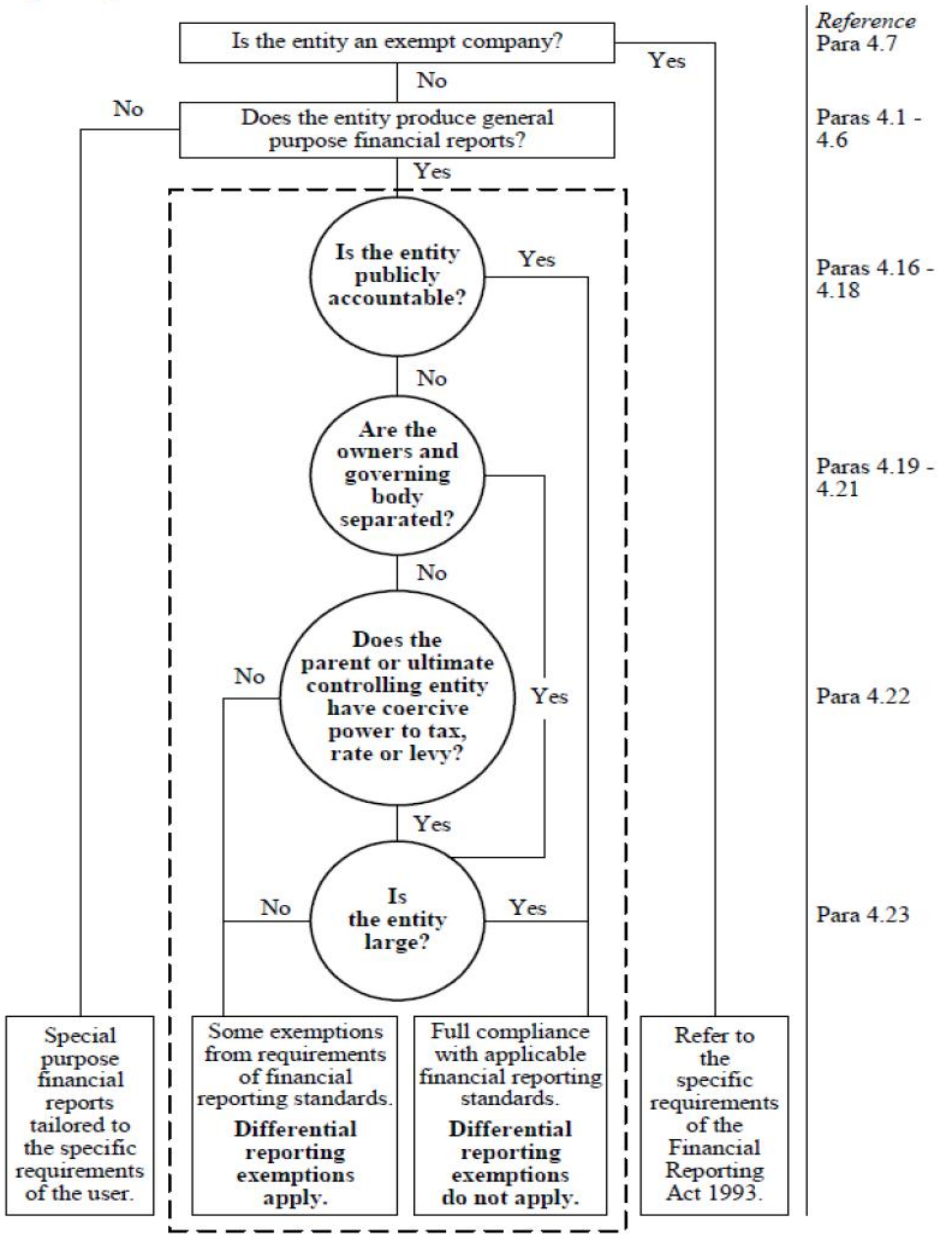
Therefore, to qualify for differential reporting exemptions, two of the three following criteria must be met (s 4.25):

a) An entity has no public accountability
b) All of an entity's owners are members of the governing body; or
c) An entity is not "large" according to two of the three size criteria: revenue, total assets, and number of employees.

Figure 5.1 provides an indication if entities qualify for differential reporting exemptions. The broken box in Figure 5.1 aims to provide the guidance for entities producing the GPFSs if they qualify for exemptions. Exempt companies are not required to comply with the FRSs. The Financial Reporting Act 1993 section 12 states that exempt companies simply need to comply with the Financial Reporting Order 1994. Size criteria for exempt companies were amended by the Financial Reporting Amendment Act 2006. Total assets do not exceed $1 million; turnover does not exceed $2 million; and there are five or fewer full-time equivalent employees.

The Framework for Differential Reporting may apply to entities producing the GPFSs if they satisfy two of three above criteria. “Differential reporting is consistent with legal requirements for financial reports to comply with [GAAP]” (s 3.4). Based on costs and benefits criteria, when an entity has public accountability, the entity’s GPFSs are the only sources of information that the general public could rely on for decision making. Therefore, the entity is not entitled to the differential reporting exemptions.

Note: material in the dotted box indicated the Framework for Differenti Reporting



Source: Baskerville & Simpkins (1997, p. 16)

Figure 5.1: Framework for Differential Reporting

Framework for Differential Reporting for Entities Applying the NZ Equivalents to IFRS

Reporting entities had the option to adopt IFRS from 1 January 2005 voluntarily and adoption became compulsory on or after 1 January 2007. Since New Zealand uses the sector-neutral approach for standard setting, the NZ IFRS appears to be a cost burden for SMEs, the Framework for Differential Reporting is rolled over from the Framework for Differential Reporting for entities applying the FRSs with certain proposed changes from the FRSB. The FRSB (2004) proposed to consider differential reporting exemptions for all disclosures in the NZ IFRS which are not currently required in a NZ FRSs, and to remove the disclosure of the reconciliations between opening and closing assets and liability amounts from the financial statements.

Table 5.2: The FRSB's proposal for changes of some FRSs

Standards	Descriptions	Current Application	The FRSB's proposal
FRS-9	Fees Paid to Auditors	Information to be disclosed in Financial Statements enables a qualifying entity to simply disclose the total dollar amount of audit fees.	The FRSB found that audit fees paid need to be broken down to adapt to the current environment. Therefore, FRSB proposes to take this concession off
FRS-10	Cash Flow Statement	Currently qualifying companies are not required to prepare Statement of Cash Flow	Statement of Cash flow is proposed to be prepared as part of the financial statements
SSAP-22	Related Party Disclosures	Qualifying entities shall comply with para 5.1 (a)(b)	The FRSB finds the necessity to fully comply with NZ IAS 24 Related Party Disclosures. Therefore, it is in the proposal of the FRSB except for the requirement of paragraph 16 which is to disclose key management personnel compensation in total and by category

Source: Adapted from Warren (2004)

The FRSB is concerned if the users receive sufficient information on the entity's related-party relationships and transactions, particularly given the potential impact of related party transactions on the reported financial performance and position of an entity. The lack of disclosure of related-party relationships and transactions appears to be a major issue for finance companies in New Zealand. Bill Wilson, finance lecturer at Massey University, has found that the collapse of the finance company sector in New Zealand was actually caused by weakness in corporate governance and regulation which had happened before the global crisis actually occurred (Parker, 2010). He has conducted his research by taking a sample of four finance companies: Provincial Finance, Bridgecorp, Five Star, and Geneva Finance. The findings are: through related party transactions the money was taken out by directors. Related party transactions were not disclosed as being such party (Parker, 2010).

The proposed changes made by the FRSB were not incorporated in the Framework for Differential Reporting for Entities Applying the NZ IFRS. However, size criteria were reviewed and changed. An entity is considered large if it exceeds any two of the following three size criteria: (i) total income of $20 million, (ii) total assets of $10 million or (iii) 50 employees (paragraph 3.9). The Framework for Differential Reporting for Entities Applying the NZ IFRS was issued in June 2005 and incorporates amendments up to November 2008. The Framework for Differential Reporting grants full exempt from the NZ IAS 7: Statement of Cash Flow for qualifying entities, certain partial exemptions (Appendix 5) and no exemptions from certain standards (Appendix 7). Figure 5.1 (above) is still being used as a guideline for assessing if an entity qualifies for exemptions.

Table 5.3 (below) provides a summary of alternatives for an entity to qualify for the Framework for Differential Reporting. There are three cases or alternatives under which an entity can be qualified.

Table 5.3: Criteria to be a qualified entity

Case 1	No public accountability	No separation of owners and governing body	
Case 2	No public accountability	Size Criteria 1	Total assets <10 million Total income <20 million
		Or Size Criteria 2	Total assets <10 million Employees < 50
		Or Size Criteria 3	Total income <20 million Employees < 50
Case 3	No separation of owners and governing body	Size Criteria 1	Total assets <10 million Total income <20 million
		Or Size Criteria 2	Total assets <10 million Employees < 50
		Or Size Criteria 3	Total income <20 million Employees < 50

Source: Author (2010)

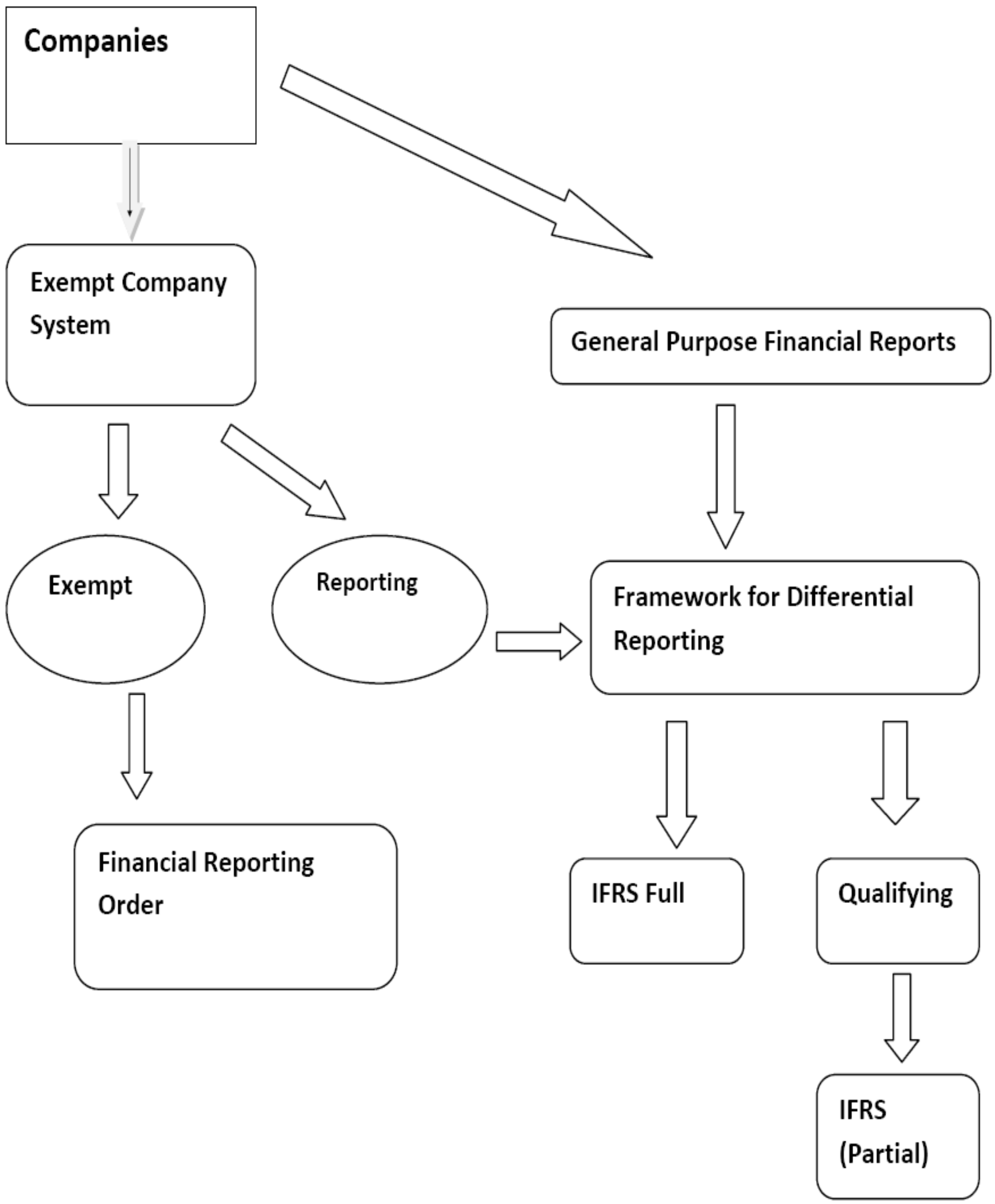
5.2.5 Stage 5: Research Authorship

The Framework for Differential Reporting plays a very important role in the SMEs community in New Zealand. It provides a relief for the qualified entities from fully complying with financial reporting requirements (see Figure 5.2 below). The Framework for Differential Reporting is based on costs and benefits assumptions to consider if the entity which produces the GPFSs qualifies for concessions.

