

Model Annual Report

A guide to
producing an
annual report
and financial
statements.



Model Annual Report



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Introduction

About the Model

Financial Statements

Welcome to the model financial statements of The Toy Company Limited and subsidiaries for the year ended 31 March 2003. The Toy Company Limited is a fictional New Zealand Company registered under the Companies Act 1993 and listed on the New Zealand Stock Exchange.



These model financial statements have been designed by the National Technical Division of Deloitte to assist clients, partners and staff in the preparation of financial statements. They have been prepared as an illustrative example of a general purpose financial report of an economic entity comprising a parent entity and its subsidiaries, in accordance with the New Zealand Financial Reporting Act 1993, the Companies Act 1993 and generally accepted accounting practice.

This model is not designed to meet specific needs of specialised industries. Rather, it is intended to meet the needs of the vast majority of companies in complying with the general reporting requirements of the Companies Act 1993 and the Financial Reporting Act 1993. Enquiries regarding specialised industries, credit unions, etc should be directed to your nearest Deloitte office.

Current accounting practices and changes in financial reporting standards have been incorporated into these model financial statements at the time of publication. Due to the continually evolving nature of accounting practices it

is important that the preparer of financial statements maintains an awareness of financial reporting developments and how these impact on the preparer's financial statements.

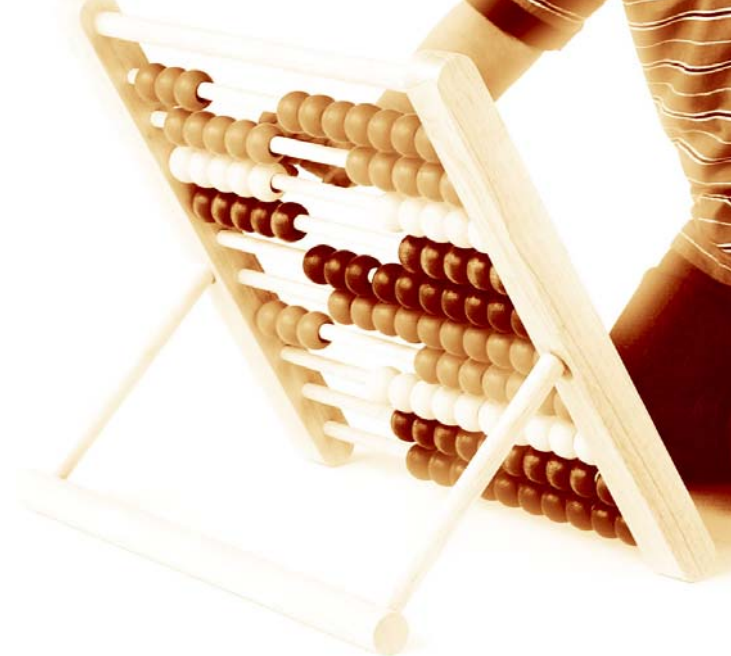
Source References

References to the relevant requirements are provided in the right hand column of each page of this model. Where doubt exists as to the appropriate treatment, examination of the source of the disclosure requirement is recommended.

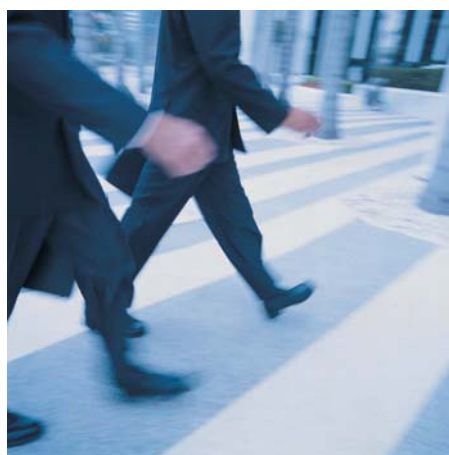
Abbreviations used are as follows:

CA	Companies Act 1993
ED	Exposure Draft
FRA	Financial Reporting Act 1993
FRS	Financial Reporting Standard
GRI	Global Reporting Initiative
IAS	International Accounting Standard
IFRS	International Financial Reporting Standard
NZX	New Zealand Stock Exchange
SIC	Standing Interpretation Committee (International)
SSAP	Statement of Standard Accounting Practice

Section 1 Overview



Developments in financial reporting



The model financial statements incorporate the latest New Zealand financial reporting standards FRS-36 – *Accounting for Acquisitions Resulting in Combinations of Entities or Operations*, FRS -37 – *Consolidating Investments in Subsidiaries* and FRS-38 – *Accounting for Investments in Associates*.

Preparers should be aware however, that there are significant changes heralded for financial reporting in New Zealand.

