MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

COVERSHEET

Minister	Hon Andrew Bayly	**Portfolio**	Minister of Commerce and Consumer Affairs
Title of Cabinet paper	Improving New Zealand's Capital Markets: Initial decisions and approval to consult	**Date to be published**	13 December 2024

List of documents that have been proactively released		
Date	**Title**	**Author**
December 2024	Improving New Zealand's Capital Markets: Initial decisions and approval to consult	Office of the Minister of Commerce and Consumer Affairs
4 December 2024	Improving New Zealand's Capital Markets: Initial Decisions and Consultation ECO-24-MIN-0296 Minute	Cabinet Office
27 November 2024	Regulatory Impact Statement – Prospective Financial Information for Initial Public Offerings	MBIE

Information redacted **NO**

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Regulatory Impact Statement: Prospective Financial Information for Initial Public Offerings

Coversheet

Purpose of Document	
Decision sought:	Analysis produced for the purpose of informing Cabinet decisions
Advising agencies:	Ministry of Business, Innovation and Employment
Proposing Ministers:	Commerce and Consumer Affairs
Date finalised:	27 November 2024

Problem Definition

New Zealand's regulations require businesses (issuers) who issue equity securities to retail investors on domestic stock markets (an Initial Public Offering, IPO) to prepare future-focused financial information (called Prospective Financial Information, PFI) to comprehensive domestic accounting and auditing standards unless doing so would be false or misleading.

These requirements impose significant costs on potential issuers. It is seen to be a barrier to issuers deciding to list in New Zealand and an area where New Zealand's settings are seen as a competitive disadvantage, particularly with Australia. Moreover, PFI disclosures are likely not providing proportionate benefits to investors generally, particularly retail investors who are the primary audience for the information.

Executive Summary

New Zealand requires PFI to be prepared by issuers and included in product disclosure statements (PDS) to retail investors in an IPO as per the Financial Markets Conduct Act 2013 (FMC Act) and the Financial Markets Conduct Regulations 2014 (FMC Regulations). The PDS required to be provided for, and targeted to, retail investors and should provide them with material information so they understand the possible risks and benefits of participating in the issuer's offer of financial products.

In addition to regulations, there are some market forces, particularly from institutional investors and the New Zealand Stock Exchange (NZX), that incentivise issuers to disclose relevant information or risk a lower valuation/price for their IPO.

As outlined above, the current PFI regulatory settings are adding costs that may exceed benefits and reducing flexibility for issuers, especially compared to alternative markets such as Australia. The required disclosures are also not catering as well as they could to the needs of retail investors. Regulatory change is needed to address this problem, likely accompanied by guidance from the regulator.

Four options for adjusting the PFI requirements in the FMC Regulations are considered in this analysis:

- Option 1: Amend the FMC Regulations to require issuers to prepare PFI to meet domestic generally accepted accounting standards for one year with a lower threshold to 'opt-out'

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- Option 2: Amend the FMC Regulations to require issuers to prepare PFI of any form for one year with lower a threshold to ‘opt-out’
- Option 3: Amend the FMC Regulations to allow issuers to ‘opt-in’ and prepare PFI that meets generally accepted accounting practices (GAAP) but not the comprehensive domestic accounting and auditing standards for one year if they think fit
- Option 4: Amend the FMC Regulations to allow issuers flexibility to ‘opt-in’ and prepare PFI of any form if they choose.

Options 1 and 2 still require an issuer to prepare PFI although only for one year, while Option 2 also removes the requirement to be consistent with GAAP. Options 3 and 4 shift to an ‘opt-in’ model with more flexibility. Option 3 requires PFI to be consistent with accounting practices, while Option 4 allows any form of PFI.

Option 4 aligns the New Zealand regulatory settings most closely with Australian legislative settings in that it would not prescribe the form of PFI but allow issuers to choose from multiple approaches. Option 4 could provide the largest cost reduction for issuers, and it had support from many submitters to the Financial Market Authority’s (FMA) consultation, although Option 3 had support as well. Option 4 has some risk that investors will get slightly less reliable information, but these risks are largely mitigated by broader regulatory settings and market forces.

On balance, we consider that Option 4 is most likely to achieve the desired objective.

Option 4 can be implemented and monitored by the Ministry of Business, Innovation and Employment (MBIE) and the FMA. FMA will support the regulatory change and monitor shifts in issuer conduct as a result, it is expected that FMA will prepare guidance to support the regulations in due course.

MBIE’s work programme includes a targeted review of aspects of the FMC disclosure regime which will be able to consider the effectiveness of the regulatory changes.

Limitations and Constraints on Analysis

This analysis is focused on the single issue of mandatory PFI and options to change the PFI provisions in the FMC Regulations. Other matters and options to address the problem are out of scope.

An underlying limitation is uncertainty about the exact costs of PFI, and the impact of PFI on issuer decision making:

- Only nine businesses have prepared PFI as part of an IPO in New Zealand in the past decade out of fourteen, and none of those were in the past two years. Five issuers did not prepare PFI, relying on the current ability in the FMC Regulations to not prepare PFI if doing so would be false or misleading. Many issuers do not know the cost of preparing PFI separate from other financial reporting in the PDS.
- Other factors influence an issuer decision to do an IPO including the ongoing costs of managing a public listing, and the availability of capital from other markets.

Due to timing constraints this analysis draws on issues identified by the *Growing New Zealand’s Capital Markets 2029* report and recent targeted consultation by the FMA, as well as some limited stakeholder engagement by MBIE. FMA consultation received fifteen submissions from a range of stakeholders including issuers, investors, industry participants that help to prepare PFI, and industry groups that represent retail investors. There has not been any public consultation with retail investors directly.

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Responsible Manager	
Tom Simcock Manager Financial Markets policy Ministry of Business, Innovation and Employment 27 November 2024	
Quality Assurance (completed by QA panel)	
Reviewing Agency:	MBIE
Panel Assessment & Comment:	A quality assurance panel with representatives from the Ministry of Business, Innovation and Employment has reviewed the Regulatory Impact Statement (RIS): Prospective Financial Information for Initial Public Offerings. The panel has determined that the RIS provided meets the quality assurance criteria.

Section 1: Context behind the policy problem

Focus of this analysis

1. This regulatory analysis focuses on a subset of financial disclosures that a business is required to make for an initial offer of equity securities to retail investors (an Initial Public Offer, IPO). The required disclosure is 'prospective financial information' (PFI) from which specific metrics must be included in a 'product disclosure statement' (PDS) and provided to retail investors and lodged on the Disclose Register.

1.1 The Financial Markets Conduct Regulatory System

The financial markets conduct regulatory system

2. The financial markets conduct regulatory system (the regulatory system) is the legislation and policies that influence conduct in relation to financial products and services, including conduct in capital markets.
3. The Financial Markets Conduct Act 2013 (FMC Act) is the key legislation in the regulatory system. The FMC Act has two main purposes: to ensure confident and informed participation in financial markets; and fair, efficient, and transparent financial markets.
4. The regulatory system was reformed in 2010-2014 after a comprehensive review of New Zealand's capital markets settings to deliver a more efficient regime that did not impose excessive costs on businesses issuing financial products (eg equity and debt securities), while ensuring investors receive information to make informed decisions.

Key participants in the regulatory system

5. The regulatory system has a range of market participants and regulatory agencies:
   a. The Ministry of Business, Innovation and Employment (MBIE) provides policy advice on issues relating to the regulatory system.
   b. Financial Markets Authority (FMA) is the principal conduct regulator. External Reporting Board (XRB) has a secondary role setting accounting and financial reporting standards.
   c. Financial product markets and stock exchanges provide the markets for certain

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financial products such as publicly listed equities (eg the New Zealand Stock Exchange, NZX)

d. Businesses that raise capital by issuing financial products (issuers)

e. Retail investors and wholesale/institutional investors who invest in businesses by purchasing financial products.

1.2 Businesses can raise capital by issuing equity on publicly listed markets for investors

Capital markets match businesses seeking funds with potential investors

6. Capital markets support investment and innovation by connecting investors with businesses. Investors receive an ownership share or right to be repaid and may receive returns (dividends) in return for their capital which businesses use to grow. Business growth supports innovation and productivity gains and grows the economy.

