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Speech Notes

"The Cooperative advantage of doing business"

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Thank you for the invitation to open this seminar and for the opportunity to welcome to New Zealand all of the representatives of cooperatives from the Asia Pacific region who are here today.

We all know of the history of the co-operative movement and its great traditions of self-help, self-responsibility, democracy, equality, equity, and solidarity. Modern co-operatives have built on those traditions, and have become a major feature of many economies. For New Zealand, co-operatives are an integral part of our economic landscape, however in order to meet today's challenges co-operatives need to be able to expand internationally and to further develop their ability to export. This often requires an increase in the ability of co-operatives to access capital, which needs to be balanced against maintaining their special ownership structure and characteristics. In this regard the recent announcement of New Zealand's largest co-operative (indeed our largest company), Fonterra is illustrative of that reality and I will address that.

I would like to focus my comments today on three main issues. I'll begin by outlining to you the government's efforts to promote an economic transformation agenda while providing leadership on sustainability and the contribution the co-operative sector can make in this regard. I'll then address the range of co-operative and mutual structures available in New Zealand; and finally the application of International Financial Reporting Standards to co-operatives.

However, before moving on to these topics I think it is useful to remind ourselves of the size and diversity of the co-operative sector both internationally and in New Zealand. Internationally, the Global 300 listing confirms that the largest 300 co-operatives and mutuals worldwide contribute nearly 1 trillion US Dollars in revenues to the global economy each year, and operate in areas as diverse as agriculture, retailing, banking and insurance.

In New Zealand, co-operatives and co-operative businesses operate in many sectors of the economy, most notably agriculture, but also in areas such as financial services, retailing, and electricity lines businesses. I understand that the total turnover of members of the New Zealand Co-operatives Association in 2006 was in the order of \$27 billion. Even excluding Fonterra this figure is still close to \$14 billion.

The significant contribution the co-operative sector makes to the New Zealand economy is clear from these figures.

However, New Zealand co-operatives are much more than their economic status. Co-operatives have made a unique contribution to our identity as a nation – there would be few towns in New Zealand that do not have a lodge built by the local friendly society that was once the centre of community life.

It is not surprising either that we see co-operatives in our agricultural sector – we are a long way from our markets and our companies have to make up for the lack of scale and scope of their international competitors by being the best that they can be.

The scale and diversity of the New Zealand co-operative sector also gives it a key role in the government's economic transformation agenda, which is the first issue that I would like to talk to you about today. Announced last year, the agenda is designed to facilitate the development of a high-income, knowledge-based economy. Economic transformation is underpinned by a number of objectives, including:

- growing globally competitive firms
- developing innovative and productive workplaces; and
- ensuring environmental sustainability.

The co-operative sector is ideally placed to be at the forefront of achieving these objectives. The co-operative business structure has proven its competitiveness internationally in a number of areas; the culture of co-operatives can facilitate innovation and productivity in the workplace as members look for ways of working together effectively, efficiently and democratically for their mutual benefit; and co-operative businesses are renowned for their commitment to social and environmental goals.

As our Prime Minister, the Rt Hon Helen Clark, said: "Sustainability is an issue whose time has come." This is a concept which is not new to the cooperative sector, underpinning as it does your business philosophy. Sustainability is based on ethical practices and strong values that guide the business' culture; in other words sustainability has always been at the core of your being as a co-operative movement.

Co-operatives are based on sustainability where members work together using the democratic model; co-operatives engender economic sustainability through keeping jobs, profits and resources within their collective and the wider community; and co-operatives can promote environmental sustainability by helping members adopt more responsible patterns of consumption, or by supporting practices that value our environmental resources.

Of course, for the co-operative sector to continue to develop and grow in New Zealand it is vital that co-operative and mutual organisations have appropriate legal structures available to them. In New Zealand, the approach we have taken to different legal forms available to co-operative businesses and other mutuals is relatively neutral, in that there are relatively few policy preferences favouring co-operatives over other organisational forms.

This is in recognition of the fact that organisations should be encouraged to choose the legal form that is appropriate for their specific circumstances.