The most significant development in financial reporting in New Zealand for a number of years was the announcement by the New Zealand Accounting Standards Review Board (ASRB) on 21 October 2002 that it would recommend to government and other affected bodies that listed issuers be required to comply with International Financial Reporting Standards issued by the International Accounting Standards Boards (IASB) by 2007, with the option to adopt the standards earlier from 2005.

The ASRB reiterated this decision in December 2002 after consultation with a number of parties and decided to broaden the scope of its recommendations to both the public and private sectors.

In broadening the scope the ASRB committed to sector neutral financial reporting standards, that is, a single set of

standards that applies to both the public and private sectors.

European Union listed companies and Australian listed companies are required to prepare consolidated financial reports in accordance with International Financial Reporting Standards (IFRS's) for periods beginning on or after 1 January 2005. It is likely that a number of New Zealand listed companies will wish to adopt IFRS's early to coincide with this requirement.

The compelling reason for the change to IFRS's is that a single set of high quality accounting standards which are accepted in major international capital markets will greatly facilitate cross-border comparisons by investors, reduce the cost of capital and assist New Zealand companies wishing to raise capital or list overseas.

The impact of the adoption of IFRS's will vary from entity to entity, depending on structure, operations, transactions and historical accounting policies. Despite New Zealand's recent harmonisation policy, a number of significant differences remain between IFRS's and current financial reporting standards in New Zealand. There are also a number of minor differences that entities will need to be aware of.

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- ABOUT THE MODEL FINANCIAL STATEMENTS



In accordance with the IASB's current agenda, a significant majority of its 33 accounting standards currently on issue are also expected to be revised between now and 1 January 2005. In addition, new IFRS's are expected on topics including share based payment, first-time adoption of IFRS, business combinations and insurance. As a result the exact nature and requirements of financial reporting standards that New Zealand entities will apply will not be known until closer to 1 January 2005. New Zealand entities will therefore need to consider the transition process in the context of concurrent changes.

There are also several financial reporting standards in New Zealand which do not have an international counterpart, including those on summary financial reports, goods and services tax, accounting for shares issued in a dividend election plan; general and life insurance and prospective financial information.

The practical impact of the adoption of IFRS's is that entities will be required to restate their prior year comparatives on implementation of the new and revised financial reporting standards. For New Zealand entities that elect to adopt the IFRS's early along with their European Union and Australian counterparts, restatement of balances as early as 31 December 2003 may be required.

Entities should not underestimate the business implications and the amount of work involved in adopting IFRS's. All entities need to consider their plans and approach to the adoption of IFRS's now.

Further information on the IASB's agenda and the process for adoption of IFRS's in New Zealand can be found on the following Deloitte websites:

www.iasplus.com

www.deloitte.co.nz

Entities should not underestimate the business implications and the amount of work involved in adopting IFRS's.

Legislative framework

Annual Report

When is an annual report required?

Section 208 of the Companies Act 1993 requires companies to prepare an annual report on the affairs of the company during the accounting period. This report is required within 5 months of balance date [9 months for an exempt company].

Who should receive a copy of the annual report?

Section 209 of the Companies Act 1993 requires the board of a company to send a copy of the annual report to every shareholder of the company not less than 20 working days before the date fixed for holding the annual meeting of the shareholders except in the following circumstances:

- (a) the shareholder has given notice in writing to the company waiving the right to be sent a copy of the annual report; and
- (b) the shareholder has not revoked that notice; and
- (c) a copy of the report is available for inspection by the shareholder.

Where the annual report is not required to be sent by the company, section 210 of the Companies Act 1993 requires the board to send to those shareholders, not less than 20 working days before the annual meeting of shareholders, a copy of the financial statements, any group

financial statements and audit report(s) for the most recently completed accounting period signed in accordance with section 10 and 13 of the Financial Reporting Act 1993.

What are the minimum requirements of an annual report?

The Companies Act 1993 Requirements:

Section 211 of the Companies Act 1993 requires the annual report to be in writing, dated and signed by two directors of the company or, if the company only has one director, by that director. The following additional disclosures in the annual report are required:

- (a) a description of any material change during the accounting period in:
 - (i) the nature of the business of the company or any of its subsidiaries or
 - (ii) the classes of business in which the company has an interest, whether as a shareholder of another company or otherwise;
- (b) signed company and group financial statements for the period;
- (c) an auditors' report if required;
- (d) particulars of entries in the interest register made during the accounting period;
- (e) in respect of each director or former

director of the company, the total of the remuneration and the value of other benefits received by that director or former director from the company during the accounting period;

- (f) the number of employees or former employees of the company (not being directors of the company) who received remuneration and any other benefits during the accounting period of \$100,000 per annum or more. The number of such employees or former employees in brackets of \$10,000 is required;
- (g) the total amount of donations made during the accounting period;
- (h) the names of the persons holding office as directors of the company at the end of the accounting period and those who ceased to hold office as directors during the period;
- (i) amounts payable to the auditor of the company as audit fees and, as a separate item, for other services provided.