7. The main capital market is the NZX, where investors can buy and sell equity securities (shares) in listed businesses.

An initial offer of equity on publicly listed markets

8. An IPO is when an issuer enters a publicly traded equity market such as the NZX by issuing and listing shares for purchase by investors.

9. The issuer has a better understanding of their business performance, risks and strategy than an investor. This is an information asymmetry which is bridged by the issuer providing the investor with disclosures about the IPO, as required by regulations.

10. Issuers are also incentivised to provide relevant information by market forces because they will face a price/valuation penalty from institutional investors if there is uncertainty around their IPO. The NZX also reviews IPOs and has its own standards for listing that must be met.[1]

1.3 Financial Markets Conduct Act 2013 disclosure requirements on businesses issuing equity on publicly listed markets

11. The FMC Act and the Financial Markets Regulations 2014 (FMC Regulations) impose a disclosure regime on issuers to address the underlying information asymmetry between an issuer and investor. The principles of the regime are in the FMC Act. The prescriptive requirements of the regime, in the FMC Regulations, are adjusted over time in response to changing market conditions.

Principled disclosure requirements in the Financial Markets Conduct Act 2013

12. Issuers making a 'first regulated offer' of equity securities to retail investors must provide disclosure in accordance with the FMC Act and Regulations and, for IPOs, the listing rules of the stock exchange.[2] The FMC Act sets out requirements on issuers of financial products:

    a. Section 19 prohibits a person from engaging in conduct that is misleading or deceptive or likely to mislead or deceive in relation to any financial product or any dealing in quoted financial products (a listed equity is a quoted financial product).

    b. Section 82 prohibits false or misleading statements or omissions in a PDS if they are materially adverse for investors.

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[1] NZX listing rules are also relevant, refer to rule 7.4.1.(a)(i) at NZX_Listing_Rules_1.8.2_-_24_July_2024.pdf.

[2] The FMC Act allows issuers to offer non-listed equity securities to non-retail investors without preparing the same disclosure because the disclosure requirements are primarily targeted to retail investors. These equity securities are not publicly traded and examples are property companies, irrigation companies and co-operatives. There are some eligibility criteria set out in the NZX rules, and the NZX Regulation Limited (RegCo) may impose further requirements (or waive certain requirements) at its discretion.

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13. The FMC Act requires issuers doing an IPO to prepare information in a PDS and to provide that information to a potential investor.

14. An issuer that completes an IPO will become an FMC reporting entity provided it meets the requirements of the NZX. It must then compare PFI, if any, with actual results for the next years and also must meet continuous disclosure requirements to update the market of information that would have a material effect on the price of its quoted financial product.

Retail investors are the primary audience for a product disclosure statement

15. Retail investors (non-professional purchasers of stocks/shares) are the primary audience for disclosure required by the FMC Regulations. Institutional investors and financial advisors are secondary audiences for disclosure (as noted in Past MBIE regulatory analysis from December 2014). They have more financial understanding than retail investors, more access to advice, and also more ability to search out disclosures by an issuer. Generally institutional investors rely on other disclosures such as historic performance, broader economic conditions, and the issuer strategy.

16. Retail investors will be best supported to make sound decisions by disclosures that are concise, in plain language, and provide straightforward information. They are less likely to be informed by (or even engage with) material that is too long or complex, eg long financial tables.[3]

17. All disclosure to retail investors should make a clear distinction between the past and the future. Fundamentally, any disclosure of financial information that is future-focused is more complex and uncertain. It must be evaluated carefully by an investor with consideration of the underlying assumptions that have been used.

Prescriptive requirements for prospective financial information in Financial Markets Conduct Regulations 2014

18. The FMC Regulations set out what information must be prepared by an issuer and made available to investors (on the Disclose Register) and what information must be in a PDS, including specific PFI metrics that must be provided to an investor. The purpose of including PFI is to provide investors with forward-looking information about an issuer's future financial performance.

Issuers must prepare detailed PFI statements and include select PFI metrics in a PDS

19. FMC Regulations set out prescriptive requirements about what issuers must provide by way of PFI. They require an issuer to prepare full prospective financial statements for two future accounting periods (the first being $\mathbf{P_{+1}}$ and the second being $\mathbf{P_{+2}}$) in accordance with Generally Accepted Accounting Practice (GAAP) and to release those documents on the Disclose Register[4] (refer to clause 53 of Schedule 3).

20. FMC Regulations clauses 35, 38, and 39 of Schedule 3 require the PDS to include certain specific PFI metrics in two financial information tables in **section 7 (of the PDS)**. Some of these specific PFI metrics are revenues, earnings before interest, tax, depreciation and amortization (EBITDA), net profit after tax, dividends, total assets, and total liabilities.

21. The specific PFI metrics that are provided in a PDS can be complex for a retail investor to understand because it is technical and includes a number of financial metrics that are similar but slightly different. This is illustrated in Figure 1 below, which is an example of a past issuer's PFI.

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[3] Refer to Lefevre, A. and M. Chapman (2017), "Behavioural economics and financial consumer protection", OECD Working Papers on Finance, Insurance and Private Pensions, No. 42, OECD Publishing, Paris, https://doi.org/10.1787/0c8685b2-en. Also MBIE Financial Product Disclosure: Insights from Behavioural Economics (2015)

[4] The Disclose Register is maintained by the Companies Office. Issuers doing an IPO must lodge documents on the Disclose Register which is available to be viewed by investors. PDS documents are actively provided to investors, while documents on the Disclose Register must be searched by investors.

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Figure 1 Selected financial information from New Zealand King Salmon PDS

SELECTED FINANCIAL INFORMATION

FINANCIAL INFORMATION $M	FY2014	FY2015 (RESTATED)[1]	FY2016	FY2017F	FY2018F
Revenue	95.1	98.3	114.1	130.1	143.6
Revenue Growth %	-	3%	16%	14%	10%
EBITDA	5.2	12.4	13.8	21.1	26.1
Pro Forma Operating EBITDA[2]	10.3	12.9	16.0	19.2	22.4
Pro Forma Operating EBITDA growth %	-	25%	24%	20%	17%
Pro Forma Operating EBITDA margin %	11%	13%	14%	15%	16%
Net profit after tax	(1.5)	6.3	2.6	10.1	14.1
Pro Forma Operating NPAT[3]	3.1	6.8	7.9	10.0	11.5
Dividends declared on all equity securities of the issuer[4]	2.6	-	-	5.0	5.6
Total assets	129.7	155.9	165.7	187.2	198.8
Cash and cash equivalents	1.6	5.5	2.4	5.5	0.6
Total liabilities[5]	111.0	119.2	128.7	42.6	45.1
Pro forma operating total debt[6]	20.0	20.6	19.5	10.4	10.3
Net cash flows from operating activities	2.6	6.9	4.1	6.6	11.5

Notes to table:

1. *As New Zealand King Salmon has applied the full provisions of NZ IFRS to FY2016, all FY2015 financial information included in this PDS is restated to reflect the application of full NZ IFRS (including NZ IAS 41-Agriculture and NZ IAS 2-Inventory) as included in the FY2016 audited financial statements.*
2. *Pro Forma Operating EBITDA refers to earnings before interest, tax, depreciation and amortisation, after allowing for the pro forma adjustments outlined on page 60. Pro Forma Operating EBITDA is a non-GAAP profit measure. We consider that Pro Forma Operating EBITDA, which normalises performance for certain structural changes within the business and removes the impact of a number of non-recurring or infrequent items, allows for a better comparison of operating performance over the historical and Prospective Period, and for comparison with that of other companies. However, caution should be exercised as other companies may calculate Pro Forma Operating EBITDA differently. The Offer Register contains full reconciliations between Pro Forma Operating EBITDA and GAAP profit measures.*
3. *Pro Forma Operating NPAT reflects pro forma adjustments reflected within Pro Forma Operating EBITDA as well as to recalculate interest costs as if we had only had bank borrowings in place since 1 July 2013. The pro forma operating tax expense has been adjusted to reflect the tax implications of the pro forma operating adjustments. Pro Forma Operating NPAT is a non-GAAP profit measure and is not determined in accordance with GAAP. The Offer Register contains reconciliations between Pro Forma Operating NPAT and GAAP profit measures.*
4. *We did not declare any dividends between FY2015 and FY2016. The FY2017F and FY2018F dividends reflect the forecast expected payment of interim and final dividends. Refer to Section 6 (Key features of ordinary shares) for further details of our dividend policy.*
5. *Total liabilities includes shareholder loans which have been converted into ordinary Shares or repaid prior to the Offer.*
6. *Pro forma operating total debt represents the closing balance of all bank debt and finance leases. It does not include shareholder loans which have been converted into ordinary Shares or repaid prior to the Offer.*

22. The specific PFI metrics which must be included in a PDS have changed over time. Prior to the 2010-2014 reforms a PDs was required to include the complete statements rather than the specific PFI metrics. Reducing the PDS content to specific PFI metrics made the information more accessible for investors but did not reduce costs for issuers because issuers need to prepare full financial statements for release on the Disclose Register.