Decisions of selecting which entities fall into the SMEs' range would have an influence on the cost–benefit argument. When public accountability is used as a basis, the size of an entity becomes irrelevant. In particular, a small (with few employees) publicly accountable entity would bear high accounting costs. On the other hand, a large entity but with no public accountability will be granted exemptions (Baskerville & Cordery, 2006). Therefore, the differential reporting framework has been used to balance the cost of fully complying with regulation and expected economic benefits to SMEs in many jurisdictions such as New Zealand, Australia, and the United Kingdom (Devi, 2003).

5.2.6 Stage 6: Philosophical/ Argumentative Reflection

The increase in size criteria in the Framework for Differential Reporting for Entities Applying the New Zealand Equivalents to IFRS increases the number of entities qualifying for the Differential Reporting Framework. Large entities appear to have benefitted from the concessions and smaller entities may find them cost burdensome. The Framework for Differential Reporting may be working well for New Zealand organisations. Since the current Framework for Differential Reporting has not been comprehensively reviewed, it may not be suitable for a wide range of entities. The Framework for Differential Reporting for Entities Applying the New Zealand Equivalents to IFRS could be seen as an interim short-term project developed to provide concessions for entities applying NZ IFRS while waiting for the upcoming issue of a global set of standards, the IFRS for SMEs. The FRSB may imply the possibility of adopting the IFRS for SMEs. The question is how the IFRS for SMEs fits in New Zealand's business community. The next chapter discusses characteristics of the IFRS for SMEs and makes a comparison between the IFRS for SMEs and the Framework for Differential Reporting.



Source: Author (2010)

Figure 5.2: Summary of Framework for Differential Reporting

Chapter Six

Discussions of adoption of IFRS for SMEs

6.1 Introduction

The IASB has found that benefits of having global financial reporting standards are not limited to listed companies. SMEs and their financial statements' users also get benefits from the common set of standards. SMEs' financial statements can be compared with those in different countries. The IASB was quite mindful of the cost and benefit for SMEs to implement IFRS for SMEs. Therefore, IFRS for SMEs was designed based on the considerations of users' needs as well as cost and benefits. According to the Basis for Conclusion (BC) on Exposure Draft IFRS for SMEs, "the nature and degree of the differences between full IFRS and an IFRS for SMEs must be determined on the basis of users' needs and cost-benefit analyses" (IASB, 2007, BC 25).

The IFRS for SMEs is a simplified version of the full IFRS and it is designed to serve SMEs. Compared with the full IFRS, extensive disclosure requirements are reduced from the IFRS for SMEs. The IASB uses SME as the name for entities eligible to use the new standard; in other places, such entities are referred to as "private entities" or "non-publicly accountable entities" (Pacter, 2008). Different jurisdictions may have different definitions of SMEs and their financial reporting obligations. As discussed in Chapter one, different countries have different size criteria to define SMEs and there may be a large variety of size of SMEs within a country. New Zealand SMEs appear to be much smaller than those in the EU and there are about seven sizes of SMEs in New Zealand (Hickey, 2009). Therefore, having a set of standards which can cover all SMEs and does not create any cost burden for small entities is challenging. The IFRS for SMEs is designed for SMEs but it may not be suitable for all SMEs in different countries. As a result, the decisions on which entities should use the IFRS for SMEs rest with countries' national regulatory authorities and standard-setters.

6.2 Historical Narrative Inquiry Model

This chapter aims to examine the appropriateness of IFRS for SMEs in New Zealand. The chapter is structured in accordance with Figure 2.2 (the six-stage historical narrative inquiry model).

6.2.1 Stage 1: Contextual beginning

The New Zealand FRSB has not decided if New Zealand is going to adopt IFRS for SMEs. The lack of any comprehensive review of the Framework for Differential Reporting for entities applying the FRSs shows that the FRSB has a high expectation on the IFRS for SMEs and for the future of SMEs in New Zealand. The key issue which needs to be considered is the appropriateness of the IFRS for SMEs for the New Zealand environment. Results of this discussion may contribute significantly to the ultimate decision of the FRSB.

6.2.2 Stage 2: In-depth questions

What are the advantages and disadvantages of the IFRS for SMEs compared to the New Zealand Framework for Differential Reporting? How does the IFRS for SMEs fit in New Zealand environment?

6.2.3 Stage 3: Secondary resource analysis

IFRS for SMEs is based on the same concept as the full IFRS but simplified to meet the needs of users. IFRS for SMEs has been shortened by 85% compared to the full (Epstein & Jermakowicz, 2007). The needs and expectation of SMEs users are different from those in listed companies because their business transactions are less extensive or less complicated. They need a simpler set of rules. The research on United Kingdom owner–manager's enterprises has found that the cost of preparing financial statements is too high (Sian & Roberts, 2009). Although this is not a formal investigation, it appears to be the belief of some prominent members of the accounting profession that New Zealand is not likely to adopt the IFRS for SMEs because Australia has stated its intention to keep the Framework for Differential Reporting (Victoria Turner—Senior Manager in Deloitte Auckland; Joanna Perry—Chairman of FRSB; Liz Hickey—Professor at Auckland University; and Jason Kearns—partner in PwC Auckland)

Grant Thornton International Business Report (IRB) (2010) conducted research which covers the opinions of over 7,400 business owners across 36 jurisdictions. “Businesses in Ireland, the Philippines and Taiwan were most enthusiastic about greater transparency with 85% of businesses citing greater transparency as a key benefit” (p. 1). In addition, the result of the research conducted by Grant Thornton shows that businesses realise financial reporting could help them to expand their business with 37% citing easy access to capital markets as a key benefit facilitating across-border trading. Alex MacBeath, a leader at Grant Thornton International, makes a comment on the research results. He said that, even though the SMEs normally have no obligation for reporting their financial information or legal business structure, leaders of the businesses increasingly recognise the fact that their financial reporting has to be transparent and more readily comparable with competitors.

When asked about their awareness of the IFRS for SMEs, “53% of businesses owners globally said they were aware of IFRS for SMEs. Regionally, business owners within the EU are the most likely to be informed (67%) with awareness highest in Ireland (86%), Spain (79%), Finland (78%), and the United Kingdom (76%). Business owners in Asia Pacific countries are the least likely to have heard of IFRS for SMEs, with Japan (19%) and Thailand (18%) being the least informed.” (IRB, 2010, p. 1)

The IRB (2010) also includes a question about whether the business owners would like their country to adopt the IFRS for SMEs. The result shows that, globally, 52% business owners answered ‘yes’ and are quite supportive (businesses in Mexico were at 89%, 85% in the Philippines, and Chile 84%).

According to the “IFRS for SMEs Update” issued on 28 May 2010, the IASB keeps a record of jurisdictions that have adopted, or are planning to adopt the IFRS for SMEs. There are currently 60 jurisdictions in the list. According to the IASB (2010), the Hong Kong Institute of Certified Public Accountants issued the Hong Kong Financial Reporting Standard (HKICPA) for Private Entities (HKFRS for Private Entities) on 30 April 2010. This new standard is almost the same with the IFRS for SMEs except for some income tax requirements modified to be appropriate for the Hong Kong’s business environment. Tanzania has announced that non-publicly accountable entities which include private business entities and government business entities are permitted to use the IFRS for SMEs. The number of employees of those entities has to be less than 100 and capital investment must less than Tanzanian Shilling 800,000,000 (approximately US$600,000). Besides this, the Egyptian Society of Accountants and Auditors is developing an exposure draft of a proposed Egyptian Accounting Standards for SMEs and expect to release the proposed exposure draft some time in 2010. The Malaysian Accounting Standards Board has also issued an exposure draft which is identical to the IFRS for SMEs. Its adoption’s objectives are: to enhance to confidence of users on the SMEs’ accounts; to provide advanced comparability for users of SMEs’ accounts; to reduce the maintaining cost of standards on a national basis; and to prepare for a growing stage of entering to the public capital markets.

These countries seem to be getting ready to adopt IFRS for SMEs. They all have the same objective, which is to enhance the transparency of SMEs’ accounting and to build up the confidence of users on the SMEs’ accounts.

6.2.4 Stage 4: Primary document analysis

The business activities of SMEs are not as complicated as those of the listed entities. Due to the simplicity of the nature of their business, SMEs mainly produce financial statements for their owner–managers or tax authorities or other governmental authorities. Financial statements produced for a specific purpose (i.e., tax authorities) are not GPFSs. The objectives of GPFSs differ from those of tax laws. Therefore, financial statements prepared in accordance with the IFRS for SMEs do not comply with all the measurements required by a country's tax laws and regulations. However, if required to prepare GPFSs, an entity could easily use information in their GPFSs to prepare a tax return.

It is essential for SMEs to have an appropriate set of standards with which they can comply without causing a significant cost burden. It also promotes the transparency of the New Zealand financial system in particular and the New Zealand economy in general (PwC, 2010). To ensure a rational decision is made as to whether New Zealand should adopt the IFRS for SMEs, the comparison between the IFRS for SMEs and the Framework for Differential Reporting plays an important role.

6.2.4.1 Comparison between characteristics of the IFRS for SMEs and the Framework for Differential Reporting

Similarities between the IFRS for SMEs and the Framework for Differential Reporting

The overall objective of the IFRS for SMEs and the Framework for Differential Reporting is to provide some financial reporting concession for the SMEs based on their different users' needs, costs and benefits consideration.

Qualifying entities are those that do not have public accountability and prepare general purpose financial statements for external users.

Differences between the IFRS for SMEs and the Framework for Differential Reporting

Overall difference

As discussed in the previous chapter, entities qualify for the Framework for Differential Reporting have to refer to the NZ IFRS, However, the IFRS for SMEs is a stand-alone document of only about 232 pages.

In developing the Exposure Draft of a proposed IFRS for SMEs, the IFRS for SMEs was planned to be stand-alone but it was not fully so. In particular, there were some sections an entity had to cross-reference to the full IFRS.

For example: investment in associates; borrowing costs; development costs; intangible assets; investment property; jointly controlled entities; presenting operating cash flows; property plant and equipment; and government grants.

The final IFRS for SMEs is a completely stand-alone set of standards (IASB, 2009c)

Standards comparison

Table 6.1: Comparison steps

Steps	Descriptions
1	The financial reporting standards named in the IFRS for SMEs are matched with those in the Framework for Differential Reporting resulting in “common standards”
2	Check the Framework for Differential Reporting if qualifying entities receive full/ partial/ or no exemptions from those “common standards”
3	Check each exempt paragraph stated in the Framework for Differential Reporting if it is required by the IFRS for SMEs. If the exempt paragraph is not exempt in the IFRS for SMEs, it is marked as “required” in the column of the IFRS for SMEs. If the paragraph is not stated in the IFRS for SMEs, it is marked as “not required”. Otherwise, a brief note is provided

Source: Author (2010)

Table 6.2: Overall comparison of the IFRS for SMEs and the Framework for Differential Reporting

IFRS FOR SMEs – JULY 2009	Framework for DR		
	Partial	Full	Not
1 SMALL AND MEDIUM-SIZED ENTITIES			
2 CONCEPTS AND PERVASIVE PRINCIPLES			
3 FINANCIAL STATEMENT PRESENTATION	x		
4 STATEMENT OF FINANCIAL POSITION	x		
5 STATEMENT OF COMPREHENSIVE INCOME AND INCOME STATEMENT	x		
6 STATEMENT OF CHANGES IN EQUITY AND STATEMENT OF INCOME, AND RETAINED EARNINGS	x		
7 STATEMENT OF CASH FLOWS			
8 NOTES TO THE FINANCIAL STATEMENTS			
9 CONSOLIDATED AND SEPARATE FINANCIAL STATEMENTS		x	
10 ACCOUNTING POLICIES, ESTIMATES AND ERRORS	x		
11 BASIC FINANCIAL INSTRUMENTS	x		
12 OTHER FINANCIAL INSTRUMENTS ISSUES	x		
13 INVENTORIES	x		
14 INVESTMENTS IN ASSOCIATES	x		
15 INVESTMENTS IN JOINT VENTURES		x	
16 INVESTMENT PROPERTY	x		
17 PROPERTY, PLANT AND EQUIPMENT	x		
18 INTANGIBLE ASSETS OTHER THAN GOODWILL	x		
19 BUSINESS COMBINATIONS AND GOODWILL	x		
20 LEASES	x		
21 PROVISIONS AND CONTINGENCIES	x		
22 LIABILITIES AND EQUITY			
23 REVENUE	x		
24 GOVERNMENT GRANTS		x	
25 BORROWING COSTS	x		
26 SHARE-BASED PAYMENT		x	
27 IMPAIRMENT OF ASSETS	x		
28 EMPLOYEE BENEFITS	x		
29 INCOME TAX	x		
30 FOREIGN CURRENCY TRANSLATION			
31 HYPERINFLATION		x	
32 EVENTS AFTER THE END OF THE REPORTING PERIOD		x	
33 RELATED PARTY DISCLOSURES	x		
34 SPECIALISED ACTIVITIES			

Source: Author (2010)

Comparing the Framework for Differential Reporting with the IFRS for SMEs is like comparing apples and oranges. The IFRS for SMEs appears to be a comprehensive set of standards which provide basic financial reporting requirements for SMEs. The language used in the standards is quite concise. It is a stand-alone set of standards. The qualifying entities do not need to refer back to the full IFRS.