Where group financial statements are required, the annual report should also disclose the information specified in (d) to (i) above in relation to its subsidiaries.

Where all shareholders agree the annual report of a company need not comply with paragraphs (a) and (d) to (i) above.

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The New Zealand Stock Exchange Listing Rules

Rules 10.5.1, 10.5.3, 10.5.4, and 10.5.5 of the NZX Listing Rules require a number of disclosures in annual reports of issuers with securities which are traded on the Exchange.

Important disclosures required by these rules are as follows:

- (a) all information required by law;
- (b) all information required in a preliminary announcement by Rule 10.4.2;
- (c) Information required to be published by section 26 of the Securities Amendment Act 1988 and in the case of a company, the information required by section 211 of the Companies Act 1993;
- (d) the names and holdings of equity securities of the holders having the 20 largest holdings of quoted equity securities on the register of the issuer as at a date not earlier than two months before the date of the publication of the annual report;
- (e) the equity securities in which each director has a relevant interest at the balance date of the current financial year;
- (f) details of the spread of security holders at a date not earlier the two months before the date of the

publication of the annual report;

- (g) current credit rating status (if any) of the issuer;
- (h) all waivers granted by NZX or the Market Surveillance Panel, published and applicable at balance date;
- (i) details of any exercise of NZX's powers set out in Rule 5.4.2;
- (j) a statement of any corporate governance policies, practices and processes, adopted and followed by the issuer;
- (k) the identity of any director appointed in accordance with Rule 3.3.5 and the security holder which appointed that director.

Rule 10.5.5 requires an issuer which changes its balance date to make a report containing such information, and to be released, at such time as NZX shall require in respect of the existing half-yearly reporting period or the period ending on the existing balance date.

An issuer is required to send copies of any documents referred to in Rules 10.4 or 10.5 including the annual report to any broker who requests, and three printed copies of the annual report must be sent to NZX at the same time as they are sent to security holders.

Rule 10.5.3(h) of the NZX Listing Rules requires listed companies to provide a statement of any corporate governance

policies, practices and processes which are adopted or followed by the issuer. We recommend the issue of such a statement by all publicly accountable entities, as an assurance to users that reasonable steps have been taken to minimise the corporate governance related risks to which entities and investors are exposed. Refer to more detailed guidance at pages 51 to 59 of the Corporate Governance section 4 of the model annual report.

Further details of the New Zealand Stock Exchange Listing Rules can be found at

The NZX Listing Rules requires listed companies to provide a statement of any corporate governance policies, practices and processes which are adopted or followed by the issuer.

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www.nzx.co.nz

Financial Statements

When are financial statements required to be prepared?

Section 10 of the Financial Reporting Act 1993 [FRA] requires the directors of every reporting entity to prepare financial statements within 5 months of balance date. This same requirement applies to group financial statements as prescribed by section 13 of the FRA 1993.

The financial statements and group financial statements must be dated and signed on behalf of the directors by two directors of the entity, or, if the entity only has one director, by that director.

If all shareholders agree, the directors of an exempt company may extend this period to 9 months after balance date.

Group financial statements are not required in relation to a reporting entity that is a company if the only shareholder of the company at that balance date is a reporting entity that is a body corporate

(and/or its subsidiary and/or the nominee of either) [FRA s13(2)].

Definitions:

A reporting entity is defined in the Financial Reporting Act 1993, section 2 as:

- (a) an issuer; or
- (b) a company, other than an exempt company; or
- (c) a person that is required by any Act, other than the FRA, to comply with the FRA as if it were a reporting entity.

An issuer is defined in the Financial Reporting Act 1993, section 4 as:

- (a) Every person who has, whether before or after the commencement of the FRA, allotted securities pursuant to-
 - (i) An offer for which, or for which but for an exemption granted by the Securities Commission pursuant to section 5 of the Securities Act 1978, an investment statement or a registered prospectus, or both, is or was required under that Act (other than an offer of a unit in a unit trust); or
 - (ii) An offer required to be contained in a prospectus required to be registered under the Companies Act 1955, -

whether or not the securities allotted are securities of the same type as the securities offered;

- (b) Every manager of a unit trust (within the meaning of section 2 of the Unit Trusts Act 1960) in which securities have been allotted, whether before or after the commencement of the FRA, pursuant to an offer of securities to the public within the meaning of the Securities Act 1978;
- (c) Every person who is a party to a listing agreement with a stock exchange in New Zealand and who has issued securities which are quoted on such an exchange;
- (d) Every insurer (to whom Part 10 of the Injury Prevention Rehabilitation and Compensation Act 2001 applies);
- (e) Every registered bank that has allotted securities to the public [FRA s4(2)].