New Zealand's accounting standard for generally accepted accounting practice requirements for prospective financial information

23. The FMC Regulations require that any GAAP-compliant PFI must comply with the domestic Financial Reporting Standard No 42 (Prospective Financial Statements) (FRS-42). FRS-42 is a New Zealand accounting standard, maintained by the XRB.
24. FRS-42 sets out principles detailed minimum disclosure requirements for PFI, and sets a higher standard than the GAAP. PFI that is prepared in compliance with FRS-42 is long and detailed. For example, the full PFI statements prepared by New Zealand King Salmon for its IPO are 35 pages long.
25. To our knowledge New Zealand is unique in having a domestic standard (FRS-42) for the application of GAAP to PFI (with the exception of Canada).

Prospective financial information is not prepared as part of business as normal

26. An issuer cannot use existing information such as any budget for the year ahead to quickly and easily prepare PFI for several reasons:
    a. Many businesses prepare budgets using non-GAAP measures meaning a number of reconciliations are required.
    b. Formal budgets tend to be for one financial year (P_{+1}), not two years (P_{+2}).
    c. Budgeting does not follow the requirements set out in FRS-42.

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There are limited grounds in the Financial Markets Conduct Regulations 2014 to not prepare prospective financial information

27. An issuer doing an IPO may prepare a PDS without PFI if, after having made reasonable endeavours to obtain all relevant information, they determine that PFI is likely to deceive or mislead with regard to any detail that is material to the offer (clause 39(c)(i), Schedule 3, FMC Regulations).

28. In practice, stakeholders consider these grounds for not preparing PFI to be very high because they require issuers to do material due diligence (as far as actually preparing draft PFI) before they can determine that the PFI would be likely to mislead or deceive. This imposes material costs on potential issuers, particularly for smaller ones. (Refer to Section 2 for more detail on this issue)

29. The issuers that have not prepared PFI when listing on the NZX are usually in one (or more) of three categories: early-stage firms with limited historical information, operating in a new industry such as medicinal cannabis, or operating with significant uncertainty over key determinants of business performance such as awaiting regulatory approval.

1.4 Prospective financial information in recent Initial Public Offerings in New Zealand

Number and cost of Initial Public Offerings on the New Zealand Stock Exchange in the past decade

30. There have been 14 IPOs from September 2015 to September 2024, nine of which produced a PFI and five did not. One offer was withdrawn.

31. Table 1 below shows the companies, IPO date, total offer (the investment sought from the IPO), and offer costs (all costs for the IPO).

32. All of the IPOs that completed PFI used a mix of GAAP and non-GAAP measures in Section 7 of the PDS. The IPOs that did not prepare PFI were seeking smaller investments and had lower offer nominal costs than the IPOs that prepared PFI, although their offer costs as a proportion of the offer value was higher:

    a. five IPOs without PFI had average offer costs of $1.8 million and an average offer (the value of equity securities on offer) was $27.5 million. The offer cost as a proportion of offer value was 6.5%.

    b. nine IPOs that did prepare PFI had average offer costs of $13.8 million and an average offer of $229.2 million. The offer cost as a proportion of offer value was 6.0%.

33. A larger IPO is expected – due to economies of scale – to have proportionally lower offer costs than a small IPO. The 0.5% reduction in offer costs between IPOs with and without PFI indicates that: (a) the cost of preparing PFI is likely high for large issuers; and (b) there are material costs involved in the high threshold to do an IPO without PFI.

Table 1: Initial Public Offerings on the New Zealand Stock Exchange

Company	IPO date	Total offer (up to $m)	Offer costs ($m)	PFI	Non-GAAP measures in PFI[5]
CBL Corporation Limited	07.09.15	125.4	8.40	Yes	Yes
AFT Pharmaceuticals	22.12.15	35.6	3.50	No	N/A
Tegel Group	03.05.16	298.8	24.70	Yes	Yes
Investore Property Limited	12.07.16	185.0	6.20	Yes	Yes
King Salmon Investments	19.10.16	77.5	5.10	Yes	Yes

[5] For example Pro forma/Non-GAAP reconciled to GAAP

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Company	IPO date	Total offer (up to $m)	Offer costs ($m)	PFI	Non-GAAP measures in PFI[5]
Oceania Healthcare Limited	28.04.17	200.0	10.50	Yes	Yes
Cannasouth Limited	19.06.19	5.0	0.67	No	N/A
Napier Port Holdings Limited	20.08.19	234.0	14.00	Yes	Yes
Rua Bioscience Limited	22.10.20	20.0	1.90	No	N/A
Truscreen Group Limited	22.12.20	2.0	0.33	No	N/A
New Zealand Rural Land Company Limited	18.12.20	75.0	2.60	No	N/A
My Food Bag Group Limited	05.03.21	342.3	16.70	Yes	Yes
Fabric Property Limited	30.09.21	250.0	16.50	Yes	Yes
Winton Land Limited	17.12.22	349.8	22.40	Yes	Yes

Estimated cost of prospective financial information in Initial Public Offerings

34. The cost of PFI for any particular IPO is commercially sensitive to the issuer. Many submitters to the FMA did not know the cost of PFI separate from other financial information prepared for a PDS. One recent issuer who provided information to the FMA said the cost to prepare PFI for their IPO was several million dollars.

35. We conservatively estimate that the total PFI cost is approximately 5-15 per cent of the IPO offer cost. The nine IPOs above that prepared PFI had a total offer cost of $124.5m meaning the total cost of PFI over the past decade is likely to have been between $6.3m - $24.9m.

36. From the FMA's targeted consultation, and data the FMA provided on independent assurance costs of PFI, the PFI cost has three components:

    a. Internal costs of preparing PFI, such as staff time, which are unknown. Some submitters mentioned that an issuer's finance team could be occupied on preparing PFI for 6 months, which signals a sizeable internal cost to prepare PFI.

    b. External costs for independent accounting services, and legal services that range between $0.375m - $1m.

    c. Independent assurance costs ranging around 0.5 per cent - 4.5 per cent of IPO offer cost. This can vary between $0.1m - $1.2m and averages $0.5m (based on previous instances where the FMA has provided independent assurance costs. independent assurance costs).

37. For many IPOs the PFI cost is expected to be at the upper end of our estimates because directors and issuers face liability under section 82 of the FMC Act for any PFI disclosure that is false, misleading or likely to mislead. This liability drives high use of external assurance services to provide confidence in the forward forecasts, assumptions, and estimates involved in PFI.

1.5 International comparison

38. Two thirds of submitters to the FMA's targeted consultation specifically commented on the Australian Securities Exchange (ASX) as a potential alternative market for an issuer to list on and raised comments about the relative difficulty of listing in New Zealand compared to Australia.

39. Currently there are 65 New Zealand companies listed on the ASX, most of which are dual listings but 18 are sole listings. In recent times there have been some high-profile businesses shifting their listings to Australia.

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40. Part of the process for a company deciding whether to list includes deciding where to list either as sole or primary listing. Some issuers have decided to conduct their primary listing in Australia, or to do a sole listing in Australia, rather than New Zealand at least partly due to regulatory costs.

Key features of prospective financial information in Australia

41. Australia requires issuers of financial products to prepare a prospectus (equivalent to a PDS) to provide the information a person would reasonably require to decide whether to acquire the product or make an informed decision about the product (Section 1013D of the Corporations Act 2001 (Australia)).

42. Issuers can choose to include PFI in a prospectus if they think it is information a person would reasonably require to make an informed decision.

