

Going Dutch on Accounting in New Zealand?

Martien Lubberink

TE HERENGA WAKA—VICTORIA UNIVERSITY OF WELLINGTON

My accounting journey

- At high school in the Netherlands, I learned:
 - Cost accounting
 - Bookkeeping for manufacturing companies, including
 - Allocation of indirect costs.
 - Standard cost calculations, variances.
 - Preparation of Financial statements.
 - Annuities, discounting, time value of money.

My accounting journey

- At high school in the Netherlands, I learned:
 - Cost accounting
 - Bookkeeping for manufacturing companies, including
 - Allocation of indirect costs.
 - Standard cost calculations, variances.
 - Preparation of Financial statements.
 - Annuities, discounting, time value of money.
- **Missing: anything to do with stock markets.**

My accounting journey

- At high school in the Netherlands, I learned:
 - Cost accounting
 - Bookkeeping for manufacturing companies, including
 - Allocation of indirect costs.
 - Standard cost calculations, variances.
 - Preparation of Financial statements.
 - Annuities, discounting, time value of money.
- Missing: anything to do with stock markets.
- **I enjoyed it and went on to study Economics / Accounting at the University of Groningen.**

My accounting journey

- After finishing my Phd (Groningen, Maastricht)
 - Lancaster university (2000 – 2008)
 - The Netherlands Bank (Central Bank) until 2013.

My accounting journey

- After finishing my Phd (Groningen, Maastricht)
 - Lancaster university (2000 – 2008)
 - The Netherlands Bank (Central Bank) until 2013.
- At THW-VUW
 - Research: bank accounting, climate change.
 - Teaching: accounting

Some observations

- There's a large demand for accounting knowledge.
- Examples:
 - Budgeting and performance measurement especially at local governments
 - Classification of hybrid securities
 - Bank capital versus bank equity
 - Business models and balance sheets
 - Groups and conglomerates
 - **The language of business**
- The demand for accounting knowledge has no end.

Some observations

- There's a large demand for accounting knowledge.
- Examples:
 - Budgeting and performance measurement especially at local governments
 - Classification of hybrid securities
 - Bank capital versus bank equity
 - Business models and balance sheets
 - Groups and conglomerates
 - **The business of language**
- The demand for accounting knowledge has no end.

Example: The business of language and the temptation of hybrid securities

See documentation of Perls X securities by the [Commonwealth bank](#).

An introduction to bank hybrid securities

Welcome to this module on basic things you should know about investing in bank hybrid securities.

- Many banks issue hybrid securities.
- Why:
 - Regulatory requirements to protect depositors from low equity capital and high leverage
 - Counts as **equity** for the bank regulator
 - Counts largely as **equity** for credit rating agencies
 - Counts as **debt** for the IRD: interest is tax deductible(!)
 - High reward for the investor: 90-day bank bill rate + 3.40%.
 - Everybody happy!

The business of language

4.2.3 Distributions may not be paid

Payment of a Distribution is subject to:

- CBA, in its absolute discretion, making the Distribution;
- payment not resulting in a breach of CBA's capital requirements under APRA's prudential standards as they are applied to the CBA Level 1 Group or the CBA Level 2 Group;
- payment not resulting in CBA becoming insolvent; and
- APRA not otherwise objecting to the payment.

No Distribution will be paid on Exchange where Exchange occurs due to a Capital Trigger Event or a Non-Viability Trigger Event.

Distributions may not be paid if CBA's Common Equity Tier 1 Ratio falls into the capital conservation buffer. For further information, see Section 3.8.1 "Capital adequacy".

Distributions that are not paid do not accrue and will not be subsequently paid. Non-payment of a Distribution on the relevant Distribution Payment Date will not be an event of default and CBA will have no liability to Holders in respect of the unpaid Distribution. However, from that Distribution Payment Date and until a Distribution is paid in full on a subsequent Distribution Payment Date (or all PERLS X are Exchanged, Redeemed or otherwise terminated), CBA cannot (subject to certain exceptions):

- declare or determine a **dividend** on Ordinary Shares; or
- return any capital or undertake any buy-backs or repurchases in relation to Ordinary Shares.

To prevent these restrictions from occurring, CBA must pay all Distributions when scheduled, or, if all or any part of a Distribution is not paid when scheduled, in full within 5 Business Days of the Distribution Payment Date. Therefore, CBA would expect to give priority to payments of Distributions and other similar Tier 1 Capital distributions to enable CBA to be able to continue paying Ordinary Share dividends.

