case study 2.2 solution

Telecom Corporation of New Zealand Limited’s Approach to Corporate Governance

Governance at Telecom

*The board and management are committed to ensuring that Telecom maintains international best practice governance structures and adheres to the highest ethical standards. The board regularly reviews and assesses Telecom’s governance structures and processes to ensure that they are consistent with international best practice, in both form and substance.*

Telecom’s approach to corporate governance

Framework

Telecom has a dual listing of its shares on the New Zealand Stock Market (NZSX) and on the Australian Securities Exchange (ASX). Telecom is required to comply with the full listing rules of the NZSX and ASX. American Depositary Shares (ADSs), each representing five ordinary shares and evidenced by American Depositary Receipts (ADRs), are listed on the New York Stock Exchange (NYSE). The Bank of New York Mellon is Telecom’s ADR Depositary.

As a result of Telecom’s stock exchange listings in New Zealand, Australia and New York, it is subject to the governance requirements of each of these jurisdictions. This includes: the NZSX Listing Rules and Corporate Governance Best Practice Code; the New Zealand Securities Commission’s report titled ‘Corporate Governance in New Zealand Principles and Guidelines’ (Securities Commission Principles and Guidelines); the ASX Listing Rules and ASX Corporate Governance Council’s Principles and Recommendations; the United States Sarbanes-Oxley Act of 2002 and United States Securities and Exchange Commission (SEC) rules and the NYSE corporate governance rules.

Where there are conflicts between the requirements or best practice recommendations of New Zealand, Australia and the United States, the board has adopted practices and policies consistent with the requirements across these jurisdictions. The board will continue to monitor developments in the governance area and review and update its governance practices to ensure the most appropriate standards of governance for Telecom are maintained.

SOURCE: *Telecom Corporation of New Zealand Limited Annual Report 2013*, Governance at Telecom, p. 133.

Questions

The financial statements of Telecom Corporation of New Zealand Group are prepared in accordance with International Financial Reporting Standards (IFRS), which differ in certain aspects from US Generally Accepted Accounting Principles (GAAP).

1 Describe what is meant by the term GAAP.

GAAP refers to ‘Generally Accepted Accounting Principles/Practices’. Essentially it incorporates all of the statutory and professional reporting requirements and guidelines, together with the residual of historical accounting conventions or doctrines.

2 Describe what is meant by the term IFRS.

IFRS stands for ‘International Financial Reporting Standards’, which are produced by the International Accounting Standards Board.

3 Outline the difference between ‘Telecom Corporation of New Zealand Group’ and ‘Telecom Corporation of New Zealand Limited’.

Telecom Corporation of New Zealand Group refers to the economic entity and the aggregated accounts being composed of the parent or holding company and all of the subsidiary companies controlled directly or indirectly by the holding company. Telecom Corporation of New Zealand Ltd represents the legal entity as the parent (holding) company on its own.

4 Telecom Corporation of New Zealand Group is required to file an annual report with the United States Securities and Exchange Commission on Form 20-F. Describe the process that is required.

A foreign private issuer of securities, such as Telecom Corporation of New Zealand Group, which is publically listed in the US, is required to file form 20-F with the United States Securities and Exchange Commission (SEC) in order to issue its annual report. This is a requirement of the United States *Securities and Exchange Act* *of 1934*.

The Form 20-F enables financial users to obtain a once-a-year overview of the business: financial results, business risks, management governance, and so on. The form also enables investors to learn more about the unique factors that affect the returns of foreign shares, from currency fluctuations to political pressures.

The United States Securities and Exchange Commission has recently changed its rules to accept from foreign private issuers in their filings with the Commission financial statements prepared in accordance with International Financial Reporting Standards (‘IFRS’) as issued by the International Accounting Standards Board (‘IASB’) without reconciliation to generally accepted accounting principles (‘GAAP’) as used in the United States. Current requirements regarding the reconciliation to US GAAP do not change for a foreign private issuer that files its financial statements with the Commission using a basis of accounting other than IFRS as issued by the IASB.

5 How does this differ from previous practice?

Telecom Corporation of New Zealand Limited shares are listed on the Australian, New Zealand and US Stock Markets. In the past (prior to early 2008), the International accounting standards satisfied listing on the Australian and New Zealand exchanges, but for the US listing US GAAP regulations had to be complied with, therefore Telecom Corporation of New Zealand Limited would have had to undertake a reconciliation of its financial statements between IFRS and US GAAP. This would then have needed to be disclosed to the United States Securities and Exchange Commission on Form 20-F.