As commentators have noted, co-operatives often develop in particular circumstances where there are multiple small competing producers of a particular product facing market power due to industry concentration further down the supply chain. A strong common interest also helps in the development of co-operative organisations.

In saying that, there is no hard and fast rule about when particular legal forms are appropriate. In New Zealand, the co-operative sector is particularly adaptable and flexible and I believe this is helped by the diverse range of legal forms that are available to them.

Foremost amongst these legal forms are co-operative companies, which have long been a feature of New Zealand's corporate landscape. The law regarding co-operative companies was reformed in 1996. There are a number of other legal forms available for use by co-operatives and co-operative businesses. These include industrial and provident societies, incorporated societies, and companies. My officials are currently working on proposals to apply uniform minimum governance standards to these other mutual legal forms, as well as credit unions and friendly societies. The objective of this work is to simplify the law and provide improved accountability to members and clarity to third parties as to the basic governance requirements that apply to these entities.

As I mentioned before, Fonterra is in the news at present asking its members to vote on a new capital structure that would involve forming a new company and listing on the stock exchange. The New Zealand dairy farmers who are the co-operative members, would retain control, and protection measures would be enshrined in legislation to prevent a takeover occurring and to maintain majority New Zealand ownership. The move is aimed at generating enough capital for the business to become a truly competitive multinational that invests globally for growth.

This is an interesting example of the flexibility of the co-operative arrangement allowing businesses to combine into innovative new structures that meet the needs of shareholders in a rapidly changing and challenging global economy.

The final issue I would like to address today is the application of International Financial Reporting Standards to co-operatives. As you know, the Accounting Standards Review Board (ASRB) decided that IFRS should apply to accounting periods commencing on or after 1 January 2007.

I am aware of the concerns raised about the application of IFRS to co-operatives. In New Zealand our Co-operative Companies Act provides for owner-patrons to redeem their co-operative capital in certain circumstances, and I know that specific concerns have been raised that IFRS requires that this redeemable share capital be classified as debt rather than equity, with potential consequences for the solvency of co-operatives.

Making financial reporting standards is a highly specialised activity, as you know. For this reason, the job of setting financial reporting standards in New Zealand has been given to an independent body, the Accounting Standards Review Board (ASRB). The government is also a major user of financial reporting standards, and for that reason does not intervene in the process of setting those standards.

The government does, however, recognise the concerns of the co-operative sector about the application of IFRS. It is for this reason that the Financial Reporting Act was amended last year.

Following these changes, the Act now provides the ASRB with the power to exempt classes of reporting entities from any provision of an applicable financial reporting standard. Such an exemption can only be granted if compliance with the standard results in financial statements that are materially misleading or likely to mislead.

This exemption-making power is expected to come into force before the middle of 2008. It aims to provide the flexibility for addressing concerns around the application of IFRS and I understand that the New Zealand Co-Operatives Association is now looking to make application under this provision.

I should make the point that IFRS also permits entities whose share capital is not defined as equity under IFRS to adapt the presentation of their financial statements. Specifically, IFRS provides the opportunity for cooperative companies to include information on total members' interest in their financial statements. To quote Paragraph 6 of NZ IAS 1:

“Similarly entities that do not have equity as defined in NZ IAS 32 Financial Instruments: Disclosure and Presentation (eg some mutual funds) and entities whose share capital is not equity (eg some co-operative entities) may need to adapt the presentation of the financial statements of members' or unit holders' interests.”

Thus, co-operative companies are able to prepare a separate table that aggregates members' interests from the equity and debt sections of the balance sheet. This should address the concerns that have been expressed about the application of the solvency test.

I would like to conclude today by emphasising again the importance of the co-operative sector and the key part it can play in the government's economic transformation agenda. Co-operative businesses have shown themselves over the years to be flexible and competitive both in New Zealand and overseas.

Co-operatives form some of the most innovative and dynamic businesses in the New Zealand economy, and the government remains committed to providing an environment that supports their growth. Thank you for the opportunity to talk to you this morning. I am sure that the seminar will be a great success. I am pleased again to welcome you all to Wellington and to officially declare your seminar open.