The Framework for Differential Reporting for entities applying the NZ IFRS does not provide a comprehensive set of standards with which qualifying entities must comply. Instead, the Framework for Differential Reporting provides a list of full exemptions; a list of partial exemptions and a list of full compliance. The presentation of the Framework for Differential Reporting appears to be confusing and complicated. In particular, to make use of the Framework for Differential Reporting, the qualifying entities have to refer back to the full NZ IFRS. The NZ IFRS is possibly where the qualifying entities have to start off and cross out any allowed concessions. It appears to be complicated for SMEs to maintain their accounts by using both NZ IFRS and the Framework for Differential Reporting.

The research is trying to obtain the answer for the question of whether New Zealand should adopt the IFRS for SMEs. The assumption is if New Zealand adopts the IFRS for SMEs, all of the reporting standards are comprehensively set in these standards. Therefore, the IFRS for SMEs are used as a foundation to compare with the Framework for Differential Reporting. In particular, the scope of the comparison is within the financial reporting standards named in the IFRS for SMEs.

It is understandable if the exempt paragraph stated in the Framework for Differential Reporting is not required by the IFRS for SMEs. The IFRS for SMEs are a simplified version of the full IFRS. As mentioned above, the IFRS for SMEs are 85% shorter than the full IFRS. “This was achieved by eliminating topics deemed to be not generally relevant to SMEs, by eliminating certain choices of accounting treatments, and by simplifying methods for recognition and measurement” (Epstein & Jermakowicz, 2007, p. 39).

Table 6.2 is the result of step 1 and 2 of Table 6.1: comparison steps. It shows that the majority of standards set in the IFRS for SMEs receive partial exemption from the full NZ IFRS. Foreign Currency Translation is not exempt as stated in the Framework for

Differential Report. According to the Framework, qualifying entities fully comply with a list of 39 standards (Appendix 6) set in the NZ IFRS. There are 6 standards out of 39 standards which are required by the IFRS for SMEs as shown in Table 6.2.

Table 6.3 (below) shows the result of step 3 (from Table 6.1: comparison steps) which compares each paragraph stated in the Framework for Differential Reporting with the IFRS for SMEs. The result shows that quite a large number of paragraphs exempted from the full NZ IFRS (stated in the Framework for Differential Reporting) are also exempt from the IFRS for SMEs. It is a good indicator that the costs and benefits are taken into consideration by the IASB. According to the Basis for Conclusion on IFRS for SMEs (IASB, 2009c), the plan of establishing a global set of standards for SMEs was conceived of as unrealistic because the size range of this group of entities is quite broad from "micro sized" entities with fewer than 10 employees up to large unlisted entities with hundreds of employees. The IASB disagreed and explained, "the IFRS for SMEs is designed for entities regardless of size, that are required, or elect, to publish [GPFSs] for external users....not in a position to demand reports tailored to meet their particular information needs" (IASB, 2009c, BC71, p. 26). The Board was also aware of some debates about the cost burden for micro sized entities to implementing IFRS for SMEs. In responding, the Board said "...over 80 jurisdictions have decided that full IFRSs should be required or permitted for all or most entities, including micro. If full IFRSs have been judged suitable for all entities, then the IFRS for SMEs will surely not be burdensome" (IASB, 2009c, BC73, p. 26).

In addition, compared with the full IFRS, the disclosure requirements in the IFRS for SMEs are substantially reduced. The some accounting policy options are also removed from the IFRS for SMEs (IASB, 2009c, BC156). To make the IFRS for SMEs a stand-alone document, the remaining options are addressed directly, appropriately simplified from the full IFRS (IASB, 2009c, BC94). The simplifications of presentation, recognition and measurement from full IFRS are also reflected in the IFRS for SMEs. These simplifications can be seen in Table 6.3 (below).

Table 6.3: Detailed comparison between the IFRS for SMEs (2009b) and the Framework for Differential Reporting

Presentation of Financial Statements	
IFRS for SMEs	**The Framework for Differential Reporting (Qualifying entities exempted from the following paragraphs)**
Statement of Financial Position	
Not required	Paragraph 31(f): when the entity starts the retrospective accounting policy; retrospective restatement or reclassification of items in its financial statements, the entity is not required to present a statement of financial position as at the beginning of the earliest comparative period
Not required	Paragraph 41(b): disclose the amount of each line or class of items that is reclassified
Required	Paragraph 54 (j, p): disclose the total assets classified as held for sale; assets and liabilities included in disposal groups classified as held for sale
Not required	Paragraph 61: to disclose the amount expected to be recovered/settled after more than twelve months for each asset and liability line item combined with amount expected to cover/settle more and less than twelve months after reporting period
Required	Paragraph 79(a)(i)(iii): disclose the number of share authorised, par value per share or if shares have no par value
Not required	Paragraph 98(a): disclose the written down inventories and the reversal of such write downs; however, qualifying entities have to disclose the write down and reversal of Property, Plant and Equipment

(6.3 cont)

Statement of Changes in Equity and Statement of Income and Retained Earning	
Not required	Paragraph 106: not required to prepare the statement of changes in equity if there are no transaction between the equity owners and the entity; and no adjustments to the opening balance of retained earnings during the current and previous period
Not required	Paragraph 122: disclose the judgement made in the process of applying the entity's accounting policies that has significant effect on the amount recognised in the financial statements
Not required	Paragraph 125: disclose information about the assumptions made about the future and other major uncertainty estimation at the end of the period which may result in the risk of material adjustment to the carrying amount of assets and liabilities within next reporting period
Not required	Paragraph 134: related to paragraph 135(a): disclose qualitative information about the entity's objectives, policies and process of managing capital; 135(b) disclose quantitative data about what an entity manages as capital; 135(c) disclose any changes in qualitative information or quantitative data from previous period.

(6.3 cont)

Accounting Policies, Estimates and Errors	
Not required	Paragraph 30: disclose the impact of a NZ IFRS that has been issued but is not yet effective
Basic Financial Instruments and other Financial Instrument Issues	
Required	Paragraph 14: disclose the carrying amount of the financial assets that the entities has pledged as collateral and related terms and condition
Not required	Paragraph 15 disclose the fair value of collateral held or collateral sold or repledged including terms and conditions associated with the use of the collateral in circumstances where an entity holds collateral and is permitted to sell or repledge the collateral
Not required	Paragraph 16: reconciliation of changes in any separate credit or impairment account relating to credit losses of any financial assets
Not required	Paragraph 23: disclose cash flow hedges including the period that cash flow are expected to occur; description of the forecast of any transaction that is not expected to occur; amount recognised in other CI during the period or reclassified from equity to profit or loss during the period
Required	Paragraph 24: disclose gains and losses in fair value hedges, ineffectiveness recognised in profit and loss from hedges of net investments in foreign operations
Required	Paragraph 25: (except for circumstances set in paragraph 29) disclose fair value of each class of financial assets and liabilities to be able to compare with its carrying amount
Required	Paragraph 26: limit the offsetting of fair value disclosures of financial assets and liabilities to the extent that the carrying amounts of classes of financial assets and liabilities are offset in the statement of financial position

(6.3 cont)

Required	Paragraph 27 discloses method and assumptions applied in determining the fair value of class of financial assets and liabilities, how changes in assumptions will affect the estimated fair value group of financial assets and liabilities
Not required	Paragraph 28 discloses the difference between fair value at initial recognition and amount determined by using a valuation technique; the accounting policy for recognising the difference in profit and loss and the aggregate difference yet to be recognised in profit and loss
Not required	Paragraph 29: no disclosure is required where carrying amount approximates fair value and where investment in equity market does not have a quoted market price in an active market or where fair value cannot be measured reliably
Required	Paragraph 30 requires entities exempted from paragraph 29(b,c) disclose the fact the financial instruments have not been disclosed, and why they cannot be measured reliably including information about the market for the instrument and how the entity intends to dispose them
Not required	Paragraph 31: disclose information that enable users of financial statements to evaluate and extent of risk associated with financial instruments
Not required	Paragraphs 32 to 42: disclose the risk arising from financial instruments and how they have been managed
Not required	In particular, paragraph 33 discloses each type of risk including how the exposure arises, the entity's objectives, policies and processes for managing the risk and methods to measure the risk and compare with previous period
Not required	Paragraph 34: disclose summary of quantitative data of each type of risk that an entity has an exposure to at reporting date

Not required	Paragraph 35: further disclosure is required if the disclosed quantitative data of risk during the period is misleading
Not required	Paragraph 36: classes of financial instruments are required to be disclosed, in particular: the entity's maximum exposure to credit risk, collateral held as security. For those financial assets which previously impaired are required to disclose information of the credit quality and the carrying amount
Not required	Paragraph 37 discloses an analysis of the age of financial assets and an analysis of impaired financial assets; and description of the collateral held by an entity as security
Not required	Paragraph 38 discloses the nature and carrying amount of assets obtained as collateral; policies for disposing of such assets when they are not readily cash convertible
Required	Paragraph 39 disclosure of maturity of financial liabilities and a description of how liquidity risk is managed
Not required	Paragraph 40 disclosure of sensitivity analysis for each type of market risk showing how profit or loss and equity are affected by changes of relevant risks variables; the methods and assumptions used to prepare such sensitivity analysis; changes of method and assumptions (if any) used from the prior periods and reasons behind those changes
Not required	Paragraph 41: disclosure of an sensitivity analysis which reflects the interdependencies between risks variables; the method and its objectives used to prepare the sensitivity analysis
Not required	An entity prepares a sensitivity analysis according to paragraphs 40 & 41 that is not representative of a risk inherent in a financial instrument. Paragraph 42 requires the entity to disclose reasons the entity believes the sensitivity analysis is unrepresentative

(6.3 cont)

Inventories	
Required	Paragraph 36(c): disclosure of carrying amount of inventories carried at fair value less costs to sell
Required	Paragraph 36(d): disclosure of inventories recognised as an expense during the period
Required	Paragraph 36(e): disclosure of the amount of any write-down of inventories recognised as an expense in the period in accordance with paragraph 34
Required	Paragraph 36(f): disclosure of any reversal of written down amount recognised as an expense in the period in accordance with paragraph 34
Not required	Paragraph 36(g): disclosure of the circumstances or events that led to write-down of inventories in accordance with paragraph 34
Investments in Associates	
Required	Paragraph 37(b): disclosure of summarised financial information of associates, including the aggregated amounts of assets, liabilities, revenues and profit or loss
Investment Property	
IFRS for SMEs have a separate sector for investment property. SMEs do not need to refer back to the full IFRS	According to the Framework for Differential Reporting, qualifying entities are given several concessions but those concessions are not stated in the Framework. Qualifying entities may have to account for investment property in accordance with the NZ IAS 40 and cost model in NZ IAS 16

(6.3 cont)

Property Plant and Equipment	
Not required	Qualifying entities can use the depreciation rate of financial report for income tax purpose, except for assets revalued in accordance with the revaluation model in NZ IAS16. If the exemption takes place, the entity is not required to comply with paragraphs 51 and 61 in the NZ IAS 16
Required	"Qualifying entities are not required to provide a reconciliation between the carrying amount at the beginning and the end of the period as required by paragraph 73(e). However, entities using this exemption must still comply with sub-paragraphs 73(e)(v) and 73(e)(vii) which require disclosure, by each class of property, plant and equipment, of impairment losses recognised, impairment losses reversed and depreciation" (p. 23)
Required	"Qualifying entities are not required to comply with paragraph 74(b) which requires disclosure of the amount of expenditure recognised in the carrying amount of an item of property, plant, and equipment in the course of its construction" (p. 23)
Not required	"Qualifying entities are not required to comply with paragraph 74(d) which requires disclosure of the amount of compensation from third parties for items of property, plant and equipment that were impaired, lost or given up that is included in profit or loss" (p. 23)
Not required	"Qualifying entities are not required to comply with paragraph 77(e) which requires disclosure of, for each revalued class of property, plant and equipment, the carrying amount that would have been recognised had the assets been carried under cost model" (p. 23)

(6.3 cont)