43. Australia does not have regulatory requirements for any PFI content that is included in a prospectus – as New Zealand does in the FMC Regulations. The Australian approach has principled legislation and then guidelines from their financial markets conduct regulator, the Australian Securities and Investments Commission (**ASIC**), to shape conduct of issuers. Alongside the guidelines, the Australian approach requires active engagement from the regulator and institutional investors to set good practice by issuers.

44. ASIC Regulatory Guidance 170 sets out when issuers should consider including or excluding PFI. In summary:
    a. If issuers choose to use PFI, there must be reasonable grounds for the PFI (eg sufficient objective foundation for the statement) and must not be misleading.
    b. Financial information should be prepared in accordance with accounting standards and any departures from those standards should be disclosed with reasons.
    c. Issuers otherwise need to give information about their “prospects” under a general disclosure test. This is generally a narrative description, may be in multiple places in the prospectus, and may cause the issuer to emphasise certain historical metrics. Information may be included provided it is not misleading or deceptive.

45. For the past 18 months (FY23 and current FY24) there have been 42 IPOs on the ASX. 26 were for mining companies and none of those prepared PFI. Of the remaining 16, six prepared PFI equating to 37.5 per cent.

46. ASIC provided the FMA with an estimate that in practice around 25 per cent of IPO prospectuses contain PFI (excluding mining), and generally for larger IPOs (broadly, the $100m+ market capitalisation) with a more stable business. These contain usually no more than 18 months’ of forward-looking information and almost always less than 2 years.

Section 2: Diagnosing the policy problem

2.1 The policy problem

The problem

47. The New Zealand regulatory requirement to prepare PFI is imposing significant costs on potential issuers and is reducing the flexibility when preparing an IPO. PFI has been identified as a key barrier to an issuer deciding to list in New Zealand compared to Australia. At the same time the PFI is not meeting the intent of informing retail investors of the potential costs and risks of an investment.

48. This problem was signalled in the recent Growing New Zealand’s Capital Markets 2029 report (CM2029) report and confirmed by recent FMA consultation with relevant

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stakeholder groups and industry.

Capital Markets 2029 report

49. CM2029 was an industry-led report published in 2019, sponsored by the FMA and NZX. It identified ways to improve and grow New Zealand's capital markets with a 10-year view.

50. CM2029 recommended removing the requirement to provide PFI for IPOs. It suggested that New Zealand's PFI settings may be disincentivising firms from listing on the NZX and, at times, contributing to firms preferring to list on the ASX due to its "opt-in" PFI rules.

Financial Markets Authority recent consultation on prospective financial information

51. In mid-2024 the FMA carried out targeted consultation on New Zealand's PFI settings. FMA asked stakeholders for comments on the costs of preparing PFI, the usefulness of PFI for investors, and on options to change PFI settings to improve alignment with Australia and to reduce costs.

52. The FMA received 15 submissions from stakeholders. We have not identified specific stakeholders (apart from the NZX). Stakeholders are grouped into a user group, issuer group, or producer group, according to their activity as shown in the table below.

Stakeholder group	Number and type
Market operator	One market operator
User group – entities that use PFI when preparing analysis to promote IPOs or to invest in IPOs	Two peak bodies (for shareholders and industry), two investment analysts and two institutional investors
Issuer group – businesses that must prepare PFI as part of an IPO	Two recent issuers and one business that considered issuing but did not list
Producer group – entities that prepare or advise on PFI as part of an IPO	Five advisors including accounting and legal businesses

2.2 Further details of the problem caused by the prescriptive regulatory requirements

Prescriptive prospective financial information requirements impose costs on issuers and reduce their flexibility

53. PFI is estimated to cost between 5-15 per cent of the IPO offer cost, as outlined in Section 1.5.

54. Three PFI requirements in the FMC Regulations are adding costs and reducing the flexibility for issuers:

    a. The requirement to prepare PFI for two future years, P_{+1} and P_{+2}.

    b. The requirement for PFI to be GAAP compliant and comply with FRS-42.

    c. The threshold that must be met to do an IPO without PFI.

The problems that arise because of the requirement to prepare PFI for P_{+2}

55. Issuers submitted to the FMA that the requirement to include P_{+2} makes PFI costly. The cost of PFI for P_{+2} is higher than P_{+1}. This is because more due diligence and assurance is needed to minimise the risk of inaccuracies for assumptions and models that go further into the future. It is not clear how much of the cost of PFI is due to P_{+2}.

56. Preparing PFI for P_{+2} also adds risk because it is harder to get forecasts accurate that far into the future. An issuer that did not end up listing said that "The PFI requirement for a two-year forecast is too long of a timeframe to forecast with the degree of accuracy expected for an IPO of significant size and scale".

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57. The P_{+2} requirement is a problem for issuers that are in a growth phase and may find it harder to model their business for 13-24 months. The P_{+2} requirement is likely contributing to fewer of these issuers in New Zealand, although there are other factors.

<u>The problems that arise because PFI must be GAAP compliant and comply with FRS-42</u>

58. New Zealand requires PFI to be GAAP compliant and has a domestic accounting standard (FRS-42) for the forecasting of PFI. This is a key driver of cost for issuers, and imposes a higher level of disclosure than Australia. One submitter said:

    "The requirements of the accounting standard FRS-42 are to produce a set of full financial statements. Producing a full set of financial statements which need to be prepared and then signed-off by the accountants is costly for listing companies."

59. Submitters from the producer group – those accounting and legal businesses that provide services to prepare PFI – provided differing views on the value of GAAP compliance. Three argued strongly for GAAP, while two saw value in GAAP but thought that the FRS-42 requirements were too onerous, and that New Zealand should move to align with Australia and provide more flexibility.

60. The three that supported GAAP argued it provided benefits such as robust and reliable forecasts of future performance to make comparisons and track performance, as well as assurance that the FMC disclosure requirements (eg section 82) are being met.

61. Issuer group and user group submitters (which includes investors) said that the GAAP requirement, particularly FRS-24, makes it more costly for an issuer to prepare an IPO. The exact cost was not mentioned.

62. These submitters often use non-GAAP measures which they say are more useful for investors to understand the business. GAAP and FRS-42 make this harder because the measures should be reconciled back to GAAP. Every one of the nine IPOs that prepared PFI over the past decade voluntarily included non-GAAP financial measures.

63. Some of the non-GAAP measures that submitters think are more useful include:

    a. proforma EBITDA with industry specific adjustments. One submitter mentioned that this measure was the primary measure used by the Board and management (including for management pay incentives)

    b. profit and loss information on a pro-forma basis down to net profit (after tax)

    c. providing a small range for revenue and earnings measures, similar to what companies do after they are listed.

<u>The threshold that must be met to do an IPO without preparing PFI is adding costs and deterring listings</u>

64. The FMC Regulations set a high threshold for an issuer to do an IPO without PFI. This is deterring earlier stage growth companies from an IPO.

65. The threshold to not prepare PFI, outlined in Section 1.3, is high.[6] Submitters to the FMA's consultation raised three issues with the current settings:

    a. The "reasonable endeavours" requirement imposes a significant burden on a potential issuer before a decision can be made. One submitter indicated that meeting the reasonable endeavours requires PFI to be prepared in full and then evaluated before a decision on whether to do an IPO without PFI can be made.

    b. The "deceive or mislead" threshold is high, or at least is interpreted conservatively by issuers, which means PFI is likely to be prepared in instances where it is very costly to prepare because there is little evidence or information available or the future for the business is hard to predict.

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[6] The grounds not to prepare PFI involve a procedural requirement ("having made reasonable endeavours to obtain all relevant information") and a threshold (determine that the "PFI is likely to deceive or mislead with regard to any detail that is material to the offer").

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c. As a combination of the above and the liability risks[7], directors are erring on the side of conservatism, meaning it is likely that more diligence and assurance processes are being applied to PFI than are needed.

66. Data on past IPOs supports the view of submissions that the PFI cost is contributing to fewer early-stage / growth phase issuers. Only 36 per cent (five out of 14) of IPOs on the NZX in the past decade have not prepared PFI. By comparison, 62.5 per cent of Australian IPOs from the past 18 months have not prepared PFI. Both NZX and ASX IPOs that do not prepare PFI are usually smaller or early-stage issuers.