Further, under the terms of some other securities issued by CBA, CBA may not be able to pay Distributions if it does not pay distributions on those other securities. If this occurs, the dividend and capital restrictions outlined above will apply.

4.2.1 Investments in PERLS X are not deposit liabilities or protected accounts under the Banking Act

Investments in PERLS X are an investment in CBA and may be affected by the ongoing performance, financial position and solvency of CBA. They are not deposit liabilities or protected accounts under the Banking Act. Therefore, PERLS X are not guaranteed or insured by any Australian government, government agency or compensation scheme of Australia or any other jurisdiction.

4.2.2 Holders of PERLS X are subordinated and unsecured creditors

In a winding up of CBA, Holders' claims will rank after the claims of holders of Senior Ranking Obligations, creditors preferred by law and secured creditors.

Holders' claims will rank equally with claims of holders of Equal Ranking Securities. This means your PERLS X rank equivalently to a preference share.

Holders' claims will rank ahead of claims of holders of Junior Ranking Securities (being holders of Ordinary Shares).

4.2.4.1 Holders may receive Ordinary Shares on the Mandatory Exchange Date

Unless Redeemed or Exchanged earlier, PERLS X must be Exchanged on the Mandatory Exchange Date (subject to the Mandatory Exchange Conditions).

Normally, you will receive a variable number of Ordinary Shares with a value equal to A\$101.01 (based on the Initial Face Value of A\$100 and the VWAP of Ordinary Shares with the benefit of a 1% discount, see Section 2.3 "Mandatory Exchange"). For example, if the *VWAP of Ordinary Shares immediately prior to the Exchange Date* was A\$70, you would receive 1.4430 Ordinary Shares per PERLS X. If the Ordinary Share price on the Exchange Date remained A\$70, this would have a market value of A\$101.01.

However, CBA will only be required to Exchange PERLS X if all the Mandatory Exchange Conditions are satisfied (see Section 2.3 "Mandatory Exchange"). For example, if the *Issue Date VWAP* had been A\$77, then:

- under the First Mandatory Exchange Condition, if the VWAP of Ordinary Shares on the 25th Business Day before the Mandatory Exchange Date was greater than A\$43.12, the First Mandatory Exchange Condition would be satisfied;
- under the Second Mandatory Exchange Condition, if the VWAP of Ordinary Shares during the period of 20 Business Days before the Mandatory Exchange Date was greater than A\$38.89, then the Second Mandatory Exchange Condition would be satisfied; and

Conversion into equity

Example: Business models and balance sheets

- A small US firm (A) and a large Far East steel company (S) **plan** to establish a joint operation using an SPV.
- Situation A - Joint Venture:
 - A owns **1/2** of the SPV shares
 - S owns **1/2** of the SPV shares
- The SPV borrows \$700 from a large Far East bank.
- Who is responsible for paying the debt?

SPV			
Assets	820	Equity	120
		Debt	700

Large Far East Steel Company (S)			
Assets	50,000	Equity	25,030
Stake in SPV	60	Debt	25,030
	50,060		50,060

Small U.S.A. based Firm (A)			
Assets	100	Equity	100
Stake in SPV	60	Debt	80
	160		180

Large Far East Bank (B)			
Assets	99,300	Equity	5,000
Lent to SPV	700	Debt	95,000
	100,000		100,000



Example: Business models and balance sheets

- Situation B: Joint Venture, but unbalanced.
- Firm (A) and a large Far East steel company (S) now established a joint operation using an SPV, but:
 - A owns **2/3** of the SPV shares
 - S owns **1/3** of the SPV shares
- Firm A now should consolidate the SPV.
- Who is responsible for paying the debt?

SPV			
Assets	820	Equity	120
		Debt	700

Large Far East Steel Company (S)			
Assets	50,000	Equity	25,020
Stake in SPV	40	Debt	25,020
	50,040		50,040

Small U.S.A. based Firm (A)			
Assets	100	Equity	100
Stake in SPV	80	Debt	80
	180		180

Large Far East Bank (B)			
Assets	99,300	Equity	5,000
Lent to SPV	700	Debt	95,000
	100,000		100,000

Example: Business models and balance sheets

- Now, in a surprise move, S pays back the debt in full.
- But it now wants to recover 2/3s of the 700 from A.
- S forces Firm A into bankruptcy as it cannot possibly repay 2/3s of the 700 claim of S.
- Result: S acquires the SPV, and the assets of Firm A for next to nothing.