Intangible Assets	
Required	"Qualifying entities are permitted to expense all research and development costs in the period they are incurred. If an entities applies this concession it is not required to comply with paragraph 57" (p. 28)
Required	"Paragraph 118(d) which requires disclosure of the line item(s) of the statement of comprehensive income in which any amortisation of intangible assets is included" (p. 28)
Required	"Paragraph 118(e) which requires for each class of intangible assets a reconciliation of the carrying amount at the beginning and end of the period" (p. 28)
Required	"Paragraph 112(c) which requires disclosure in relation to intangible assets acquired by way of a government grant and initially recognised at fair value" (p. 28)
Not required	"Paragraph 124(a)(iii) which requires disclosure of the carrying amount that would have been recognised had the revalued class of intangible assets been measured after recognition using the cost model in paragraph 74" (p. 28)
Not required	"Paragraph 124(b) which requires disclosure of the amount if the valuation surplus that relates to intangible assets at the beginning and end of the period, indicating the changes during the period and any restrictions on the distribution of the balance to shareholders" (p. 28)
Not required	"when amortising software in accordance with paragraph 97, qualifying entities are permitted to use the rates adopted for income tax purposes in allocating the depreciable amount of the software over its useful life" (p. 28)

(6.3 cont)

Business Combination and Goodwill	
Not required	"Paragraph B64(d) which requires disclosure of the primary reasons for the business combination and a description of how the acquirer obtained control of the acquiree" (p. 30)
Required	"Paragraph B64(e) which requires a qualitative description of the factors that make up the goodwill recognised" (p. 30)
Not required	"Paragraph B64(g)(iii) which requires disclosure of an estimate of the range of outcomes for contingent consideration and indemnification assets" (p. 30)
Required	"Paragraph B64(h) which requires disclosures relating to acquired receivables" (p. 30)
Not required	"Paragraph B64(k) which requires disclosure of the amount of goodwill that is expected to be deductible for tax purposes" (p. 30)
Not required	"Paragraph B64(o)(ii) which requires disclosure of the valuation techniques and key model inputs used for determining the fair value of the non-controlling interest in an acquiree" (p. 30)
Not required	"Paragraph B64(q)(ii) which requires disclosure of the revenue and profit or loss of the combined entity as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period" (p. 30)
Not required	"Paragraph B67(a) which requires disclosure relating to business combinations that are incomplete for each material business combination or in aggregate for individually immaterial business combinations that are material collectively" (p. 30)

(6.3 cont)

Not required	"Paragraph B67(b)(ii) and (iii) which requires disclosures relating to changes in the range of outcomes and the valuation techniques and key model inputs used to measure contingent consideration for each material business combination or in aggregate for individually immaterial business combinations that are material collectively" (p. 30)
Required	"Paragraph B67(d) which requires a reconciliation of the carrying amount of goodwill at the beginning and end of reporting period for each material business combination or in aggregate for individually immaterial business combinations that are material collectively" (p. 30)
Provision and Contingencies	
Required	"Qualifying entities are not required to comply with paragraph 84(b) which requires disclosure of additional provisions made in the period, including increases to existing provisions" (p. 27)
Required	"Paragraph 84(c) which requires disclosure of amounts used (i.e. incurred and charged against the provision) during the period" (p. 28)
Not required	"Paragraph 84(e) which requires disclosure of the increase during the period in the discounted amount arising from the passage of time and the effect of any change in the discount rate" (p. 28)

(6.3 cont)

Revenue	
Not required	"Qualifying entities are exempt from accounting for Goods and Services Tax (GST) in accordance with NZ IAS 18)" (p. 25)
Required	"Paragraph 35(b) which requires disclosure of significant categories of revenue recognised during the period" (p. 25)
Not required	"Paragraph 35(c) which requires disclosure of the amount of revenue arising from exchanges of goods or services included in each significant category of revenue" (p. 25)
Borrowing Costs	
Required	Paragraph 29 (b)(c): disclose "the amount of borrowing costs capitalised during the period" and "the capitalisation rate used to determine the amount of borrowing costs eligible for capitalisation" (p. 26)
Impairment of Assets	
Required	"Paragraph 10 which requires an entity to undertake an annual assessment of impairment of an intangible asset with an indefinite useful life or intangible asset not yet available for use or goodwill acquired by a business combination" (p. 27). The impairment test is only taken place when the assets may be impaired at the end of the reporting period
Required	Paragraph 129,130: disclosure of segment information and information related to each material impairment loss recognised or reversed
Not required	"Paragraph 131 which requires disclosure of information for the aggregate impairment losses and the aggregate reversals of impairment losses recognised during the reporting period for which no information is disclosed in accordance with paragraph 130" (p. 27)

(6.3 cont)

Not required	"Paragraph 134 (c) which requires disclosure of the basis in which the unit's (group if units') recoverable amount has been determined" (p. 27)
Not required	"Paragraph 134(d) which requires disclosure of the assumptions and methodology used to determine value in use" (p. 27)
Not required	"Paragraph 134(e) which requires disclosure of the methodology used to determine fair value less costs to sell" (p. 27)
Not required	"Paragraph 134(f) which requires disclosure if information regarding the sensitivity if values to changes in key assumptions" (p. 27)
Not required	"Paragraph 135(c) which requires a description if the key assumption(s) in relation to goodwill or intangible assets with indefinite useful lives allocated across multiple cash generating units where the amount so allocated is not significant in comparison with the entity's total carrying amount of goodwill or intangible assets with indefinite useful lives" (p. 27)
Not required	"Paragraph 135(d) which requires a description of management's approach to determining the value(s) assigned to the key assumptions(s) in paragraph 135(c) and information about those assumptions" (p. 27)
Not required	"Paragraph 135(e) which requires disclosure of information regarding the sensitivity if values to changes in key assumptions" (p. 27)
Not required	"Paragraph 136 which provides additional guidance on the calculation of amounts disclosed in accordance with paragraph 134 and 135" (p. 27)

(6.3 cont)

Employee Benefits	
Required	"Paragraph 120A(c) which requires disclosure of a reconciliation of opening and closing balances of the present value of the defined benefit obligation" (p. 25)
Not required	"Paragraph 120A(d) which requires disclosure of an analysis of the defined benefit obligation into amounts arising from plans that are wholly unfunded and amount arising from plans that are wholly or partly funded" (p. 25)
Required	"Paragraph 120A(e) which requires disclosure of a reconciliation of the opening and closing balances of the fair value of plan assets and of the opening and closing balances of any reimbursement right recognised as an asset under paragraph 104 A" (p. 25)
Not required	"Paragraph 120(j) which requires disclosure for each major category of plan assets, which shall include, but is not limited to, equity instruments, debt instruments, property, and all other assets, of the percentage or amount that each major category constitutes of the fair value of the total plan assets" (p. 25)
Not required	"Paragraph 120A(k) which requires disclosure of amounts included in the fair value of plan assets for each category of the entity's own financial instruments; and any property occupied by, or other assets used by, the entity" (p. 25)
Not required	"Paragraph 120A(o) which requires disclosure of a sensitivity analysis in respect of medical costs" (p. 25)

(6.3 Cont)

Income Tax	
Income tax section of IFRS for SMEs derived from the full IFRS. However, it has been simplified to be appropriate for SMEs	"Qualifying entities are not required to account for income tax in accordance with NZ IAS 12" (p. 21)
"An entity shall disclose separately the major components of tax expense (income)" including deferred tax items. "An entity shall disclose information that enables users of its financial statements to evaluate the nature and financial effects of the current and deferred tax consequences of recognised transactions and other events" (s29.30, s29.31, s29.32)	"A qualifying entity may elect to account for income tax in accordance with NZ IAS 12 or it may use the taxes payable method" (p. 21). Under the taxes payable method, income tax expense in respect of the current period is equal to the income tax payable for the same period. The income tax effects of temporary differences, unused tax losses and unused tax credit under NZ IAS 12 are not recognised but may be disclosed in the notes." (p. 21). They are exempt from disclosure requirements stated in NZ IAS 12 insofar as they relate to disclosure of deferred tax expense (income) (paragraphs 81(a)(e)(f)(g)(h)(j)(k) and paragraph 82); they do not need to disclose the items listed in paragraphs 80(c)(d)(f) and (g) insofar as they relate to deferred tax; they do not need to comply with NZ IAS 1 paragraph 54(o); and they also do not need to "disclose the amount of income tax relating to each component of other comprehensive income as required by paragraph 81(ab) of NZ IAS 12" (p. 22)
Not required	"Qualifying entities are permitted to explain the relationship between tax expense (income) and accounting profit as required by paragraph 81(c) using gross amounts of the relevant items of income or expense". (p. 23)
Related Party Disclosures	
Required	"paragraph 16 which requires disclosure of key management personal compensation in total by category" (p.26)

(6.3 cont)

Leases	
SMEs are not required to provide a reconciliation between the total of future minimum lease payment at the end of the reporting, and their present value. However, SMEs are required to disclose a time period analysis of the total of future minimum lease payments, and their present value, at the end of the reporting period in accordance with the requirement in paragraph 20.13	"Paragraph 31(b) insofar as it requires a reconciliation between the total of future minimum lease payments at the end of the reporting, and their present value. Qualifying entities are still required to disclose a time period analysis of the total of future minimum lease payments, and their present value, at the end of the reporting period in accordance with the requirement in paragraph 31(b)" (p. 24)
Required	"Paragraph 31(c) which requires disclosure, by lessees in respect of finance leases of contingent rents recognised as an expense during the period" (p. 24)
Required	"Paragraph 31(e) which requires a general description of lessee's material finance leasing arrangements" (p. 24)
Required	"Paragraph 35(d) which requires a general description of the lessee's significant operating leasing arrangements" (p. 24)
Required	"Paragraph 47(a) which requires lessors to disclose a reconciliation between the gross investment in the finance lease at the end of the reporting period, and the present value of minimum lease payments receivable at the end of the reporting period and disclosure of the gross investment in the lease and the present value of minimum lease payment receivable classified into three time periods" (p. 24)

(6.3 cont)

Required	"Paragraph 47(d) which requires disclosure by lessors of the accumulated allowance for uncollectable minimum lease payment receivable in respect of finance leases" (p. 24)
Required	"Paragraph 47(e) which requires disclosure by lessors of contingent rents recognised as income in the period in respect of finance leases" (p. 24)
Required	"Paragraph 47(f) which requires disclosure by lessors of a general description of the lessor's material finance leasing arrangements" (p. 24)
Required	"Paragraph 56 which requires a range of disclosures by lessors in respects of operating leases" (p. 24)

6.2.5 Stage 5: Research Authorship

Qualifying entities receive full exemption of statement of cash flow which does not seem be in the favour of financial statements' users. From the users' perspective, the statement of cash flow provides the financial health of a business so it is essential to every business. Four basic financial statements: statement of financial position; statement of financial performance; statement of cash flow; and statement of changes in equity, are like "tools" to communicate a business' performance to users. Preparation of a financial statement of cash flow is not too difficult for a business, but it brings a lot of benefits to external users. Therefore, the full exemption of the statement of cash flow in the Framework for Differential Reporting may not be significant. The IASB (2007, BC96, p. 36) also noted:

> If a comparative balance sheet (with amounts for the beginning and the end of the reporting period) and an income statement are available, preparing a cash flow statement is not a difficult, time consuming or costly task. The accounting frameworks of most jurisdictions require broad groups of entities, including

SMEs, to prepare a cash flow statement. Moreover, the great majority of lenders and other users of SMEs' financial statements who have communicated with the Board—including particularly lenders and short-term creditors—indicated that the cash flow statement is useful to them.

Therefore, transparency of a business' financial reporting is a key benefit to a business.

The Framework for Differential Reporting reduces significant burdens for qualifying entities applying the NZ IFRS. However, compared to the extensive requirements of the IFRS which are around 2700 pages, the exemptions provided may not be enough for entities' sizes in New Zealand. The IFRS for SMEs appear to give a solution. The IFRS for SMEs are 232 pages long. Alex MacBeath states, "Unlisted businesses around the world who currently have to comply with full IFRS will be pleased to find that the new standard is about one tenth of the length of full IFRS and that the number of potential disclosure items will be nearer to 300 than the current 3000" (cited in Grant Thornton International Business Report, 2010, p. 1)

SMEs in New Zealand are in quite a broad range of sizes. Except for exempt and listed entities, all entities, in general, must comply with the Framework Differential Reporting. In other words, the Framework for Differential Reporting covers a wide range of entities. As discussed in the prior chapter, qualifying entities are subjected to the Framework for Differential Reporting and NZ IFRS. It appears to be burdensome for small businesses. Since a large proportion of exemptions stated in the Framework for Differential Reporting are also exempted in the IFRS for SMEs, IFRS for SMEs is a good "candidate" for SMEs in New Zealand. As the IASB affirmed, full IFRS is considered to be appropriate for small entities in 80 jurisdictions. There is no reason for the inappropriateness of IFRS for SMEs, which is simplified up to 85% from the full IFRS. In fact, before the IASB issued the proposed Exposure Draft for IFRS for SMEs, all entities (except for exempt companies) were going to adopt the NZ IFRS with some exemptions stated in the Framework for Differential Reporting. The emergence of the proposed Exposure Draft for IFRS for SMEs triggered the revision of financial reporting requirements for SMEs by the government.

Beside the advantages mentioned above, the IFRS for SMEs have a limitation. The limitation is from the wording used in the standards. Since it is shorter compared to the full IFRS, the IFRS for SMEs may lack in-depth instructions for users. Users may find it hard to understand or may not be sure of what exactly they have to do.