6 Outline jurisdictional governance requirements that Telecom Corporation of New Zealand Group is subject to. How might the organisation comply with such requirements?

Jurisdictional Governance Requirements include:

• New Zealand – the NZSX Listing Rules and Corporate Governance Best Practice Code; the New Zealand Securities Commission’s report titled ‘Corporate Governance in New Zealand Principles and Guidelines’ (Securities Commission Principles and Guidelines)

• Australia – the ASX Listing Rules and ASX Corporate Governance Council’s Principles and Recommendations

• United States of America – the United States *Sarbanes-Oxley Act* *of 2002* and United States Securities and Exchange Commission (SEC) rules and the NYSE corporate governance rules.

Compliance with NZSX Best Practice Code, Securities Commission Principles and Guidelines and ASX Corporate Governance Council Recommendations:

• The NZSX Listing Rules require Telecom to include a statement in its annual report disclosing the extent to which it has followed the NZSX Corporate Governance Best Practice Code for the reporting period. Telecom considers its governance practices comply with the Code in its entirety for the year ended 30 June 2013. Telecom also considers that its governance practices comply with the Securities Commission Principles and Guidelines in their entirety for the year ended 30 June 2013.

This includes adhering to the principles of the Statement of Corporate Governance:

• observe and foster high ethical standards

• balance of independence, skills, knowledge and experience among directors so the board works effectively

• board uses committees to enhance effective decision making

• gain integrity in financial reporting and in the timeliness and disclosure of information

• remuneration of directors should be fair, transparent and reasonable

• risk management process and policy is in place

• ensure quality and independence of external audit

• foster constructive relationships with shareholders encouraging them to engage with the company

• respect the interests of stakeholders.

In addition, the ASX Listing Rules require Telecom to include a statement in its annual report disclosing the extent to which Telecom’s governance practices comply with the ASX Corporate Governance Council Principles and Recommendations set out in the second edition of the Corporate Governance Principles and Recommendations during the reporting period, identifying the recommendations that have not been followed and providing reasons for that variance.

The ASX Corporate Governance Council released changes to the Corporate Governance Principles and Recommendations on 30 June 2010. Listed companies are expected to disclose the extent to which their governance practices comply with these changes in respect of financial years beginning on or after 1 January 2011.

Compliance with NYSE listing standards:

• As a ‘foreign private issuer’ registered with the SEC with securities listed on the NYSE, Telecom has a ‘home country’ exemption from most of the NYSE corporate governance requirements. However, Telecom is still required to comply with certain corporate governance requirements contained in United States securities laws, including applicable portions of the *Sarbanes-Oxley Act 2002* and applicable NYSE listing standards. As required under the NYSE listing standards and SEC rules, Telecom must provide a concise summary of any significant ways in which its corporate governance practices differ from those followed by United States domestic companies under the NYSE listing standards.

Telecom has reviewed the NYSE’s corporate governance requirements and believes its practices are broadly consistent with the NYSE corporate governance requirements, with the following material exceptions:

• Under sections 303A.04 and 303A.05 of the NYSE corporate governance rules, United States domestic-listed companies are required to have a corporate governance committee and a compensation committee comprised entirely of independent directors. The Telecom committee charters of the Nominations and Corporate Governance Committee and the Human Resources and Compensation Committee require that only a majority of members be independent (as that term is defined in the board charter) directors, as permitted by New Zealand and Australian corporate governance requirements. In addition to the independence test contained in section 303A.02 of the NYSE corporate governance rules, the independence test contained in the board charter also contains the broader NZSX and ASX recommended independence standards.

• Under section 303A.08 of the NYSE corporate governance requirements, shareholders must be given the opportunity to vote on all equity-compensation plans and material revisions of these plans. Telecom considers that its share plans all come within the definition of ‘discretionary plan’ as set out in the explanatory note to section 303A.08, which also states that additional grants under discretionary plans may not be made without further shareholder approval. Since 2003, when the requirement came into effect, shareholder approval has been sought at the time each equity-compensation plan was established. However, Telecom will not be seeking further shareholder approval in relation to allocations under its share plans.