67. Overall the PFI requirements are likely discouraging growth stage issuers and smaller issuers from listing on the NZX in favour of other markets. There are likely other factors at play such as costs of maintaining a listing on the NZX or accessing a larger market through the ASX. Despite these factors, evidence from submitters is that the costs added by PFI requirements is a material factor.

Prescriptive prospective financial information requirements are not delivering the most useful information for retail investors

68. In addition to the costs on prospective issuers, the prescriptive PFI requirements may also not be providing the best information to investors. This is because the PFI that must be required may be too complex or overly-relied on by retail investors, and because the PFI for the second outyear (P_{+2}) is less reliable.

69. Where issuers provide PFI they must provide the specific PFI metrics, although they may include industry-specific measures. Issuers are limited in their ability to provide alternative financial disclosures that could better inform a retail investor of the possible risks and investment returns associated with any IPO.

70. The specific PFI metrics – such as EBITDA or a price-earnings ratio – are complex and may be misunderstood or – in the case of a forecast dividend yield – relied on by a retail investor without examining the underlying assumptions.

71. A user group submitted to the FMA that retail investors either do not engage with PFI (in which case it is excess information they gloss over) or they place an over-reliance on one or two PFI figures without understanding the underlying assumptions and limitations. This exposes the retail investor to risks if they do not notice other disclosures.

72. Submitters also indicated that PFI is not necessary for institutional investors and advisors to prepare their market commentary. Institutional investors and advisors use a wide range of information to work out valuations, including historic performance, governance arrangements, business strategy, industry performance, and future risks.

73. Additionally, the requirement to prepare PFI for P_{+2} means investors are getting a mix of reliable and less reliable information in the PFI. P_{+2} forecasts are less reliable than P_{+1}. FMA analysis indicates that all IPOs on the NZX from the past decade that provided PFI delivered actual dividends and revenue that exceeded the PFI for P_{+1}. But only 62.5 per cent – 75 per cent of IPOs met their expected performance in P_{+2}:

    a. five out of eight[8] IPOs met or exceeded the revenue forecast.

    b. six out of eight IPOs met or exceeded the dividend forecast.

74. Retail investors may not know the different reliability between P_{+1} and P_{+2}. They are likely to place significant weight on any PFI as an expected outcome, especially a predicted dividend forecast.

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[7] Section 82 of the FMC Act has a general disclosure obligation, it requires that any disclosure must not be false, misleading or likely to mislead. Any contravention can create a liability for directors of companies under sections 533 and 534 of the FMC Act in certain circumstances. Section 533 requires directors to be “involved in a contravention”, and section 534 is a deeming provision that only applies section 82, and has a number of defences. The FMA may seek a court to order pecuniary penalties (eg up to $1 million for an individual or $5 million for any other case) or for compensation to an affected person.

[8] The FMA can only compare PFI to actuals for the eight IPOs that were completed.

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Issuers can list on the Australian Stock Exchange and then issue into New Zealand, which means investors do not get the protections of New Zealand regulations

75. One submitter noted that issuers can choose to primary list on ASX and offer equity into New Zealand using a Corporations Act 2001 (Australia) prospectus and the mutual recognition regime.

76. This provides the ability for reverse listing where a New Zealand company could list on the ASX (with lower costs, and without New Zealand's PFI requirements) then offer equity securities to New Zealand investors providing whatever PFI disclosures they prepared for the Australian market.

77. This potentially undermines the effectiveness of PFI requirements in New Zealand.

The problem is expected to persist if no action is taken

78. Without any changes, it is expected that the current PFI requirements, and the problems outlined above, will continue.

2.3 What objective is sought in relation to the policy problem?

79. The objective is to ensure any regulations for PFI support:

    a. efficient and transparent markets that contribute to economic growth and do not have any unnecessary costs for issuers considering an IPO, particularly compared to other jurisdictions where an issuer may be considering listing, and

    b. confident and informed participation in offers of relevant financial products by retail investors who have access to appropriate disclosure information.

80. Regulatory provisions adding costs that do not contribute to the confident and informed participation of retail investors can be removed because the regulations are not addressing the information asymmetry.

81. There is a trade-off where any regulatory changes reduce costs to issuers by removing regulation that requires the issuer to provide disclosures that support confident and informed participation of retail investors. The criteria prepared under Section 3.1 should highlight this trade-off if it occurs.

Section 3: Deciding upon an option to address the policy problem

3.1 What criteria will be used to compare options to the status quo?

82. We have developed four criteria to assess the options against the status quo. These criteria reflect the purpose of the financial markets regulatory system as it relates to the issue of PFI disclosure:

    a. **Appropriate information for investors** – whether the information that an issuer prepares in their PFI (or in the absence of a PFI) is the sort of information that retail investors need and can understand to make decisions.

    b. **Reliable information for investors** – whether the information that an issuer prepares in their PFI can be relied upon to make investment decisions.

    c. **Flexibility for issuers** – whether issuers have choices that allow them to prepare the most suitable information for their listing.

    d. **Costs for issuers** – whether costs faced by the issuer due to regulation (direct costs and indirect costs) are reduced.

83. The four criteria are weighted equally. They reflect the most relevant elements of the purposes of the FMC Act to the issue of PFI disclosure and provide an equal weighting to issuer and investor needs. The first two criteria focus on whether PFI addresses the

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information asymmetry issue between issuers and investors.

84. There is no overlap between the criteria focused on investors. Whether information is appropriate is a matter of investor understanding. Whether information is reliable is about accuracy or certainty of the information. Forecast financial information can be appropriate for an investor but not be reliable and vice-versa.

85. There is minor overlap between the criteria that focus on issuers because flexibility and cost can be related. This overlap has been minimised and is considered acceptable. Flexibility has been defined as the existence of choice while reduced costs is defined as whether the costs of disclosure that is required will be lower. Where issuers have choices with different costs, this is reflected in a range for the costs criterion.

86. There is no criterion on economic growth or efficiency because it is not considered necessary and is also difficult to assess. Regulatory settings that address information asymmetry with minimal costs should be efficient and contribute to economic growth.

3.2 What scope will options be considered within?

87. Only options that change the PFI requirements in the FMC Regulations are being considered. The following are out-of-scope:

    a. Legislative changes to the FMC Act. For example, there will not be any changes to the requirements in s82 of the FMC Act to not make false or misleading statements, or to director and advisor liability settings.

    b. Changes to other PDS requirements in the FMC Regulations, such as the 60 page limit.

    c. Changes to GAAP, including accounting standards such as FRS-42 which are maintained by the XRB.

3.3 What options are being considered?

The options we are considering and those we are not considering

88. The table below shows the four options we are considering along with the status quo. The options are described and analysed below then compared in the following section.

Option	Description
Status quo	Require FRS-compliant PFI for P_{+1} and P_{+2} unless it would deceive or mislead
1	Require FRS-compliant PFI for P_{+1} with lower threshold to 'opt-out'
2	Require PFI of any form for P_{+1} with lower threshold to 'opt-out'
3	'Opt-in' GAAP compliant (but not FRS-42 compliant) PFI for P_{+1}
4	'Opt-in' PFI of any form for P_{+1}

89. The table below shows options we are not considering with the reasons.

Option	Reason
Require GAAP-compliant PFI for P_{+1} with lower threshold to 'opt-out'	This is half-way between Options 1 and 2 and was not considered necessary to analyse because Options 3 and 4 perform better than Options 1 and 2.
'Opt-in' FRS-42 compliant PFI for P_{+1}	This option was not considered workable because the flexibility of an opt-in regime does not match with a highly prescriptive accounting standard.
Reduce the specific PFI metrics that are to be included in a PDS	The specific PFI metrics were chosen in 2014 as a targeted set for investors. We do not have sufficient information to choose a further sub-set that will reduce costs to issuers, while still providing meaningful information to investors.

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Option	Reason
Remove all regulatory requirements	This option was not considered. It may have unintended consequences because the regulations prescribe other IPO requirements in detail. Option 4 is intended to provide issuers with flexibility that is similar to this option.

All options reduce duration of prospective financial information to P_{+1}

90. All of the options reduce the duration of PFI to P_{+1}. This is because there was near unanimous support in submissions to the FMA for reducing the duration of PFI from P_{+1} and P_{+2} down to P_{+1}.