6.2.6 Stage 6 Philosophical /argumentative reflections

As discussed in stage 3, many jurisdictions around the world are moving towards the IFRS for SMEs as they increasingly recognise the need to enhance confidence of users on the financial accounts of SMEs. Australia and New Zealand are currently using the sector-neutral approach. The Framework for Differential Reporting is currently applicable to SMEs. The IFRS for SMEs may be a good option for New Zealand SMEs due to the advantages of the IFRS for SMEs themselves and the implied expectation of the FRSB for the IFRS for SMEs published. In addition, the emergence of the IFRS for SMEs appears to be a chance for New Zealand to move away from the sector-neutral standards and establish a transparent and specific set of standards for each size of business and each business sector in New Zealand.

If IFRS for SMEs is adopted, it is essential for the New Zealand standard setter to provide an additional document which provides some guidance for users of the IFRS for SMEs. Some instructions or in-depth explanation of any unclear paragraphs may be appropriate. Even though New Zealand already has the Framework for Differential Reporting, the IFRS for SMEs should help SMEs in New Zealand involved in buying/selling goods and services across national borders to initiate new relationships with customers and suppliers. The IFRS for SMEs also contribute to strengthening the financial reporting system in New Zealand. A future research question could be “What is the actual result of applying the IFRS for SMEs in practice?”

Chapter Seven

New Zealand Financial Reporting Framework: Past—Present—Future

7.1 Introduction

The NZ IFRS has largely been adopted by large issuers, subsidiaries of companies owned by overseas interests and the public sector. However, the NZ IFRS has not been similarly adopted by SMEs because it appears to be too complicated for a wide range of SMEs in New Zealand. In 2007, the IASB issued the proposed ED of the IFRS for SMEs. The proposal appeared to be a motive for countries to review their financial reporting requirements for SMEs and explore the possibilities of adopting the IFRS for SMEs. In Australia, the financial reporting regime for small proprietary companies is under revision. Also in New Zealand, the New Zealand FRSB has conducted several consultation meetings discussing financial reporting requirements for SMEs throughout the country. Feedback from those consultation meetings is as expected. The participants (practitioners, accountants and business owners), show their concerns over whether SMEs would be required to comply with a set of financial reporting standards, and if the IFRS for SMEs is better than the Differential Reporting regime.

The MED has commenced reviewing the Financial Reporting Framework aiming to restructure the financial reporting requirements to be appropriate for different business tiers, in particular, reviewing the financial reporting requirements for SMEs. The Financial Reporting Framework which proposes a set of concepts to underlie the preparation of GPFSs of all sectors: private, public, and not-for profit, is governed by the Financial Reporting Act 1993 (FRA).

7.2 Historical Narrative Inquiry Model

This chapter discusses the revision of the Framework for Financial Reporting. Figure 2.3 (the five-stage historical narrative inquiry model) is used to structure this chapter.

7.2.1 Stage 1: Contextual beginnings

The MED has released a discussion document on the Statutory Framework for Financial Reporting regarding which law should govern and who should be required to prepare the GPFSs. The revision of the MED contributes significantly to the New Zealand financial reporting system by clearly defining business tiers, and "who" should report "what" (Simpkins & Dale, 2009).

7.2.2 Stage 2: In-depth questions

How many tiers are appropriate for New Zealand? To fairly release the cost burden for SMEs, which tier should comply with which financial reporting standards? Should SMEs be regulated for producing GPFSs? Should New Zealand adopt the IFRS for SMEs?

7.2.3 Stage 3: Secondary resource analysis

In December 1991, the ARSB released seven Exposure Drafts (EDs): an Explanatory Foreword, Statement of Concepts, and Public Sector Guide to the Statement of Concepts, Disclosure of Accounting Policies, Presentation of Financial Reports and two statements relating to Differential Reporting, collectively titled "A Proposed Framework for Financial Reporting in New Zealand". By the time the Framework was finalised, the FRSs, approved by the ASRB, were to be sector-neutral and apply to all entities.

As mentioned above, the public-benefit entities are not within the scope of this research. For the profit-sector, there are basically two tiers in New Zealand except for exempt companies which comply with the Financial Reporting Order 1994.

Table 7.1: Two basic tiers in New Zealand

Tiers	Entity	Financial Reporting standards
1	Issuers	NZ IFRS
2	All others required to prepare the GPFSs	Framework for Differential Reporting

Source: Author (2010)

As shown in the above table and in Chapter 5, a large range of entities is covered by the Framework for Differential Reporting. It is important to examine the efficiency of the current New Zealand Framework for Differential Reporting. The findings in Chapter 5 show that, by increasing the size criteria, many large entities qualify for concessions. In other words, large unlisted entities benefit from the concessions, but smaller entities may find the cost burdensome. The main questions are addressed in 7.2.2 stage 2: In-depth questions.

The main objective of the review of the Statutory Framework for Financial Reporting is to establish a coherent, complete and consistent system which balances the benefits of financial reporting against the compliance costs. The Framework for Financial Reporting is underpinned by the coherent financial reporting principles which include public accountability, the economic significance, and the separation of ownership and management. It also has to be simple, clear and practicable as well as to promote New Zealand–Australia financial reporting convergence (MED, 2009b).

In the MED's discussion document, the following questions are used to get feedback from the participants.

- What constitutes a clear and consistent financial reporting framework?
- Which entities should be required by legislation to prepare financial statements?
- Should all of these financial statements be required to comply with GAAP? Should some entities be allowed to instead comply with a simplified, non-GAAP framework?
- Should some entities be exempted from a legislation requirement to prepare financial statements?
- How will any changes impact on entities operating in both New Zealand and Australia?

Unlike Canada and United Kingdom, the sector-neutral approach of New Zealand standard setters creates no separate standards for not-for-profit entities. This would result in a significant cost burden under the proposed IFRS regime (Baskerville & Cordery, 2006).

The MED document proposes changes to the standard setting infrastructure and discusses which entities should have financial reporting obligations. Together with the discussion document released by MED, the ASRB has simultaneously prepared a document showing possible accounting and assurance standards that would be implemented when MED proposed changes become enacted. The lines of responsibility are clearly distinguished.

- The Government and Parliament provide a legal decision on which entities will have reporting obligations (the “who” question).
- The ASRB should decide on the reporting obligations for each class of reporting entity (the “what” question).

Apart from having clear lines of responsibility, it is important for the accounting profession and the Government to be consistent with one another. There is an issue found in the definition of SMEs. According to the MED (2009a), SMEs are defined as entities with 19 employees or less. The Framework for Differential Reporting for entities applying the New Zealand Equivalent to IFRS as set by the ASRB has increased the size criteria to less than 50 employees. According to the Framework for Differential Reporting, an entity is considered as large if it exceeds two of the following criteria: employees number 50, total income is $20 million and total assets are $10 million (section 3.9).

For example: when an entity has 49 employees and total assets are less than $10 million or total income is less than $20 million, an entity is considered “not large” according to the Framework for Differential Reporting. There is no definition of a “not large” sized entity. If it is a “not large” sized entity, can it be a medium-sized entity? However, the MED define SMEs as those with fewer than 20 employees. There seems to be an inconsistency between the ASRB and the MED.

7.2.3.1 Legal perspective

The three key principles: public accountability; economic substance; and separation between owners and managers play a very important role for the healthy economic growth of New Zealand. It is essential for the readers to note that this research simply uses the collapse of finance companies in New Zealand to illustrate the importance of regulating the GPFS for unlisted entities. The research does not aim to go into economic analysis.

The collapse of 24 finance companies since 2006 could be used by the New Zealand accounting professions to examine if there is any co-relation with the financial reporting standards or the regulations (the list of failed companies is shown chronologically in Appendix 6).

Bill Wilson, finance lecturer at Massey University, has examined four finance companies: Provincial Finance, Bridgecorp, Five Star, and Geneva Finance in his research. He has found that the collapse of the finance company sector in New Zealand was actually from the weakness of corporate governance and regulation which was in place before the global crisis actually occurred (Parker, 2010).

Moreover, “the demise of Strategic Finance demonstrates once again that investors have been badly let down by our securities law, regulators, directors, management, the accounting profession and investment advisory industry” (Gaynor, 2010, p. 1). Strategic Finance, in the year 2000, got off the ground by successfully raising $41.6 million from the public. A year later, it purchased Strategic Mezzanine Partners with $6.2 million of goodwill that appeared on Strategic's balance sheet. This was an unusual deal because Strategic Mezzanine Partners was a highly geared finance company. Gaynor (2010) observed that there were graphs showing percentages of the first and second mortgages and other loans held by the company in 2002 and 2003. These graphs disappeared in the 2004 prospectus which resulted in difficulties for ensuring the composition and quality of the loan books. In addition, within a five-year period ending June 2007, total assets rose from $188.6 million to $696.1 million and net profit increased from $6.6 million to $30.0 million over the same period. These indicated an unusual growth of the company.

The business activities of any entities (regardless of their sizes) appear to have significant impact on the economy. They may create a crisis of confidence from investors in particular and affect the reputation of the New Zealand economy in general. Quite consistently with the three key principles of public accountability, economic significance and separation of owners and managers in the New Zealand Framework, managers must be accountable to the external users. As we can see, it is crucial to have companies to prepare proper GPFSs following an international set of standards where investors would feel more confident in the reliability, transparency, accuracy and comparability of the financial statements.

7.2.3.2 The accounting perspective

Business activities are no longer limited by a country's boundary. Due to extensive competition, companies tend to seek lower prices or better quality products or services overseas. Therefore, the financial statements are a key source of financial information for suppliers to evaluate the financial health of their buyers before making any transactions on credit. On the other hand, SMEs can also use their overseas suppliers' financial statements to assess the prospects of a viable long-term business relationship. Apart from bankers, venture capital firms also need reliable financial statements to make overseas investment decisions. In addition, credit ratings agencies, banks and other institutions need to rely on reported financial figures to develop credit ratings. Existing and potential investors who are not involved in managing the daily operation of an entity need reliable, comparable and understandable financial statements, especially when they are located in different jurisdictions.

7.2.3.3 Should the IFRS for SMEs be regulated?

Regulation is referred to as a way the government's power is addressed. In other words, regulation tells an entity what has to be done and the entity is penalised for not doing so (Wood, 2006). According to Drever, Stanton, & McGowan (2007), regulation comprises of elements: interventions of accounting professions in the production of financial information by reporting entities; a restriction on choice of accounting methods to achieve certain goal by accounting standards; and a control is exercised by an independent party who is not directly involved in the business activities.

Below are descriptions of some theories used for the justification for regulation.

Signalling theory

Signalling theory asserts that entities benefit from the transparency of their financial reporting because it signals how well an entity is performing. Good enterprises are encouraged to disclose their financial information through financial reports. An entity which is perceived as a poor performer is encouraged to improve their performance for a better reputation. The outcome is reflected in the disclosure of financial reports.

Therefore, signalling theory is primarily about the self-regulating system. Enterprises seem to be motivated to issue financial statements to lower its cost of capital (Drever, Stanton, & McGowan, 2007).

Public Interest theory

Even though signalling theory is described as a self-regulating system, it does rely on the economy which is a perfect and free. In fact, economic markets are hardly perfect or free and are instead comprise of various imperfections or uncertainties. According to public interest theory, regulation is issued to rectify these inefficient market practices and to serve the best interests of the general public. Public interest theory is based on two assumptions: economic markets are likely operating inequitably if it is unregulated because economic markets themselves are volatile; and no cost occurs for regulation.

Accounting standards are set to respond to the inequitable market for accounting or financial information. Public interest is reflected in the quantity and quality of financial information. The inefficient market can be seen in its over or under production of financial information (Drever et al, 2007).

Capture Theory

Evidence that interest groups are closely engaged in setting regulation is used to build capture theory. Capture theory holds that regulation is issued as interest groups attempt to take advantages of regulations to maximise their incomes or interests of their members. Capture theory holds the assumption that people tend to maximise their self-interest and do so rationally. In addition, there are two insights which capture theory is based on:

Firstly, a particular group can be benefited by the coercive power of the government. For example: by making accounting standards mandatory, auditors are benefitted. Accounting profession was claimed for not sufficiently adhering to standards. This problem can only be eliminated when the government backs for standards.

Secondly, regulation is perceived as a product governed by the laws supply and demand. All it means the value of regulation and cost of obtaining it are focussed to a particular group. Management can be an interest group because the standards are more likely to be lobbied by them. Eventually, the reporters of financial information are benefitted rather than users of that information (Drever et al, 2007)

Principal and Agent Theory

In contrast to listed entities, the sizes of SMEs are generally smaller and the owners are more likely to be involved in the business management. The agency conflict can be described as the behaviour of managers who do not act in the best interests of the owners. The agency conflict may be reduced when the owner is involved in management (Fama & Jensen, 1983; Jensen & Meckling, 1976). In other words, the opportunities for business growth and the associated risks with regard to the owner's interests are aligned. With personal involvement in management, the owner could reduce the incentive for opportunistic behaviour and ensure the manager will maximize the shareholder's wealth in its daily operation (Schultz, Lubatkin, Dino & Bucholtz, 2001). Carey (2008) suggests that the separation of ownership and management can cause agency conflict. With the owner's involvement, the incentive for opportunistic behaviour can therefore be reduced.