Certain entities are specifically excluded from the definition of issuer under section 6 including a company that does

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not have more than 25 shareholders and that would be an issuer by reason only of the allotment of equity securities.

An exempt company under the Financial Reporting Act 1993 is a company (other than an overseas company or an issuer), where during the accounting period:

- The value of total assets did not exceed \$450,000,
- Turnover did not exceed \$1,000,000,
- The company was not a subsidiary of another body corporate or association of persons, and
- The company did not have any subsidiaries.

An overseas company is a company which is incorporated outside New Zealand which carries on business in New Zealand [FRA s2]. The meaning of carrying on business is explained in section 332 of the Companies Act 1993.

Other companies with overseas connections are:

- Subsidiaries of companies or body corporates incorporated outside New Zealand, and
- Companies in which:
 - a subsidiary of a company or body corporate incorporated outside New Zealand or a subsidiary of that subsidiary, or

- a company or body corporate incorporated outside New Zealand, or
- a person not ordinarily resident in New Zealand

hold shares which in aggregate carry the right to exercise or control the exercise of 25% or more of the voting power at a meeting of the company [FRA, s19].

When are financial statements required to be audited?

Issuers

Section 15 of the FRA requires the directors of an issuer to ensure that the financial statements of the issuer and group financial statements (if any), are audited.

The financial statements and any group financial statements must be audited by an auditor appointed or qualified for appointment under the Companies Act 1993. If the issuer is incorporated or registered under any other Act that provides for the appointment of an auditor, an auditor will be appointed under that Act. If the issuer is a public entity under the Public Audit Act 2001, the financial statements and any group financial statements will be audited by the Auditor-General.

The New Zealand Stock Exchange Rules require the financial statements

contained in the annual report of an issuer to be audited (Rule 10.5.1).

Other

Section 196 of the Companies Act 1003 requires overseas companies and other companies with overseas connections (as outlined above), to appoint an auditor.

Section 196 also requires other companies to appoint an auditor unless there is a unanimous resolution of shareholders at or before the annual meeting of shareholders. If the company is a public entity as defined in section 4 of the Public Audit Act 2001, the Auditor-General is automatically appointed its auditor.

When are financial statements required to be filed?

All issuers, overseas companies and certain other companies with overseas connections (as outlined above) are required to deliver copies of their financial statements, group financial statements and auditors' report to the Registrar, within 20 working days after the financial statements are required to be signed [FRA, s18(1) and 19(2)]. In respect of reporting entities and companies other than issuers which are societies or credit unions, the Registrar is the Registrar of Companies, the Deputy Registrar of Companies, a District Registrar of Companies or an Assistant Registrar of Companies.

The New Zealand Stock Exchange Rules

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require each issuer to issue an annual report (which must contain audited financial statements) to the NZX and to its quoted security holders within three months after the end of each financial year of the issuer. The annual report is required to be received by the exchange at the same time as it is sent to security holders (NZX Rule 10.5.1).

What should the financial statements include?

Under the Financial Reporting Act 1993, Section 8, the term “financial statements” in relation to an entity means a statement of financial position, and

- (a) in respect of an entity trading for profit, a statement of financial performance
- (b) in respect of an entity that is not trading for profit, an income and expenditure statement
- (c) in respect of an entity that is a building society within the meaning of the Building Societies Act 1965, a revenue and appropriation account; and
- (d) in respect of a reporting entity where an applicable financial reporting standard requires, a statement of cash flows

together with any notes or documents

giving information relating to the above statements.

Under the Financial Reporting Act 1993, section 9, the term “group financial statements” in relation to a group means a consolidated statement of financial position for the group, and

- (a) where a member of the group trades for profit, a consolidated statement of financial performance
- (b) where no member of the group trades for profit, a consolidated income and expenditure statement; and
- (c) if an applicable financial reporting standard requires, a consolidated statement of cash flows

together with any notes or documents giving information relating to the above statements.

In respect of a reporting entity that is an overseas company, the term “financial statements” and “group financial statements” includes, in addition to the financial statements and group financial statements (if any) of the overseas company, financial statements and group financial statements in respect of the company’s and the group’s New Zealand

business prepared as if that business were conducted by a company or companies formed and registered in New Zealand.