SPV			
Assets	820	Equity	820
		Debt	-

Large Far East Steel Company (S)			
Assets	49,300	Equity	25,020
Stake in SPV	740	Debt	25,020
	50,040		50,040

Small U.S.A. based Firm (A)			
Assets	100	Equity	100
Stake in SPV	80	Debt	80
	180		180

Large Far East Bank (B)			
Assets	99,300	Equity	5,000
Cash	700	Debt	95,000
	100,000		100,000



Example: Management accounting, incentives

- How did Uber solve a typical management control problem, and what does it tell us about the importance of accounting?
- But before I answer that question, let's talk about speaking up.

Example: Management accounting, incentives

- For decades, the Federal Aviation Administration has grounded pilots dealing with depression or other mental diagnoses, with policies so strict that the decision to seek psychiatric help or a prescription for standard antidepressant medication is enough to trigger a suspension of their flight eligibility. It is a system that has left many pilots, including Mr. Emerson, to struggle largely alone.
- “A lot of us aren’t as forthcoming as we otherwise would be,” Mr. Emerson said.
- From “Is This Hell? The Pilot Accused of Trying to Crash a Plane Tells His Story.”

Example: Management accounting, incentives

- We know that the best decisions are made with the best information available.
- But ...
- Sometimes the best information is located at specialist staff lower down in the hierarchy.
- If important, that information should reach the C-suite.

Example: Management accounting, incentives

- An important trade-off:
 - Suppose you work for a large organisation.
 - What if your manager is a bossy-boot, strongly focused on meeting targets?

Example: Management accounting, incentives

- An important trade-off:
 - Suppose you work for a large organisation.
 - What if your manager is a bossy-boot, strongly focused on meeting targets?

Example: Management accounting, incentives

- An important trade-off:
 - Suppose you work for a large organisation.
 - What if your manager is chill, not at all focused on meeting targets?

Example: Management accounting, incentives

- An important trade-off:
- Suppose you work for a large organisation.
- What if your manager is chill, not at all focused on meeting targets?

Example: Management accounting, incentives

- Recap:
 - Too much focus on control:
 - Poor decision making – employees don't speak up
 - Too little focus on control:
 - Anarchy

Example: Management accounting, incentives

- Accounting to the rescue
- How do companies solve these problems?
 - What was the problem with traditional taxis and tourists?
- How did Uber solve that problem?

Example: Management accounting, incentives

- Solving control problems in general
- The three legged stool:
 - Matching the right person with the right job
 - Measuring performance
 - Rewarding performance

Matching
the right
person with
the right job

Measuring
performance

Rewarding
performance

The 3-legged
stool

Example: Management accounting, incentives

- Solving control problems in general
- The three legged stool:
 - Matching the right person with the right job
 - Measuring performance
 - Rewarding performance
- Which of the legs did Uber adjust to control the typical taxi problem?

Matching
the right
person with
the right job

Measuring
performance

Rewarding
performance

The 3-legged
stool

Is there a future for accounting?

- Sustainability reporting
 - The International Sustainability Standards Board (ISSB) is an independent, private-sector body that develops and approves IFRS Sustainability Disclosure Standards (IFRS SDS).
 - The ISSB operates under the oversight of the IFRS Foundation. The ISSB was formed in 2021 following two consultations on the demand for global sustainability standards and what role the Foundation might play in the development of such standards and on proposed amendments to the IFRS Foundation Constitution that would enable the creation of a new sustainability standards board under the governance of the Foundation.

International Sustainability Standards Board

Follow



ABOUT

MEMBERS

MEETINGS

RESOURCES

NEWS

About the International Sustainability Standards Board

International investors with global investment portfolios are increasingly calling for high quality, transparent, reliable and comparable reporting by companies on climate and other environmental, social and governance (ESG) matters.

On 3 November 2021, the IFRS Foundation Trustees announced the creation of a new standard-setting board—the International Sustainability Standards Board (ISSB)—to help meet this demand.

The intention is for the ISSB to deliver a comprehensive global baseline of sustainability-related disclosure standards that provide investors and other capital market participants with information about companies' sustainability-related risks and opportunities to help them make informed decisions.

Related information

[Sustainability Reporting project](#)

[Contact us](#)

The importance of sustainability reporting

- See notredamebusiness:
- [YouTube](#)
- [Jacob Soll – YouTube](#)
- 1'46 – 8'46
- Cyclone Gabrielle
 - Impairments
 - Depreciation
 - Accountability of funds