Bushfire theory

By taking into consideration the reaction of users and society to the 'failure' of regulatory processes, bushfire theory focuses on the political and public nature aspects of regulatory. Bushfire theory holds that regulation attempts to be issued from crises such as the collapse of Enron. These crises are unexpected occurred and they indicate inadequacies in accounting. Auditors are then blamed by the media. Solutions for the crises which can be new legislations or accounting standards may be issued. The resulting rules or regulation may not necessarily solve the causes of the crises but appear to please the general public for election purposes (Drever et al, 2007). For example: the collapses of high-profile companies such as Enron and WorldCom resulted in many new legislative initiatives worldwide, including the Sarbanes-Oxley Act in the US, and Corporate Law Economic Reform Program in Australia. As the result, the principle-based framework is the proposed answer for the crises. The rule-based framework was claimed to be easy to manipulate which causes the crises.

For instance, the collapse of Enron and the demise of international accounting firm Arthur Anderson are good evidence of the weaknesses of rule-based accounting standards. A former FASB staff who had written the accounting rules was hired by Enron for "gaming the system". The weaknesses of the rule-based approach make it too easy to get around it. It, in fact, provides the "road map" and "opportunities" for smart people without being caught, argued Enron employees. The following describes the "gaming system" process:

> "Say you have a dog, but you need to create a duck on the financial statements. Fortunately, there are specific accounting rules for what constitutes a duck: yellow feet, white covering, and orange beak. So you take the dog and paint its feet yellow and its fur white and you paste an orange plastic beak on its nose, and then you say to your accountants, 'This

> is a duck!" Don't you agree that it is a duck?' And accountants say, 'Yes, according to the rules, this is a duck.' Everyone knows that it's a dog, not a duck, but that does not matter because you have met the rules for calling it a duck" (McLean & Elkind, 2003, pp.142-143).

To ensure optimal accounting information is provided, regulation is required, especially in contractual situations. Regulation frequently evolves in accordance with its political nature and the regulator, in advance of setting the regulation, knows less about costs than does the regulated firm. However, adjustment occurs only when the compliance costs exceed the benefits (Brown, 1990). It is not easy to measure all economic benefits of increased information, thus full quantification of those costs is almost impossible. Furthermore, when the entity size is increased, it is more likely that the relative costs will reduce. The numbers of users of each individual SME are quite small. Therefore, comprehensive benefits may not be obtained, even when the relative cost of a fully compliant financial statement is low (Korea Accounting Standards Board, 2004). Ultimately, it is important to examine the number of users and their diversity, the existence of other non-financial information, as well as the concepts of relevance, reliability and timeliness of the financial information issued (Devi, 2003). Two benefits of regulation from the optimal provision have been acknowledged. They are "comparability across entities" and an "increase in confidence in the equity and lending markets" (Wolk, Francis, & Tearney, 1992).

7.2.4 Stage 4: Research Authorship

The findings from the Chapter 6 show the strength and advantages of having the IFRS for SMEs in New Zealand. The IFRS for SMEs plays an important role in allocating appropriate financial reporting standards to appropriate tiers. They could be shown as follows:

Table 7.2: Suggested future business tiers

Tiers	Entities	Financial Reporting Standards	GAAP Compliance
1	Issuers and large	NZ IFRS	Yes
2	Medium sized entities	IFRS for SMEs	Yes
3	Small entities	Framework for Differential Reporting	Yes
4	Exempt companies	Financial Reporting Order 1994	No

Source: Author (2010)

As discussed in Chapter 5, the Framework for Differential Reporting covers a wide range of SMEs. It may be beneficial for large entities but may be inappropriate for small entities. Therefore, the Framework for Differential Reporting may need to be reviewed to suit the small entities in New Zealand. In fact, the Framework for Differential Reporting for entities applying the equivalent to the IFRS may need to be reviewed because it has not been comprehensively reviewed but rolled over from the Framework for Differential Reporting for entities applying the FRSs. There are two alternatives available for New Zealand. The first is to modify the Framework for Differential Reporting to cater for different sizes of entities. The second alternative is to adopt the IFRS for SMEs. It may be a burden for New Zealand to maintain both the Framework for Differential Reporting and the IFRS for SMEs as shown in the table above.

As discussed in Chapter 6, if New Zealand adopts the IFRS for SMEs, the GPFSs prepared in New Zealand can be comparable to those in other countries if other countries adopt IFRS for SMEs. The advantages of the IFRS for SMEs are discussed in Chapter 6. It can be argued that the IFRS for SMEs may be a burden for small entities in New Zealand. In this author's opinion, 'yes', the IFRS for SMEs could be a burden for small entities but there is a solution. New Zealand has adopted the "top down approach" when designing the Framework for Differential Reporting (discussed in Chapter 5). The top-down approach could be used to create a Framework for Differential Reporting for entities applying the IFRS for SMEs. The advantage of this alternative is that the "pure" IFRS for SMEs is still maintained in New Zealand and the objectives of globalised accounting standards for SMEs can be achieved. The IASB selects the 50-employee entity as a guideline to decide the kinds of transactions, events and conditions that should be addressed in the IFRS for SMEs. Fifty employees were not used to form a quantitative definition of SMEs (IASB, 2007, BC45). In fact, the IASB leaves definitions of SMEs for jurisdictions to decide. Even though the MED defines SMEs as entities with less than 20 employees, the IFRS for SMEs can be applied for entities with 20 to 50 employees. It would not be cost effective if New Zealand decides to retain the Framework for Differential Reporting for entities with 20 to 50 employees. Since different countries have different sizes of SMEs as discussed in Chapter 1, the 50-employee guideline used in the IFRS for SMEs appears to be a parameter and it is a subject for each jurisdiction to decide. The MED may wish to change the definition of SMEs to 50 employees. Alternatively, the definition could remain unchanged but New Zealand should concentrate on "substance" (content that IFRS for SMEs can covers) over "form" (definition of SMEs).

Now the question is "Should the IFRS for SMEs be regulated?"

Owners who get involved in business operations are more likely to receive management reports rather than the GPFSs. Given contractual arrangements, owners would be able to request GPFSs. Increased flows of information would enhance the confidence of investors in SMEs because of the increase in transparency (Watts, 2003).

New Zealand PwC (2010) indicates there would be benefits to the New Zealand economy to be derived by requiring entities to prepare GPFSs. It is important for entities to keep and maintain good financial records and periodically prepare reliable financial statements. In their view, requiring entities to prepare financial statements (even if these are not published) would yield significant benefits to the country by smoothing and making transparent the operation of the economy. On the other hand, the preparation of reliable financial statements for SMEs is a basic step and that is almost on a par with the requirement to maintain proper accounting records. It is technically correct and quite a good opinion. Each individual entity is responsible for maintaining accurate and transparent accounting records, at least for tax purposes (filling tax returns). Technically, all the elements in the financial statements are taken out from the accounting records. Adding to the comments, PwC (2010) also believes that if a business is responsible and well run, they will continue to prepare annual financial statements. However, the less well operating and irresponsible will not. PwC also has a concern that without a requirement to prepare annual GPFSs, the New Zealand tax system will suffer. PwC (2010) provides the reason noted below for having reliable financial statements which:

i. are a fundamental element in the proper governance of companies;
ii. assist in the efficient operation of the tax system; and
iii. provide a common language for business when providing financial information (either on a mandatory or voluntary basis). Most businesses are required to provide financial information to a range of users and it is efficient from an economic perspective if that information is written in a common language and is readily available (p. 4).

In addition, experience from the collapse of a series of finance companies seems to suggest that, except for very small companies (exempt companies), all of the entities should be prepared better by preparing GPFSs and comply with "quality" financial reporting standards. By doing so, the New Zealand financial system in particular, and the New Zealand economy in general, would be strengthened and transparent. It may be fair to say that the crisis in users' financial statements is at the root of the financial crisis. Therefore, to enhance confidence in the financial statements is very important. According to the agency theory, the manager is responsible for maximising the owners' wealth. It is fair to say that the managers also have work for the benefit of the general public because the damage of the crisis caused to the general public is to be significant. The theories of regulation discussed above also suggest that the IFRS for SMEs should be regulated.

5.2.5 Stage 5: Philosophical/ argument reflection

Since New Zealand intends to move away from sector-neutral accounting standards (Perry, 2006), it appears to be essential for New Zealand to have a 'solid' and globally recognised set of financial reporting standards for each sector. As discussed in Chapter 6, the IFRS for SMEs have certain advantages that New Zealand could consider. A question was raised by the New Zealand PwC in the letter responding to the MED's discussion documents, which questioned the role of the standard setters in New Zealand if both IFRS and IFRS for SMEs are adopted. I believe this question is a good one. As discussed above, there are two alternatives for New Zealand to move the accounting profession forward. New Zealand standard setters play a very important role in making appropriate adjustments to the relevant accounting standards to suit entities in different tiers.

The research shows that it is feasible for New Zealand to adopt the IFRS for SMEs. It may give the New Zealand accounting system a "new look" with an expectation for a consistent, transparent and globally recognised accounting system in the future.

Chapter Eight

Research Summary and Conclusion

Table 8.1: Summary of the research

<table>
<tr><td>Research Question</td><td colspan="2">What was occurring during the period of development of New Zealand accounting standards for SMEs and how appropriate is it for New Zealand to adopt the IFRS for SMEs?</td></tr>
<tr><td rowspan="2">Chapter 3</td><td>In-depth questioning</td><td>What is sector neutrality?
Why does New Zealand adopt a sector-neutral standards approach?
How important are sector-neutral standards in New Zealand?</td></tr>
<tr><td colspan="2">Sector neutrality :
1. is defined as the way economic transactions are treated regardless of the type of entities undertaking them
2. resulted from the reforms of the New Zealand government in 1984
3. brought New Zealand’s reputation to international level
4. remains the most effective and efficient approach
5. may not be appropriate when transactions of each sector become more complicated
6. may obstruct the New Zealand accounting profession from setting appropriate standards for each sector
7. may cause IFRS in New Zealand being different from the rest of the world because IFRS is modified to accommodate public benefit entities</td></tr>
</table>

<table>
<tr><td rowspan="2">Chapter 4</td><td>In-depth questions</td><td>What are the differences between the sector-neutral standards and the international accounting standards?

What are the impacts of the sector-neutral standards on the globalisation objective?

What is the future of the sector-neutral standards in New Zealand?</td></tr>
<tr><td colspan="2">1. there are three impacts of the sector-neutral approach to the Conceptual Framework, impacts on setting on terminology, and impacts on setting on the timeliness of the due process
2. on behalf of the FRSB, Perry stated that New Zealand will continue to use the sector neutral approach and attempt to address the needs of users of Public Benefit Entities financial statements
3. it would not be difficult for New Zealand to develop a separate set of standards for public benefit entities
4. it may be even easier than attempting to aggregate standards of different sectors into one set of standards
5. the compliance costs would be increased if multiple sets of standards are maintained
6. the barriers would also occur for accountants to work across sectors. Public benefit entities find difficult to attract qualified accountants
7. it is important for New Zealand to move away from the sector-neutral approach and concentrate on comprehending the needs of each sector, e.g., education on public benefit sector</td></tr>
<tr><td rowspan="2">Chapter 5</td><td>In-depth questions</td><td>What is the historical development of the Framework for Differential Reporting?</td></tr>
<tr><td colspan="2">1. Objective of establishing the Framework for Differential Reporting:
• The Framework for Differential Reporting is established to provide some concessions for entities which are required to prepare GPFSs that comply with NZ GAAP
• Costs and benefits are used as criterion to differentiate if an</td></tr>
</table>

	entity has qualified for differential reporting exemptions 2. Historical development of the Framework for Differential Reporting: 2a. In February 1994, the Framework for Differential Reporting for entities applying FRSs was firstly promulgated. To qualify for exemptions, two out of three must be met: i. An entity has no public accountability ii. All of an entity's owners are members of the governing body; or iii. An entity is not "large" according to two of the three size criteria: revenue, total assets, and number of employees. Size criteria are regularly reviewed: In 1994, the revenue threshold was $2.5 million; total assets threshold was $1.5 million; employees were 20 In 1997, the revenue threshold was $5 million; total assets threshold was $2.5 million, employees were fewer than 20 2b. In 2005, the Framework for Differential Reporting for Entities Applying the NZ IFRS was developed on the basis of the Framework for Differential Reporting for entities applying NZ FRSs Size criteria: (i) total income of $20 million; (ii) total assets of $10 million; or (iii) 50 employees 3. Discussion (i) Decisions of selecting which entities fall into the SMEs, range would have an influence on the cost–benefit argument (ii) When public accountability is used as a basis, the size of

<table>
<tr><td></td><td colspan="2">an entity becomes irrelevant. In particular, a small (with few employees) publicly accountable entity would bear high accounting costs

(iii) A large entity but no public accountability will be granted exemptions

(iv) Therefore, the differential reporting framework has been used to balance the cost of fully complying with regulation and expected economic benefits to SMEs

(v) Since size criteria are increased, more large entities qualify for exemptions

(vi) The ‘roll-over’ of the Framework for Differential Reporting for Entities Applying the NZ IFRS implies that the FRSB was waiting for the upcoming issue of a global set of standards, the IFRS for SMEs

(vii) There is a possibility of adoption of IFRS for SMEs</td></tr>
<tr><td rowspan="2">Chapter 6</td><td>In-depth questions</td><td>What are the advantages and disadvantages of the IFRS for SMEs compared to the New Zealand Framework for Differential Reporting?