Rule 10.6.2 of the New Zealand Stock Exchange Listing Rules notes that the NZX may require an issuer to provide in its financial statements, information additional to that required by the Financial Reporting Act 1993.

On what basis should the financial statements be prepared?

Financial reporting requirements are governed by the Financial Reporting Act 1993 and the Framework for Differential Reporting, issued by the Institute of Chartered Accountants of New Zealand. The three tiers of reporting requirements are as follows:

1. Exempt Companies Under the Financial Reporting Act 1993

Exempt companies are required to produce their financial statements in accordance with the Financial Reporting

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- (ii) Have authoritative support within the accounting profession in New Zealand.

The Accounting Standards Review Board (ASRB) has approved FRS-29: *Prospective Financial Information* for the purposes of the Public Finance Act 1989 (ie in respect of the Crown and all departments, Office of Parliament and Crown entities) and declared FRS-29 as authoritative support for other reporting entities. All other Financial Reporting Standards (FRSs) except FRS-31: *Disclosure of Information About Financial Instruments* and FRS-39: *Summary Financial Reports* have been approved by the ASRB as applicable financial reporting standards.

The ASRB, in its Release number 1 (subsequently replaced by Release number 7), declared that all Statements of Standard Accounting Practice (SSAPs), FRS-29 and FRS-31 are deemed to have authoritative support within the accounting profession in New Zealand. The ASRB has also given a direction that FRS 39 has authoritative support within the accounting profession in New Zealand.

Other sources of authoritative support are listed in the Explanatory Foreword to

General Purpose Financial Reporting, issued by the Institute of Chartered Accountants of New Zealand as follows:

- New Zealand financial reporting standards which are applicable to analogous items or matters;
- Guidance notes to New Zealand financial reporting standards;
- Statement of Concepts for General Purpose Financial Reporting;
- Exposure drafts of financial reporting standards issued by the Financial Reporting Standards Board;
- Interpretations by the Financial Reporting Standards Board of financial reporting standards;
- Technical practice aids and technical guidance bulletins issued by the Financial Reporting Standards Board;
- Research bulletins published by the Institute;
- Accounting standards published by the Australian Accounting Standards Board;
- International accounting standards published by the International Accounting Standards Board;
- Accounting standards published by

other well-recognised bodies with the authority to promulgate financial reporting standards in other jurisdictions; and

- Practice widely accepted as appropriate and prevalent for the industry or sector concerned.

Where there are conflicts between sources of authoritative support, professional judgement is required in the selection process.

True and Fair View

The financial statements and notes thereto prepared to satisfy the reporting requirements of the Companies Act 1993 must comply with financial reporting standards issued by the Institute of Chartered Accountants of New Zealand, even if compliance does not result in a true and fair view. Sections 11 and 14 of the Financial Reporting Act 1993 require directors to provide additional information and explanation when compliance with financial reporting standards issued by the Institute of Chartered Accountants of New Zealand would not give a true and fair view. This additional information and explanations should be given by way of a note to the financial statements.

Materiality

In accordance with Statement of Standard Accounting Practice (SSAP) 6: *Materiality in Financial Statements*, subject to

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compliance with statutory or other requirements binding upon the reporting entity, financial statements should be prepared having regard to the materiality of the information to be given.

A statement, fact, or item is material if it is of such a nature that its disclosure, or the method of treating it, given full consideration of the circumstances applying at the time the financial statements are completed, is likely to influence users of the financial statements in making decisions or assessments.

In determining whether the amount of an item is material, the item should be compared with the more appropriate of the following base amounts:

- (a) in the case of items relating to the statement of financial position – equity or the appropriate asset or liability class total;
- (b) in the case of items relating to the statement of financial performance – pre-tax net surplus or deficit for the current year or the average for, say, the last three years whichever is the most relevant measure of trading results having regard to the trend of the business over that period. Where the tax charge is not fully equal to a charge at current tax rates on pre-tax surplus, or an item being considered for adjustment is not tax deductible, it may be more appropriate to evaluate the materiality of the item based on the after tax surplus.

- (c) Where an item is subject to comparison with the base amounts in both (a) and (b) above, the more stringent test should prevail.

The appendix to SSAP-6 suggests the following quantitative threshold that may be used as a guide in considering the materiality of an item in the absence of evidence to the contrary:

- (a) A variation in amount equal to or greater than 10 percent of the appropriate base amount is presumed to be material; and
- (b) A variation in amount which is equal to or less than 5 percent of the appropriate base amount is presumed to be immaterial; and
- (c) Whether or not a variation which lies between 5 percent and 10 percent of the appropriate base amount could be material is a matter of judgement and depends upon the particular circumstances of the case.