91. This change benefits issuers. P_{+2} added significant extra costs and risk to an IPO because it was harder to form assumptions and model that far into the future.

92. Removing P_{+2} has a slight benefit to investors. It removes the less reliable information for the second year (P_{+2}) of trading, which investors should use with far more caution than the first year (P_{+1}). This outweighs the slight disadvantage as investors will only be able to use PFI to hold issuers to account for performance over the first year.

Status Quo

93. Under the status quo, any issuer doing an IPO must disclose GAAP-compliant PFI that covers P_{+1} and P_{+2}. Alternatively, a high threshold must be met before an issuer may do an IPO without disclosing PFI.

94. None of the 15 submissions to the FMA supported retaining the current regulatory settings for the various reasons outlined in the problem above.

Evaluation of option against criteria	
Appropriate information for investors	Retail investors may not be well informed because PFI disclosure can be complex with multiple financial metrics. Headline PFI figures in a PDS such as NPAT, or Earnings per Share are hard to understand. Retail investors may rely on these without noticing other disclosures investment risks.
Reliable information for investors	Any PFI is relatively reliable for a retail investor because it is GAAP compliant and follows FRS-42. But PFI forecasts for P_{+2} are only 62.5 per cent to 75 percent reliable.
Flexibility for issuers	Limited flexibility for issuers. Regulations require PFI for an IPO. There is a high threshold that must be met to do an IPO without PFI. Proportionally more New Zealand issuers are producing PFI than Australian issuers. Some issuers do not have flexibility to do an IPO without PFI in New Zealand when they could in Australia.
Costs for issuers	The current regulatory settings impose significant compliance costs for issuers. One issuer mentioned that PFI cost several million dollars for their IPO. We estimate the PFI cost varies between 5-15 per cent of the total cost of an IPO offer.

Option 1: Require GAAP and FRS-42 compliant PFI for P_{+1} with lower threshold to 'opt-out'

95. Under this option any issuer doing an IPO must provide PFI that is GAAP-compliant and covers the future period P_{+1} in the PDS.

96. The threshold for an issuer to do an IPO without PFI would be lowered and the process requirement (to make reasonable endeavours) removed. The lower threshold would likely be that an issuer may do an IPO without PFI if the issuer determines they do not have a reasonable objective basis (of information or facts/data) from which PFI can be prepared for any part of the required time period.

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97. A reasonable objective basis could be linked to the availability of information to develop assumptions and models that support clear and accurate PFI. Without a good foundation, any PFI is likely to be costly to prepare and less likely to be reliable for an investor.

98. In that instance, a preferable disclosure would be an explanation of the reasons for why PFI has not been prepared. This informs an investor of the uncertainty and risk.

99. The modified threshold and process is not expected to make a significant shift in issuer behaviour. This is because the default obligation is to prepare PFI, and the overarching disclosure requirements in the FMC Act (especially section 82) with the relevant liability for issuers and directors are likely to drive behaviour.

100. This option does not align with Australia.

101. This option has a low risk of any unintended consequences or risks to investors from reduced disclosures.

Evaluation of option against criteria	
Appropriate information for investors	Investors will receive similar information as the status quo, for only P_{+1}. A few extra issuers will do an IPO without PFI they will provide retail investors with appropriate information that highlights the underlying risks or uncertainty of the investment. Institutional investors will still have access to broader disclosures in the PDS for example the business strategy, key drivers of returns and key risks.
Reliable information for investors	Improved reliability because P_{+2} is removed. PFI for P_{+1} is generally reliable. Issuers can only opt-out of preparing PFI if there was not reliable evidence to prepare PFI, this does not reduce reliability of information to investors.
Flexibility for issuers	It is marginally easier for issuers to do an IPO without PFI which may help a few issuers. However, this does not improve flexibility overall because the FMC Regulations still require PFI.
Costs for issuers	Reduced costs for all issuers by removing the costs associated with P_{+2}, and by allowing a few issuers to more easily do an IPO without PFI.

Option 2: Require PFI of any form for P_{+1} with lower threshold to 'opt-out'

102. This option would amend the Regulations to require issuers to prepare PFI, where that PFI does not have to be GAAP or FRS-42 compliant and is only for P_{+1}. This option applies the same lower threshold to 'opt-out' as Option 1.

103. Under this option issuers could provide non-GAAP metrics, such as industry measures, or other metrics with commentary explaining what the financial information is that they are providing. Issuers will need to explain any financial measures they use with a clear explanation of the basis of calculation. If issuers use non-GAAP metrics then they do not have to reconcile (by financial calculations) that metric to a GAAP metric.

104. Guidance from the FMA and/or NZX may be needed to ensure any PFI disclosures are high quality. The FMA can already issue guidance and has some guidance on Disclosing non-GAAP financial information, that could be expanded to apply to PFI.

105. This option is more closely aligned with Australia than Option 1 but is not fully aligned. The key difference is that Australia operates an 'opt-in' model.

106. This option was not considered by most submitters to the FMA. It removes the domestic accounting standards which are highly valued by most producer group submitters. However, it does not fully align with Australia's 'opt-in' model that has flexibility on GAAP which was supported by most issuer group and user group submitters.

107. As with option 1, this option is not expected to make a significant shift in issuer behaviour. The default obligation is to prepare PFI, and the overarching disclosure

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requirements in the FMC Act (especially section 82) with the relevant liability for issuers are likely to drive behaviour. There is low risk of any unintended consequences or risks to investors from reduced disclosures.

Evaluation of option against criteria	
Appropriate information for investors	Retail investors may receive shorter financial disclosures with accompanying explanation that they can more readily understand. However, they may also find different disclosures harder to understand or compare to past performance which will be reported using GAAP measures. There is a risk that investors or analysts find it harder to compare possible investments where PFI uses non-GAAP measures. However, this is considered unlikely because the market forces of institutional investors working with issuers should prevent this risk from eventuating.
Reliable information for investors	Information reliability will vary. The removal of P_{+2} improves reliability but the removal of GAAP and FRS-42 reduces the reliability from the status quo. Any risk of unreliable information is small because issuers will need to explain the financial measure they are using and the FMC Act requires issuers not to provide false or misleading information (section 82), and there are market forces (eg institutional investors, regulatory expectations, NZX) that incentivise issuers to prepare thorough information.
Flexibility for issuers	As per Option 1.
Costs for issuers	As per Option 1 plus lower costs for issuers that do not need to prepare GAAP and FRS-42 compliant PFI. The size of any savings is unknown. Some risk-averse issuers may still follow GAAP and/or FRS-42 to minimise liability risk of non-compliance with FMA Act (eg section 82).

Option 3: 'Opt-in' GAAP compliant PFI for P_{+1}

108. This option involves removing the mandatory requirement to prepare PFI. Instead, any issuer doing an IPO may choose whether to 'opt-in' to preparing PFI as part of their disclosures. If an issuer 'opts-in' to preparing PFI then that PFI must comply with requirements in the FMC Regulations.

109. FMC Regulations would allow an issuer to choose whether to prepare PFI or not based on what they think fit and how they expect the market to respond to their IPO. Issuers may:

    a. not include PFI and disclose why no PFI is provided

    b. prepares PFI for the future period P_{+1} and comply with GAAP, but not FRS-42. Non-GAAP metric may be used if they are reconciled to GAAP using calculations to show how the non-GAAP metric relates to a GAAP metric.

110. Regulations do not need to signal when an issuer should "think fit" to provide PFI because issuers can rely on the existing direction from the requirements in section 49 and 82 of the FMC Act to provide the information needed by a prudent, non-expert investor, and not to provide false or misleading information. Market forces will push issuers of larger IPOs to disclose PFI or face valuation pressure.

111. This option is close to being aligned with Australian settings but still sets a higher regulatory expectation of PFI. The key point of difference is that the New Zealand regulation would require any PFI to be GAAP compliant. By contrast in Australia, there are no mandatory regulatory requirements for PFI. Guidance from the regulator ASIC expects PFI to be GAAP compliant but allows non-GAAP provided it is explained and also allows narrative descriptions of future 'prospects'.