How does the IFRS for SMEs fit in New Zealand environment?</td></tr>
<tr><td colspan="2">1. Advantages:

(i) IFRS for SMEs is a stand-alone document with 85% shorter than the full IFRS, significant reduction of treatments and disclosure requirements

(ii) IFRS for SMEs enhances confidence of users on SMEs’ accounts

(iii) If New Zealand adopts the IFRS for SMEs, financial</td></tr>
</table>

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<tr><td></td><td colspan="2">
statements prepared by SMEs in New Zealand can be comparable and understandable by overseas investors
(iv) IFRS for SMEs enhances transparency of financial statements
(v) IFRS for SMEs is designed particularly for SMEs
2. Disadvantages:
Since IFRS for SMEs is shorter compared to the full IFRS, it may lack in-depth instructions for users. Users may find it hard to understand or may not be sure of what exactly they have to do
3. IFRS for SMEs fits in New Zealand environment
(i) The Framework for Differential Reporting reduces significant burden for qualifying entities applying the NZ IFRS. However, compared to the extensive requirements of the IFRS which are around 2700 pages, the exemptions provided may not be enough for entities’ sizes in New Zealand
(ii) By using the Framework for Differential Reporting, the entities have to refer back to the full IFRS
(iii) The Framework for Differential Reporting for Entities Applying the NZ IFRS was not comprehensively reviewed to reflect the actual needs of users
(iv) The majority of the business community in New Zealand are SMEs. MED (2009) defines SMEs as those with less than 20 employees. The Framework for Differential Reporting covers entities with less than 50 employees.
</td></tr>
<tr><td>Chapter 7</td><td>In-depth questions</td><td>
How many tiers are appropriate for New Zealand?
To fairly release cost burden for SMEs, which tier should comply with which financial reporting standards?
Should SMEs be regulated for producing GPFSs? Should New Zealand adopt the
</td></tr>
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<table>
<tr><td rowspan="2"></td><td></td><td>IFRS for SMEs?</td></tr>
<tr><td colspan="2">Except for exempt companies complying with non-GAAP Financial Reporting Order, there are two basic set of standards applicable to entities producing general purpose financial statements in New Zealand:

(i) NZ IFRS and
(ii) Framework for Differential Reporting.

Three key principles: public accountability, economic significance and separation of owners and managers in the New Zealand Framework

Large unlisted entities are advantaged by the Framework for Differential Reporting. Small entities may find cost burdensome

Sector-neutral approach of New Zealand standard setters creates no separate standards for not-for profit entities. This would result a significant cost burden under the proposed IFRS regime

MED reviews the Framework for Financial Reporting which comprises financial reporting requirements for SMEs. No final result has yet emerged. MED may need to revise the definition of SMEs when they restructure tiers and their financial reporting standards

It is hard for New Zealand to maintain two sets of standards: IFRS for SMEs and Framework for Differential Reporting. Even though IFRS for SMEs may be a burden for small entities, there is a solution for New Zealand. If New Zealand decides to adopt the IFRS for SMEs, New Zealand can adopt the “top down approach” to establish a Framework for Differential Reporting for entities applying the IFRS for SMEs.

The theories of regulations recommend IFRS for SMEs to be regulated.</td></tr>
</table>

To recap, the research question is “What was occurring during the period of development of New Zealand accounting standards for SMEs and how appropriate is it for New Zealand to adopt the IFRS for SMEs?” It is broken into sub-research questions in each chapter to address what was happening in each period of development of New Zealand accounting standards for SMEs as shown in Table 8.1 above.

New Zealand and Australia are two countries using a sector-neutral approach for standards setting. The benefits of sector-neutral standards are widely acknowledged as it has enhanced New Zealand international reputation as a standard setter. The emergence of sector-neutral standards was in conjunction with the financial reforms of the New Zealand government. In 1992, the FRSB adopted the sector-neutral approach to standard setting in New Zealand.

Sector-neutral standards may no longer be appropriate for New Zealand because of the increasingly complicated business activities in each sector. A single set of financial reporting standards for each sector appears to be practical to capture and monitor business events by restructuring disclosure requirements. The relationship between performance information and accountability is more likely to be emphasized in the standards for each sector. New Zealand institutional structures are well designed to synthesize international materials to generate a single set of standards neutral to both sectors and approve these standards as New Zealand regulation. Except for the Financial Reporting Order 1994 which is used by exempt companies, there are two set of standards available: NZ IFRS and Framework for Differential Reporting.

NZ IFRS became mandatory to New Zealand reporting entities in January 2007. The Framework for Differential Reporting for entities applying New Zealand Equivalent to IFRS was established to provide some exemptions from some of financial reporting requirements to entities that meet certain requirements. The changes of size criteria (see Table 8.1 above) have resulted in more large entities qualifying for Framework for Differential Reporting. This is obviously advantageous for large unlisted entities and disadvantageous or burdensome for small entities. The majority of New Zealand business entities are SMEs. SMEs have a significant effect on the New Zealand economy. They total 97.1% of New Zealand entities, account for 40.7% of the economy’s total output and for 30.7% of employees in New Zealand. Compared to other countries, the EU in particular, the sizes of SMEs in New Zealand are quite small. The medium-sized entities in New Zealand are just small or even micro-sized entities in countries in EU. Therefore, it is essential for New Zealand to establish different tiers with appropriate sets of standards applied to each of them. In September 2007, the Minister of Commerce announced that government was going to review financial reporting requirements for SMEs. This resulted in the delay in adoption of NZ IFRS for SMEs. Costs and benefits of implementing a set of standards are commonly a major concern for standard setters and business owners. In fact, it is a subject matter commonly discussed in the literature and no consistent finding has been found. The crisis in 2008 has again enhanced the importance of transparent financial reporting standards for business entities, in particular SMEs. It is essential to build up the confidence of users on SMEs' accounts.

IFRS for SMEs is a global stand-alone set of standards and designed for unlisted entities. When comparing the IFRS for SMEs with the Framework for Differential Reporting, the IFRS for SMEs seems appropriate for the New Zealand business community. The Framework for Differential Reporting for entities applying IFRS for SMEs can be developed to accommodate very small entities by using the "top-down approach". The current Framework for Differential Reporting covers a wide range of SMEs and the qualifying entities have to refer back to the NZ IFRS. It is too burdensome for small entities. In addition, no comprehensive review was taken place when the Framework for Differential Reporting for entities applying NZ IFRS was developed. Therefore, it does not reflect the actual users' needs and needs costs and benefits consideration.

By examining the development of accounting standards in New Zealand, this research shows that the current Framework for Differential Reporting is not appropriate for SMEs in New Zealand. The revision of the Framework for Financial Reporting is taking place and it is expected to change the situation of New Zealand SMEs to where business structures (tiers) and financial reporting standards are clearly classified to appropriate tiers. The trend of the accounting standards development in New Zealand shows that it is a time for New Zealand to move away from the sector-neutral approach and IFRS for

SMEs is a destination of SMEs in New Zealand. Down the track, the adoption of IFRS for SMEs may result in two classes of accountants in New Zealand: one specialised in IFRS and another in IFRS for SMEs. When IASB makes changes to the IFRS, the IFRS for SMEs may not always automatically be updated. In other words, full IFRS and IFRS for SMEs may not be updated at the same time. IFRS for SMEs accountants may not focus on the changes or updates on the IFRS. Therefore, they may not be as updated as IFRS accountants. When an entity grows from the SMEs range to large entities, the entity encounters significant changes in measurement and disclosures. The transition does not seem to be a big problem because IFRS for SMEs is developed on the basis of the full IFRS. According to McMahon and Davies (1992), the transition from IFRS for SMEs is probably not a major concern because SMEs tend to avoid growth. For IFRS for SMEs accountants, workshops organised by the accounting professional may keep them up to dated from any changes of IFRS.

Limitations

This research uses secondary documents as primary data to examine the historical development of accounting standards in New Zealand. However, the research does take into consideration direct responses of business owners about possibilities of adopting IFRS for SMEs in New Zealand. No interview with business owners was conducted. The research makes use of business owners' feedback from secondary documents. This leaves scope for future research in this area.

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Appendix 1: Time for Due Process

Number of months between issue of exposure draft and issue of final standard

	Pre- 1992	Months	Post-1992	Months
FRS-2: Presentation of Financial Reports	SSAP 1	23	ED 65	29
FRS-3: Property, Plant and Equipment (Including Depreciation)	SSAP 4 and 6 ED 28 ED 50 and 50A	89 15 26	ED 82	36
FRS-36: Accounting for Acquisitions Resulting in Combinations of Entities or Operations	SSAP 7	17	ED 83	40
FRS-37: Consolidating Investments in Subsidiaries	ED 16	17	ED 84	40
FRS-38: Accounting for Investments in Associates	ED 38 ED 49 and 49A	12 8	ED 81	40
FRS-9: Information to be disclosed in Financial Statements	ED 17	18	ED 67	16
FRS-15: Provisions, Contingent Liabilities and Contingent Assets	ED 24	21	ED 78 and 86	66

Appendix 2: Stakeholders' Discussion in Chronological Order

Year	Stakeholders	Title	Pages
1997	Chartered Accountants	Promulgations Framework for Differential Reporting	54
	Chartered Accountants	The Framework for Differential Reporting is an integral part of requirements for preparation of financial reports in New Zealand	14-17
2003	Chartered Accountant	New Zealand slow to adopt new accounting standards	46
2004	Chartered Accountants	Differential reporting-FRSB issues Exposure Draft	47
	Chartered Accountants	Financial Reporting Act compliance	48
	Chartered Accountants	At the crossroads	26-29
	Chartered Accountants	Implications of IFRS for sector-neutral standard setting	21-24
2005	Chartered Accountants	New Zealand Framework a key component in financial reporting	33-35
2006	Chartered Accountant	Work together to get the right answers	4
2006	Lecturers	Small GAAP: a large jump for the IASB	1-32
2006	Chartered Accountant	Financial reporting by SMEs	27-30
2007	ASBR	Delay of the Mandatory Adoption of NZ IFRS for Certain Small Entities	1-4
	Chartered Accountants	Future of financial reporting requirements for SMEs	12-14
	IASB	Draft implementation guidance-IFRS	1-80

		for SMEs	
	IASB	Basis for conclusions on exposure draft-IFRS for SMEs	6-46
	Institute of Chartered Accountants of New Zealand	Framework for Differential Reporting	20-32
	Chartered Accountant	Where to for accounting for…most of New Zealand	4
	Lecturers	Sector-neutral Accounting Standards: A Ten-year Experiment	1-19
	Lecturers	How IFRS has destabilized financial reporting for UK non-listed entities	394-408
	Chartered Accountant	IFRS for SMEs: A Brave New World	10-11
	Certified Practice Accountants	International Standards for Small and Medium-Sized Entities	38-40
	Certified Practice Accountants	Greater certainty, clarify and cost-effectiveness	59
	Certified Practice Accountants	More complex and costly financial reports	58
	Chartered Accountants	Mandatory adoption of international standards delayed for small entities	40-42
	Lecturer, Accounting Standards Board of Great Britain and Ireland	IASB's Exposure Draft on new international standard for SMEs	16-18
	Ministry of Economic Development	SMEs in New Zealand: Structure and Dynamics	1-18
	Lecturer	Is there a solid empirical foundation for the IASB's draft IFRS for SMEs?	1-29
	Chartered Accountant	IASB's IFRS for SMEs	30-32
	New Zealand Institute of Chartered Accountants	Request for comment on "IASB Exposure Draft of a Proposed IFRS for SMEs"	1-8

2008	Chartered Accountants	Standard-setting alive well in New Zealand after IFRS	18-19
	Chartered Accountants	Review of the financial reporting framework	4
	Lecturers, Chartered Accountants	Evidence on the Impact of IFRS in New Zealand	1-26
	Ireland Accounting Standards Board	Accounting for SMEs: The European Debate Goes On	8
	Chartered Accountants	IFRS for Private Entities: A Practical Guide	29-31
2009	Chartered Accountants	Future standards	42-43
	Lecturers	UK small owner-managed businesses: accounting and financial reporting needs	289-302
	IASB	IASB publishes IFRS for SMEs	1-2
	Ministry of Economic Development	The Statutory Framework for Financial Reporting	1-81
	Chartered Accountant	New Zealand on the cusp	26
	Chartered Accountant	Up for debate	27
	IASB	IFRS for SMEs	1-109
	Chartered Accountant	Have a little faith	28
2010	PwC	The statutory framework for financial reporting	1-14
	Chartered Accountants	Presentation on “NZ IFRS Update for SMEs”	1-42