SSAP-6 notes that these percentage limits are not “magic numbers” and all circumstances surrounding the items, the reporting entity and the users should be taken into account.

Comparatives

FRS-2: *Presentation of Financial Reports* requires comparative figures for the prior period to be given for all items in the

financial statements. In meeting this requirement the figures for the prior period are reclassified, where necessary, so that said information corresponds to the classification for the current period. The nature and reason for the reclassification must be disclosed. The reclassification may only be made within a primary statement (eg statement of financial performance) but not between primary financial statements (eg the net surplus must not be restated).

Set off of assets and liabilities

Assets and liabilities should only be set-off in accordance with the provisions of FRS-27 *Right of Set-Off*. FRS-27 only permits set off where there is a ‘right of set off’, ie where:

- i) parties to an agreement owe each other fixed amounts of money;
- ii) the parties acknowledge the right to set off;
- iii) the entity intends to set off; and
- iv) the right to set off is enforceable at law.

Nil Figures in both years

Where the consolidated and parent entity figures are nil in both years the line should be omitted.

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Timeline of critical dates

CRITICAL EVENT	CRITICAL DATE	
Completion and signing of financial statements (all reporting entities)	No later than 5 months after balance date ¹	FRA s10, 13
Filing with Companies Office (Issuers and certain other entities)	No later than 20 working days after financial statements are required to be signed	FRA s18(1), 19(2)
Issue to the New Zealand Stock Exchange and quoted security holders (listed issuers)	No later than 3 months after balance date	NZSE 10.5-1
Completion and signing Annual Report	No later than 5 months after balance date	CA s208(1)
Annual report to shareholders (Companies)	No less than 20 working days before the date of the annual meeting of shareholders	CA s209(1)
Annual Meeting of shareholders (Companies)	No later than 6 months ² after balance date and 15 months after the previous annual meeting	CA s120(1)

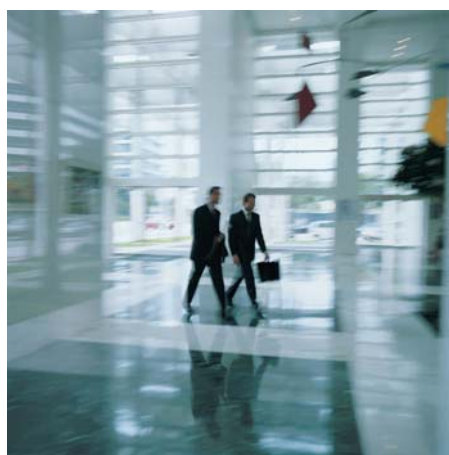
Notes

- ¹ The Financial Reporting Act 1993 allows an extension to 9 months for exempt companies where all the members or shareholders agree. FRA s10(2)
- ² 10 months for exempt companies if all shareholders agree. CA s120(1)(b)(i)

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Other information in annual reports



Directors' Reports

What matters should be considered when preparing the Directors' Report?

A "Directors' Report" is not specifically required by the Companies Act 1993 however many companies include a Chairman's Report and a Managing Director's Report in their Annual Report which include information regarding the performance of the company and the events that have occurred during the reporting period. Information that could be considered in preparing such reports (including some of the specific requirements of s211 of the Companies Act 1993):

- The names and particulars of the directors of the company during or since the end of the financial year;
- Particulars of each directors' qualifications, experience and special responsibilities;
- A review of the consolidated entity's operations during the financial year and the results of those operations;
- A review of financial conditions such as capital funding and treasury policies, restriction of funds transfer, covenants and the maturity profile of borrowings;
- Where changes to the state of affairs of the company are material, provide details and cross reference these to relevant notes in the financial statements;
- Details of likely future developments in operations that directors wish to bring to the attention of the users of the financial report;
- Details of performance in relation to environmental or other legislation, as appropriate;
- Details of dividends paid and / or declared;
- Details of the number of directors' meetings (including meetings of committees of directors) held during the financial year and the number of meetings attended by each director;
- Details of directors' shareholdings; and
- Details of directors' and executives' remuneration and the broad policy for determining the nature and amount of directors' and executives' remuneration.