112. There was some support for this option from submitters to the FMA:

    a. There was support for moving an opt-in model where an issuer may choose to

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prepare PFI while providing reasons if they do not.

b. Three out of five submitters in the producer group strongly support retaining GAAP compliance in regulations.

113. However two submissions from the issuer group argued strongly against retaining GAAP as it adds costs and reduces their ability to provide other financial metrics, which they considered to be better indicators of performance.

114. The move to an 'opt-in' model should give issuers more confidence to do an IPO without preparing PFI. This is expected to result in higher numbers of IPOs without PFI.

115. There is a small risk that retail investors in the market for IPOs in New Zealand have less confidence if there are more IPOs without PFI. This risk is unlikely to eventuate because the PFI changes are highly targeted and the rest of the FMC Act requirements and disclosure regulations are unchanged.

116. This option may have dynamic benefits for investors and issuers if it encourages more growth companies to list if they can do an IPO without PFI.

Evaluation of option against criteria	
Appropriate information for investors	Investors receive more useful information that explains any future uncertainty or risks when issuers do IPOs without PFI. This is expected to happen more as there may be extra IPOs that would not happen under the status quo. Retail investors less likely to over-weight PFI figures when they are made with complex underlying assumptions to address uncertainty about the future because those issuers are less likely to prepare PFI. Institutional investors will still have access to broader disclosures in the PDS for example the business strategy, key drivers of returns and key risks.
Reliable information for investors	Improved reliability because P_{+2} is removed. PFI for P_{+1} is reliable and GAAP compliant. More issuers would likely choose to do IPOs without preparing PFI. These are expected to be mostly early-stage growth companies or issuers raising smaller amounts of capital with some instances where PFI is too costly to prepare due to uncertainty. These issuers will provide appropriate disclosures which will be reliable in a different way. The risk of unreliable information is likely low because the FMC Act requires issuers not to provide false or misleading information (section 82), and market forces incentivise issuers to prepare thorough and accurate information.
Flexibility for issuers	Issuers have a choice to prepare PFI or not. More issuers will be able to do an IPO without PFI. This may result in a change in the quality of issuing candidates which will be monitored over time. Any issuers that opt to prepare PFI will still need to follow GAAP. Many submitters to the FMA from the issuer group wanted the flexibility to be able to prepare alternative PFI disclosures more easily, for example earnings ranges without reconciliation to GAAP.
Costs for issuers	Reduced costs for issuers that do IPOs without PFI due to the 'opt-in' approach. Some issuers that would not have done an IPO under current settings may do IPOs with this option in place. Issuers that do PFI face lower costs because P_{+2} is not required.

Option 4: 'Opt-in' PFI of any form for P_{+1}

117. This option gives issues the flexibility to choose to 'opt-in' to prepare PFI or not and providing appropriate reasons or explanation for their decision. If an issuer 'opt-in' then it may prepare PFI in any form it wants for the next financial year (P_{+1}).

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118. Some examples of the forms that PFI could take are:

    a. non-GAAP compliant, meaning it has other accounting or industry measures that are clearly explained with information on the basis of the calculation; this could include PFI in the form of earnings guidance or ranges

    b. GAAP compliant, meaning it may use GAAP metrics or non-GAAP metrics provided they also show how those metrics can be reconciled to a GAAP metric (but PFI does not need to comply with FRS-42); or

    c. FRS-42 compliant PFI.

119. Regulations do not need to signal when an issuer should choose to 'opt-in' and provide PFI because there is direction from the FMC Act, and there is expected to be guidance from the FMA and/or NZX. Market forces of institutional investors will likely also require larger IPOs to prepare PFI or face a price/valuation impact.

120. Guidance from the FMA and/or NZX are likely to be needed to ensure any PFI disclosures are high quality and issuers provide PFI when it is expected. FMA can already issue guidance and has some on Disclosing non-GAAP financial information, that could be expanded to apply to PFI.

121. Under this option the New Zealand regulatory requirements for PFI in the FMC Act and Regulations would be close to alignment in effect with the Australian settings in the Corporations Act (Australia) in that they would not prescribe the form of PFI but allow issuers to choose from multiple approaches. Guidance equivalent to the ASIC guidance – from FMA or NZX – may be needed to support market forces and ensure that best practice disclosures are provided by issuers doing an IPO. Any guidance should impose minimal extra costs and should be flexible to change over time as needed. Two-thirds of submitters to the FMA supported alignment with Australia.

122. Many of the issuer group and user group submitters supported more flexibility to provide non-GAAP PFI metrics in a PDS as long as it is clear what information is prepared and the basis on which it has been prepared. One user group wanted GAAP retained because it provides reliability and consistency for retail investors.

123. Many producer group submitters do not support removing the regulatory requirement to prepare GAAP because it could undermine the financial reporting framework, dilute the quality of IPOs and result in investors receiving misleading and inconsistently prepared information. However, two producer group submitters thought the GAAP requirement could be relaxed to improve alignment with Australia and allow issuers to provide non-GAAP information more easily.

124. There are some risks that retail investors may receive less reliable information if issuers do not follow standardised accounting practices. There is also a risk that financial disclosures will be less comparable. However, this should be minimised by the broader regulatory framework that will maintain the quality of IPOs – including the anticipated guidance that will be prepared and FMC Act requirements to provide the information needed by a prudent, non-expert investor, and not to provide false or misleading information. Market forces will also encourage quality, and comparable, disclosures for larger IPOs.

125. This option may result in lower quality disclosure by issuers, and changes in the quality of issuers which could impact the confidence of retail investors. This will be monitored.

126. However, this option has the highest chance of more IPOs and growth of New Zealand's capital markets. More growth companies conducting listings could improve the range of investment opportunities for retail investors and provide dynamic efficiency gains and economic growth in the long-term.

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Evaluation of option against criteria	
Appropriate information for investors	Retail investors may receive shorter financial disclosures with more use of non-GAAP measures and descriptions or explanations as needed. These should be understandable, with no more complexity than the status quo. Retail investors are less likely to overweight PFI in decisions. Instead they may focus more on other key disclosures such as business strategy, key drivers of returns and key risks, or reasons why PFI cannot be prepared. However, retail investors may find different financial disclosures hard to understand or compare to past information. Retail and institutional investors may find it harder to compare historic financial information in the PDS (which is GAAP-compliant) with any alternative PFI disclosures. Institutional investors may find it harder to compare possible investments with non-GAAP information.
Reliable information for investors	Information reliability will vary. The removal of P_{+2} improves reliability but the removal of GAAP and FRS-42 reduces reliability. Any risk of unreliable information, including from more issuers doing IPOs without PFI, is low (or concentrated to a subset of potential issuers) because issuers must explain the financial measures they are using to ensure investors understand what is provided. Additionally, the FMC Act requires issuers not to provide false or misleading information (section 82), and market forces incentivise issuers to prepare thorough and accurate information.
Flexibility for issuers	Issuers have flexibility to opt-in to providing PFI if they think fit and to provide PFI in whatever form they want. This will give issuers the flexibility to provide: a range of prospective scenarios and revenue forecasts rather than single point forecasts. Issuers could not provide PFI and instead discuss their business model and strategic risks or market dynamics that could impact future performance.
Costs for issuers	Issuers regulatory costs are reduced by removing P_{+2} and the costs associated with GAAP-compliance. Issuers face lower costs doing an IPO without preparing PFI. Reductions in cost are not certain. Some risk-averse issuers may prepare GAAP-compliant PFI as an assurance that they are meeting FMA Act requirements and minimising any liability risk. Regulatory guidance would mitigate this risk.