Appendix 3: Full Compliance with NZ FRSs

Standards	Description
FRS-1	Disclosure of Accounting Policies
FRS-2	Presentation of Financial Reports: This financial reporting standard must be followed by all entities. While there are certain exemptions for qualifying entities within FRS-2 these all relate to exemptions provided by other standards
SSAP-3	Accounting for Depreciation
FRS-5	Events After Balance Date
SSAP-6	Materiality in Financial Statements
FRS-7	Extraordinary Items and Fundamental Errors
FRS-20	Accounting for Shares Issued Under a Dividend Election Plan: All companies must comply with FRS-20
SSAP-21	Accounting for the Effects of Changes in Foreign Currency Exchange Rates
SSAP-25	Accounting for Interests in Joint Ventures and Partnerships
FRS-26	Accounting for Defeasance of Debt
FRS-27	Right of Set-Off
FRS-29	Prospective Financial Information
FRS-32	Financial Reporting by Superannuation Schemes
FRS-33	Disclosure of Information by Financial Institutions
FRS-34	Life Insurance Business
FRS-35	Financial Reporting of Insurance Activities
FRS-36	Accounting for Acquisitions Resulting in Combinations of Entities or Operations
FRS-37	Consolidating Investment in Subsidiaries
FRS-38	Accounting for Investments in Associates

Appendix 4: Partial Exemptions from NZ FRSs

Standards	Descriptions	Partial Exemptions from NZ FRSs
FRS-3	Accounting for Property, Plant and Equipment	Qualifying entities have options to choose any of exemptions from the requirements of FRS-3 (a)(b)(c)
FRS-4	Accounting for Inventories	Qualifying entities are exempted from sub-classifying inventory as required in para 5.29(b)(ii) of FRS-4
FRS-9	Information to be Disclosed in Financial Statements	Qualifying entities are given several disclosure concessions identified by an asterisk in the standard
FRS-13	Accounting for Research and Development Activities	Qualifying entities are not required to comply with section 5. Where this exemption is applied, all research and development costs are treated as expense within the period it incurred
FRS-14	Accounting for Construction Contracts	Qualifying entities need to comply with just para 4.1 which states that profit on all construction contracts may be recognized by the completed method
FRS-15	Provisions, Contingent Liabilities and Contingent Assets	Qualifying entities are exempted from making disclosures in their financial statements of the requirements in FRS-15 denoted with an asterisk
SAAP-17	Accounting Investment Properties and Properties Intended for Sale	Qualifying entities which recognize investment property revaluation or development margins shall comply with all provisions of SSAP-17. Other qualifying entities need not account for investment properties and properties intended for sale in terms of SSAP-17
SSAP-18	Accounting for Lease and Hire Purchase Contract	Qualifying entities are exempt from para 5.15(b) and may satisfy the requirements of para 5.15(c) and 5.17 by disclosing lease liabilities and commitments classified into

Appendix 4 (cont)

		current and noncurrent amount only
FRS-9	Accounting for Goods and Service Tax	Qualifying entities have an option to either recognize revenue and expense items with GST (gross) or exclude GSR (net), provided that section (a) and (b) are complied with
FRS-21	Accounting for the Effects of Changes in Foreign Currency Exchange Rates	FRS-21 (a) (b) provide some exemptions for qualifying entities
SSAP-22	Related Party Disclosure	Qualifying entities are just need to comply with SSAP-22, para 5.1 (a) and (b)
FRS-24	Interim Financial Statements	All reporting entities have to comply with FRS-24. Qualifying entities may apply differential reporting exemptions available under other specific financial reporting standards in addition to the specific disclosure exemptions identified in the Standard.
FRS-30	Reporting Share Ownership Arrangements Including Employee Share Ownership Plans	Qualifying entities are exempted from the requirements of paragraph 5.6 of FRS-30

Appendix 5: Partial Exemptions from IFRS

Standards	Description
NZ IAS 1	Presentation of Financial Statements
NZ IAS 2	Inventories
NZ IAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
NZ IAS 11	Construction Contracts
NZ IAS 12	Income Taxes
NZ IAS 16	Property, Plant and Equipment
NZ IAS 17	Leases
NZ IAS 18	Revenue
NZ IAS 19	Employee Benefits
NZ IAS 21	The Effects of Changes in Foreign Exchange Rates
NZ IAS 23	Borrowing Costs
NZ IAS 24	Related Party Disclosure
NZ IAS 28	Investment in Associates
NZ IAS 36	Impairment Assets
NZ IAS 37	Provisions, Contingent Liabilities and Contingent Assets
NZ IAS 38	Intangible Assets
NZ IAS 40	Investment Property
NZ IAS 41	Agriculture
NZ IFRS 3	Business Combination
NZ IFRS 5	Non-current Assets Held for Sale and Discontinued Operations

Appendix 5 (cont)

NZ IFRS 7	Financial Instrument: Disclosure
FRS 42	Prospective Financial Information
NZ SIC-27	Evaluating the Substance of Transactions Involving the Legal Form of a Lease
NZ SIC-32	Intangible Assets-Website Costs
NZ IFRIC 7	Applying the Restatement Approach under NZ IAS 29 Financial Reporting in Hyperinflationary Economies
NZ IFRIC 15	Agreement for the Construction of Real Estate

Appendix 6: Chronological order of collapsed finance companies in New Zealand

NZ Herald (2008). The sorry list of finance company failures. (2008). Retrieved 7 June 2010 from http://www.nzherald.co.nz/personal-finance/news/article.cfm?c_id=12&objectid=10517059

Time	Name
May-06	National Finance 2000
Jun-06	Provincial Finance
Aug-06	Western Bay
2-Jul-07	Bridgecorp
21-Aug-07	Nathans Finance
29-Aug-07	Property Finance
30-Aug-07	Five Star Consumer Finance
4-Sep-07	LDC Finance Ltd
5-Sep-07	Finance and Investments
4-Oct-07	Clegg and Co Finance
Oct-07	Beneficial Finance
16-Oct-07	Geneva Finance
29-Nov-07	Capital and Merchants Investments
17-Dec-07	Numeria Finance
14-Mar-08	MFS Boston
3-Apr-08	Lombard Finance and Investments
15-Apr-08	Kiwi Finance
13-May-08	Cymbis New Zealand
18-May-08	MFS Pacific Finance
28-May-08	Belgrave Finance
6-Jun-08	IMP Diversified Fund
18-Jun-08	Dominion Finance Holdings
24-Jun-08	St Laurence Ltd
25-Jun-08	Dorchester

Appendix 7: Full Compliance for entities applying the NZ IFRS

Standards	Description	IFRS for SMEs
NZ IAS 10	Events after the Reporting Period	x
NZ IAS 20	Accounting for Government Grants and Disclosure of Government Assistance	x
NZ IAS 26	Accounting and Reporting by Retirement Benefits Plans	
NZ IAS 27	Consolidated and Separate Financial Statements	x
NZ IAS 29	Financial Reporting in Hyperinflationary Economies	x
NZ IAS 30	Disclosures in the Financial Statements of Banks and Similar Financial Institutions	
NZ IAS 31	Interest in Joint Ventures	x
NZ IAS 32	Financial Instruments: Presentation	x
NZ IAS 33	Earnings per shares	
NZ IAS 34	Interim Financial Reporting	
NZ IAS 39	Financial Instruments: Recognition and Measurement	
NZ IFRS 1	First-time Adoption of NZ IFRS	
NZ IFRS 2	Share-based payment	x
NZ IFRS 4	Insurance Contracts	
NZ IFRS 6	Exploration for and Evaluation of Mineral Resources	
NZ IFRS 8	Operating Segments	
FRS-43	Summary Financial Statements	
NZ SIC-7	Introduction of the Euro	
NZ SIC-10	Government Assistance-No Specific Relation to Operating Activities	
NZ-SIC-12	Consolidation-Special Purpose Entities	
NZ-SIC 13	Jointly controlled entities-Non Monetary Contributions by Ventures	
NZ-SIC-15	Operating Leases-Incentives	
NZ-SIC-21	Income Taxes-Recovery of Revalued Non-Depreciable Assets	
NZ-SIC-25	Income Taxes-Changes in the Tax Status of an Entity or its Shareholders	

Appendix 7 (cont)

Standards	Description	IFRS for SMEs
NZ-SIC-29	Disclosure-Service Concession Arrangements	
NZ-SIC-31	Revenue-Barter Transactions Involving Advertising Services	
NZ-IFRIC 1	Changes in Existing Decommissioning Restoration and Similar Liabilities	
NZ-IFRIC 2	Members' Shares in Co-operative Entities and Similar Instruments	
NZ-IFRIC 4	Determining Whether an Arrangement Contains a Lease	
NZ-IFRIC 5	Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds	
NZ-IFRIC 6	Liabilities Arising from Participating in a Specific-Market-Waste Electrical and Electronic Equipment	
NZ-IFRIC 8	Scope of NZ IFRS 2	
NZ-IFRIC 9	Reassessment of Embedded Derivatives	
NZ-IFRIC 10	Interim Financial Reporting and Impairment	
NZ-IFRIC 11	NZ IFRS 2-Group and Treasury Share Transactions	
NZ-IFRIC 12	Service Concession Arrangements	
NZ-IFRIC 13	Customer Loyalty Programmes	
NZ-IFRIC 14	NZ IAS 19- The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction	
NZ-IFRIC 16	Hedges of a Net Investment in a Foreign Operation	

Appendix 8: IFRS for SMEs is sourced from the full IFRS from which the principles in each sector of the IFRS for SMEs were derived

	Section in the *IFRS for SMEs*	**Sources**
	Preface	*Preface to International Financial Reporting Standards*
1	*Small and Medium-sized Entities*	—
2	*Concepts and Pervasive Principles*	IASB *Framework*, IAS 1 *Presentation of Financial Statements* as revised in 2007
3	*Financial Statement Presentation*	IAS 1
4	*Statement of Financial Position*	IAS 1
5	*Statement of Comprehensive Income and Income Statement*	IAS 1
6	*Statement of Changes in Equity and Statement of Comprehensive Income and Retained Earnings*	IAS 1
7	*Statement of Cash Flows*	IAS 7 *Statement of Cash Flows*
8	*Notes to the Financial Statements*	IAS 1
9	*Consolidated and Separate Financial Statements*	IAS 27 *Consolidated and Separate Financial Statements* as amended in 2008
10	*Accounting Policies, Estimates and Errors*	IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*
11 and 12	*Basic Financial Instruments* and *Other Financial Instruments Issues*	IAS 32 *Financial Instruments: Presentation*, IAS 39 *Financial Instruments: Recognition and Measurement*, IFRS 7 *Financial Instruments: Disclosures*
13	*Inventories*	IAS 2 *Inventories*
14	*Investments in Associates*	IAS 28 *Investments in Associates*
15	*Investments in Joint Ventures*	IAS 31 *Interests in Joint Ventures*
16	*Investment Property*	IAS 40 *Investment Property*
17	*Property, Plant and Equipment*	IAS 16 *Property, Plant and Equipment*
18	*Intangible Assets other than Goodwill*	IAS 38 *Intangible Assets*
19	*Business Combinations and Goodwill*	IFRS 3 *Business Combinations* as revised in 2008
20	*Leases*	IAS 17 *Leases*

Appendix 8 (cont)

21	*Provisions and Contingencies*	IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*
22	*Liabilities and Equity*	IAS 1, IAS 32
23	*Revenue*	IAS 11 *Construction Contracts*, IAS 18 *Revenue*
24	*Government Grants*	IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance*
25	*Borrowing Costs*	IAS 23 *Borrowing Costs*
26	*Share-based Payment*	IFRS 2 *Share-based Payment*
27	*Impairment of Assets*	IAS 2, IAS 36 *Impairment of Assets*
28	*Employee Benefits*	IAS 19 *Employee Benefits*
29	*Income Tax*	IAS 12 *Income Taxes*
30	*Foreign Currency Translation*	IAS 21 *The Effects of Changes in Foreign Exchange Rates*
31	*Hyperinflation*	IAS 29 *Financial Reporting in Hyperinflationary Economies*
32	*Events after the End of the Reporting Period*	IAS 10 *Events after the Reporting Period*
33	*Related Party Disclosures*	IAS 24 *Related Party Disclosures*
34	*Specialised Activities*	IAS 41 *Agriculture*, IFRS 6 *Exploration for and Evaluation of Mineral Resources*
35	*Transition to the* IFRS for SMEs	IFRS 1 *First-time Adoption of International Financial Reporting Standards*