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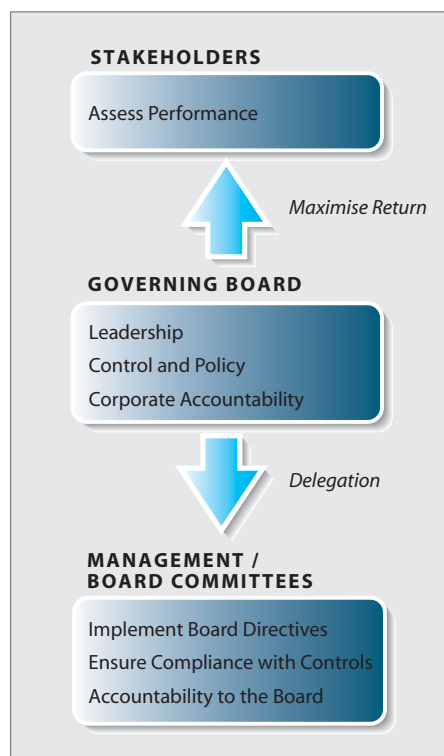
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Corporate Governance

What is Corporate Governance?

Put simply, corporate governance is the method used by corporations to manage and control their activities. Directors are accountable for the effectiveness of these requirements. These principles are equally applicable to governing boards of non corporate entities in the private and public sectors.

Corporate governance can be shown diagrammatically as follows:



Who is required to prepare a Statement of Corporate Governance?

The New Zealand Stock Exchange Listing Rule 10.5.3(h) requires listed companies to provide a statement of any corporate governance policies, practices and processes adopted or followed by the issuer for the reporting period.

We recommend the issue of such a statement by all publicly accountable entities, as an assurance to users that the Board has considered and implemented good corporate governance policies and practices.

What matters should be considered when preparing a Statement of Corporate Governance?

When preparing a Statement of Corporate Governance the company should consider the following:

- Distinguishing between executive and non-executive directors;
- Procedures relating to the nomination and appointment of new directors;
- Company policy relating to the appointment and retirement of directors;
- Procedures to enable directors to obtain independent legal or accounting advice;
- Procedures for the determination of remuneration for the Chief Executive Officer, senior executives and board members;

Corporate governance is the method used by corporations to manage and control their activities



- Procedures for the nomination of external auditors;
- The board of directors' approach to identifying and managing significant business risks; and
- Company policy relating to the maintenance of ethical standards.

Deloitte publications on corporate governance matters include:

- Corporate Governance;
- Directors' Duties;
- Audit Committees; and
- Quality of Earnings – a Guide for Audit Committees.

An illustration of a statement of corporate governance is included in these model financial statements on page 51 to 59 of the Corporate Governance section 4 of the model annual report..

Sustainability Reporting

A number of entities in New Zealand are adopting some form of sustainability reporting which encompasses the matters detailed above, as well as a wealth of other information useful to stakeholders. Detailed below is an overview of sustainability reporting, reasons for incorporating such reporting in the annual report and sustainability reporting frameworks available and in use currently in New Zealand and internationally.

An overview of sustainability

Annual Reports are an important tool for an entity's communication with stakeholders. Expectations of corporate responsibility in areas such as environmental protection, human rights, human capital and product safety are rising rapidly. Key stakeholders such as shareholders, employees, consumers and financial institutions want businesses to be responsible, accountable and transparent.

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They are referring to the entity's reports to get forward looking information and understand the external environment the entity operates in before deciding whether they wish to enter into a relationship with the organisation.

Many entities internationally and in New Zealand understand the need to go beyond simply meeting their mandatory disclosure requirements, focusing on their past financial performance. Some have extended their annual reporting to prepare isolated reports on their environmental or health and safety impacts. Others can see the business arguments and value in moving beyond this to prepare an annual evaluation of how sustainable their business is, and how it will manage future growth to ensure that it meets the concept of "Sustainable Development".¹

What is Sustainability Reporting?

An external Sustainability Report presents and interprets the direct and indirect impact that an entity has on the world around it. It helps users understand if their concerns as stakeholders have been identified and acted on, whether the entity has understood and addressed the risks to its future sustainability and what opportunities have been identified to add value to both society and shareholders. In each area, the entity should report on key material indicators of past performance and future short, mid and long-term goals. By communicating in this way, the entity demonstrates that it understands how its decisions and

performance will not only have a short-term financial impact, but that the economic, environmental and social effects link together.

An effective report should communicate an organisation's vision, strategy, commitment and progress towards a more sustainable economy, environment and society. This should be visible as a thread tying together the organisation's aims throughout the report.

WHAT ARE THE ISSUES?	Identify Relevance
HOW TO DEAL WITH THEM?	Demonstrate Commitment and Management Quality
WHAT ARE THE ACTIONS AND WITH WHOM?	Address the Sustainable Development Agenda
HOW MUCH TO ACHIEVE BY WHEN?	Quality Performance

What are the internal and external costs and benefits of preparing Sustainability Reports?