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3.4 How do the options compare to the status quo

	Status Quo	Option 1: Require GAAP and FRS-42 compliant PFI for P_{+1} with lower threshold to 'opt-out'	Option 2: Require PFI of any form for P_{+1} with lower threshold to 'opt-out'	Option 3: 'Opt-in' GAAP-compliant PFI for P_{+1}	Option 4: 'Opt-in' PFI of any form for P_{+1}
Appropriate information for investors	Retail investors receive complex financial information. **0**	Retail investors get similar information to status quo but for a shorter time period. **0**	Shorter PFI that may be more easily understood. Some risks from difficulty understanding PFI (retail investors) and comparing IPOs. **(1) - 1**	Retail investors likely to get more concise and shorter information from GAAP/non-GAAP PFI and more IPOs without PFI. Some small risks. **0 - 1**	More concise and shorter information from non-GAAP PFI and more IPOs without PFI. Some risks from difficulty understanding PFI and comparing IPOs. **(1) - 1**
Reliable information for investors	PFI for P_{+1} is highly reliable, but P_{+2} is less reliable. **0**	Removal of P_{+2} improves reliability, and PFI is GAAP and FRS-42 compliant which is reliable. **1**	Removal of P_{+2} improves reliability. Non-GAAP PFI may be less reliable. Issuers without reasonable information 'opt-out' and explain why. **(1) - 1**	Removal of P_{+2} improves reliability and GAAP compliant PFI is reliable too. More IPOs without PFI due to 'opt-in' approach. **1**	Removal of P_{+2} improves reliability. Non-GAAP PFI may be less reliable. More issuers disclose other future-focused metrics. More IPOs without PFI. Risks managed by legislative settings and market forces. **(1) - 1**
Flexibility for issuers	Issuers face high threshold and have little flexibility. **0**	No overall improvement to flexibility because Regulations still require PFI. **0**	No overall improvement to flexibility because Regulations still require PFI. **0**	Opt-in improves flexibility but GAAP compliance limits choice for issuers slightly. **1**	Issuers may opt-in and have flexible pathways to provide any form of PFI they want. **2**
Costs for issuers	PFI imposes high costs, especially due to P_{+2} and GAAP compliance. **0**	Reduces costs by removing P_{+2}. minimal change to the number of issuers that will 'opt-out'. **1**	Reduces cost by removing P_{+2} and GAAP / FRS-42. Some issuers may have costs for assurance to manage liability risk. **1 - 2**	Reduces cost by removing P_{+2} and removing FRS-42. More issuers will do IPO without PFI due to opt-in. Some issuers have costs to manage liability risk. **1 - 2**	Highest cost reduction by removing P_{+2} and GAAP and FRS-42, as well as shifting to opt-in meaning more issuers do IPO without PFI. Some issuers have costs to manage liability risk. **2**
Overall assessment	**0**	**2**	**(1) - 4**	**3 - 5**	**2 - 6**

Example key for qualitative judgements:

(1)	worse than the status quo	0	about the same as the status quo	**2**	much better than the status quo
(2)	much worse than the status quo			**1**	better than the status quo

Ranges have been used where the outcome an option could deliver is unclear. A judgement of (1) - 1 indicates a range from 'worse than the status quo' to 'better than the status quo'.

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3.5 What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

127. On balance, Option 4 is the preferred approach as it is most likely to meet the objective and deliver the highest benefits.
128. Option 4 provides the most potential benefit to issuers but with some risks to retail investors. Issuers should have the most flexibility to opt in to a PFI regime if they want and to disclose whatever financial information / future-focused performance information they consider to be relevant. The ability for issuers to prepare non-GAAP compliant PFI for only P_{+1} means Option 4 reduces costs for issuers the most.
129. Option 4 has possible benefits for investors as PFI should be shorter, more concise and easier to understand and it may highlight possible risks or uncertainty about the future. Shorter PFI should also point investors to other information in the PDS which is important to evaluate a possible investment opportunity.
130. However, Option 4 provides these benefits to issuers at a potential risk to investors. The outcome for investors is less certain under this option and there are down-side risks of less reliable information if issuers do not follow accounting practices or standards. However these risks should be managed by the broader regulatory system including expected regulatory guidance clarifying when and what PFI should be disclosed, general legislative requirements that protect investors interests, and market forces.
131. Option 4 aligns New Zealand with Australia's requirements and is expected to encourage more potential issuers to list in New Zealand, which should provide dynamic efficiency benefits and improved investment options for investors over time.
132. Stakeholder submissions provided strong support for aligning New Zealand's PFI requirements with Australia.
133. The following section is completed for Option 4 because of the stakeholder support and the potentially higher benefits overall, recognising the possible downside risks to investors.

3.6 What are the marginal costs and benefits of the option?

Affected groups *(identify)*	**Comment** *nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks.*	**Impact** *high, medium or low for non-monetised impacts.*	**Evidence Certainty** *High, medium, or low, and explain reasoning in comment column.*
Additional costs of the preferred option compared to taking no action			
Regulated groups (issuers)	Transitional cost for any issuers considering IPO while new PFI settings are bedding in.	Low	High
Investors (retail and institutional)	Risk that some information is less reliable for a retail investor because it is not GAAP compliant. PFI may not be prepared when the investors expect PFI to be prepared. The Australian regime has an 'opt-in' approach and has not encountered this issue.	Medium-low	Medium
Assurance providers	One-off cost to adjust to new regulatory requirements.	Medium	High

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	Ongoing reduced revenue due to PFI being prepared less often and less GAAP/FRS-42 compliant PFI. Data from the FMA shows less frequent use of PFI in Australia compared to New Zealand, expect fewer IPOs in New Zealand to prepare PFI.		
Regulators (FMA)	One-off cost to engage with industry during transition. Ongoing monitoring costs increase with more pre-IPO reviews if there is an increase in the number of IPOs. Ongoing costs of creating and maintaining guidance.	Low	High
Total monetised costs			
Non-monetised costs		*Low*	*High*
Additional benefits of the preferred option compared to taking no action			
Regulated groups (issuers)	Ongoing benefit from improved efficiency of IPOs by reducing costs PFI which are currently between 5 – 15 per cent of the total IPO cost, sometimes several million dollars. Expect more IPO of early-stage (growth) issuers and issuers raising lower amounts of capital without PFI – these issuers will face reduced costs because of the shift to an 'opt-in' model.	Moderate	High
Investors (retail and institutional)	Some alternative disclosures may be more easily understood by retail investors which could help them to make informed decisions. More IPO opportunities and therefore more investment opportunities on NZX.	Low	Medium
Assurance providers	More IPOs which may provide additional revenue.	Low	Medium
New Zealand Stock Exchange	PFI changes encourage more IPOs which would benefit New Zealand stock exchange. The FMA consultation and advice signals that PFI changes are a small but material component for issuers deciding whether to list, and where to list.	Low	Medium
Total monetised benefits			
Non-monetised benefits		*Medium*	*Medium-high*

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Section 4: Delivering an option

How will the new arrangements be implemented?

134. The new arrangements will be implemented by amendments to the FMC Regulations.

135. The regulatory changes would be publicised to ensure market participants and investors are aware of the change. MBIE and the FMA will prepare communications to help ensure all relevant issuers and investors are aware of the changes. The NZX and professional advisors and industry groups will likely prepare communications too.

136. The FMA will engage with the sector (including professional advisors) as regulatory changes are made, setting out initial views on what is expected of issuers and investors in IPOs.

137. FMA engagement will inform MBIE and the FMA's understanding of how the changes are being implemented in order to provide appropriate longer-term tools such as detailed guidance to support best practice conduct by industry. A key goal is to ensure all market participants have a common understanding of what might lead them to choose to develop PFI as part of an IPO, and the quality of the PFI that they should prepare.

How will the new arrangements be monitored, evaluated, and reviewed?

138. MBIE and the FMA will monitor the new arrangements, in consultation with the NZX. Monitoring will focus on:

    a. conduct of any businesses that are preparing to do an IPO and the disclosures they are preparing.

    b. any concerns from investors about difficulty understanding disclosures

    c. effectiveness of market forces and initial sector engagement to drive positive outcomes such as reduced costs and preparation of appropriate disclosures for investors

    d. areas of concern or industry uncertainty that will be addressed in guidance

    e. performance of issuers that have done IPOs without PFI compared to their disclosures and comparable listed entities.

139. A specific focus is monitoring whether the industry adopts either a conservative approach to the new PFI settings and continues to produce PFI when it is not needed or an overly risky approach where more issuers are doing IPOs without PFI than expected. We expect conduct in the New Zealand market should be roughly comparable to Australia. In the event that monitoring signals any issues, further guidance from the FMA is the first likely response.

140. The disclosure requirements in the financial markets conduct regulatory system have been in place for about ten years since the reforms of 2010-2014. MBIE plans to review disclosure settings to ensure they are effective and efficient. Any review will consider how effective the changes to PFI settings are to ensure they are having the intended effect.

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