As producing a Sustainability Report requires the joint effort of many departments, it is unlikely to be successful without top management commitment, clear lines of responsibility and sufficient resources. Many entities will begin along a continuum - beginning to develop reports internally from existing information, then over time, developing external reports to be more comprehensive. Once committed and on the path to implement and report on sustainable strategies, entities have identified various benefits that are commonly received as follows:

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1. Provides a management tool to enhance the quality of operations both through continuous improvement and by linking the separate functions in the organisation;
2. Creates transparency and therefore strengthens public accountability and reputation. It may reduce the volatility and uncertainty in share price, avoiding major swings in investor behaviour caused by unexpected disclosures;
3. Enhances relationships with stakeholders (e.g. customers, suppliers, employees, trade unions regulators, communities, non-governmental organisations, etc) by raising internal awareness of their information needs, communicating with them and reporting how the entity is meeting their concerns and expectations;
4. Highlights the need for a sustainable vision and aligns strategy and operations with this;
5. Assists in identifying trouble spots and managing risks before they become an unwelcome surprise;
6. Highlights areas where policies and measures (performance appraisal systems) are lacking;
7. Encourages innovation by revealing unanticipated opportunities such as new products and/or markets;
8. Motivates, empowers and aligns existing employees with the sustainable strategic objectives and attracts high calibre employees;
9. Documents economic, social and environmental achievements;
10. Helps management to assess the organisations contribution to natural, human and social capital and therefore both its long term prospects and licence to operate;
11. Establishes the organisation's boundaries of direct and indirect impact.

Is this the way of the future?

As issues such as corporate governance, accountability and citizenship are moving to the mainstream of policy and management debates in organisations, entities both internationally and in New Zealand are using sustainability reports to communicate how they are responding. Stakeholder pressure, government policy, regulations and increasing globalisation are driving change. Many observers believe that in today's information economy, accounting and reporting must continue to evolve and develop to meet stakeholders' demands for richer disclosure. There are rapid advances in areas such as environmental management accounting, valuation of intangible assets and value reporting. As these develop, it is likely that there will eventually be a full integration of single reports that depict the performance of a company in all dimensions – conventional financial, economic, environmental and social – as a fully integrated assessment of the sustainability of an organisation.

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What assistance is available?

Various groups are actively contributing assistance to provide guidance to entities wanting to extend their reporting. The Global Reporting Initiative (GRI), aiming to create a common framework for voluntary corporate sustainability reporting, has issued a set of sustainability reporting guidelines which give guidance to organisations interested in producing a report. This year we have included an example of a Sustainability Report as part of our Annual Report, to illustrate the reporting principles and an example of specific content that is included when a Sustainability Report is prepared in accordance with these GRI Guidelines.

We have chosen to follow the GRI guidelines as they provide a platform to work towards the harmonisation of disclosure by all entities and therefore maximise the value of reporting for both the reporting organisation and users.

If your organisation would like additional information and recent examples of sustainability reporting, please contact your nearest Deloitte office.

Guides to preparing a Sustainable Development Report

The World Business Council for Sustainable Development (WBCSD)

(A coalition of international companies who aim to provide business leadership as a catalyst for change toward sustainable development, promote eco-efficiency, innovation and corporate social responsibility)

WBCSD website: Sustainable Development Reporting Portal

www.sdportal.org

WBCSD publication: Sustainable Development Reporting – Striking the Balance

www.wbcasd.org

The New Zealand Business Council for Sustainable Development (NZBCSD)

(New Zealand member organisation of the WBCSD, with member organisations united by a shared commitment to balance social, environmental and economic development)

NZBCSD: Sustainable Development Reporting (SDR) website

www.nzbcasd.org.nz

What Reporting Frameworks can be used?

The Global Reporting Initiative

(A multi-stakeholder process and independent institution (originally a joint initiative of the U.S. non-governmental

organisation Coalition for Environmentally Responsible Economies (CERES) and United Nations Environmental Programme) whose mission is to develop and disseminate globally applicable Sustainability Reporting Guidelines.)

2002 Sustainability Reporting Guidelines, Technical Protocols, Sector Supplements, Issue Guidance Documents, Resource Documents

www.globalreporting.org

AccountAbility – Institute of Social and Ethical Accountability

(An international, not-for-profit, professional institute dedicated to the promotion of social, ethical and overall organisational accountability, a precondition for achieving sustainable development.)

AA1000 Framework to establish a systematic stakeholder engagement process.

www.accountability.org.uk

Sustainable Development is defined as “development which meets the needs of the present without compromising the ability of future generations to meet their own needs.” World Commission on Environment and Development 1987/ Sustainable Development for New Zealand - Programme of Action January 2003.