LGFA New Zealand Local Government Funding Agency

ANNUAL REPORT 2012-2013

New Zealand Local Government Funding Agency Limited

Annual Report
2012 – 2013

New Zealand Local Government Funding Agency Limited

Annual Report
2012 – 2013

Contents

Governance structure

Shareholders, governance and management structure for the LGFA as at 30 June 2013.

LGFA Shareholders

Auckland Council	Otorohanga District Council
Bay of Plenty Regional Council	Palmerston North City Council
Christchurch City Council	Selwyn District Council
Gisborne District Council	South Taranaki District Council
Greater Wellington Regional Council	Tasman District Council
Hamilton City Council	Taupo District Council
Hastings District Council	Tauranga City Council
Hauraki District Council	Thames-Coromandel District Council
Horowhenua District Council	Waimakariri District Council
Hutt City Council	Waipa District Council
Kapiti Coast District Council	Wanganui District Council
Manawatu District Council	Wellington City Council
Marlborough District Council	Western Bay of Plenty District Council
Masterton District Council	Whakatane District Council
New Plymouth District Council	Whangarei District Council
	New Zealand Government

LGFA Shareholders Council

Brian Trott. Bay of Plenty Regional Council. Chairman
Alan Adcock. Whangarei District Council
Mohan De Mel. Tauranga City Council
Warwick Hayes. Wellington City Council
Douglas Marshall. Selwyn District Council
Matt Potton. Western Bay of Plenty District Council
Mike Timmer. Greater Wellington Regional Council
Damian Zelas. New Zealand Government
(2 vacancies)

LGFA Board

Craig Stobo. Independent Chairman
Paul Anderson. (Formerly Christchurch City Council)
John Avery. Independent
Mark Butcher. Auckland Council
Philip Cory-Wright. Independent
Abigail Foote. Independent

LGFA Executive

Philip Combes. Chief Executive Officer
Neil Bain. Chief Financial Officer

Directors' report

"We are delighted that the success of our first bond tender was recognised at the 2013 INFINZ Annual Awards where it was judged as the best debt issue of the 2012 calendar year."

Craig Stobo, Chairman LGFA Board

The 2012/13 year saw the Local Government Funding Agency (LGFA) continue to build on the solid base established in the first half of last year following the commencement of market operations in February 2012. In particular, we are pleased to highlight three key achievements during the 2012/13 year that will establish a platform for LGFA's continued strong growth in future years:

1. **We have more than doubled the lending forecast in the original business case**

   By 30 June 2013, LGFA had lent $2.48 billion to 37 participating councils. This outcome is more than double the lending volume forecast in the original business case for LGFA.

2. **We have halved our base margin charged to councils in just eighteen months of operation**

   From the inaugural bond tender in February 2012, LGFA charged a base margin to borrowers of 30 basis points (bps). During 2012/13, this margin was cut twice; to 25 bps in February 2013 and to 20 bps in June 2013. With a further cut to 15 bps in September 2013, we have now halved our base margin in little over eighteen months since first commencing lending services to councils.

3. **Our first dividend is double the original business case forecast**

   A $1.515 million dividend has been declared by the LGFA Board for the year ended 30 June 2013. This dividend is double the original business case forecast of $0.757 million for the 2012/13 year.

Continued strong support from local authorities over the year has contributed greatly to our success. On 30 November 2012, 12 new council shareholders joined the original 18 local authorities who were foundation members of LGFA. This brings the total number of shareholders in LGFA to 31, comprising 30 participating councils and the New Zealand Government.

In addition, a further nine councils joined LGFA between February 2013 and April 2013, either as borrowers and guarantors, or as borrowers only.

In all, 39 local authorities are eligible borrowers of LGFA (as at 30 June 2013), which is estimated to represent over 90% of local government sector debt.

In the relatively short period we have been operating, LGFA has provided significant savings in interest cost to our member councils. As at 30 June 2013, we estimate that LGFA was saving AA rated councils approximately:

- 20 to 30 bps in annual interest costs on a December 2017 maturity, and
- 30 bps in annual interest costs on a March 2019 maturity.[1]

We estimate that savings for A rated and unrated councils would be somewhat higher (by around 5 to 10 bps).

During 2012/13, nine bond tenders were undertaken, raising $1.64 billion across four maturities. As at 30 June 2013, the level of LGFA's bonds on issue amounted to $2.48 billion, with almost $1 billion outstanding in our largest maturity (March 2019).

In our first full year of operation, LGFA recorded a net operating profit of $2.6 million. This compares very favourably with the Statement of Intent forecast for profit in 2012/13 ($0.7 million).

The success of LGFA's inaugural tender on 15 February 2012 was noted in last year's Annual Report. We are delighted that the success of our first bond tender was recognised at the 2013 INFINZ Annual Awards where it was judged as the best debt issue of the 2012 calendar year. This award followed on from earlier success in the year where LGFA also won New Zealand Domestic Issuer of the Year at the KangaNews Awards 2012.

Fitch Ratings (on 30 November 2012) and Standard & Poor's (on 20 December 2012) have both recognised our strong credit fundamentals by affirming LGFA's local currency rating at AA+ and foreign currency rating at AA, both with stable outlooks. These credit ratings are the same as the New Zealand sovereign ratings.

We appreciate the Crown's continuing involvement as the largest single shareholder in LGFA and as provider of operational support and a significant liquidity facility through the New Zealand Debt Management Office (NZDMO).

Finally, the Directors wish to express their appreciation to the staff, who made a significant contribution to LGFA's key achievements in 2012/13.

1 Refer 1.1 of the statement of service performance (page 9)

Our people

The LGFA management team

From left: Neil Bain, Philip Combes (Chief Executive), Andrew Michl, Sonny Southon

The LGFA Board of Directors

From left: John Avery, Philip Cory-Wright, Abby Foote, Craig Stobo (Chairman), Paul Anderson, Mark Butcher

New Zealand Local Government Funding Agency Limited

Statement of service performance

Statement of service performance

PERFORMANCE AGAINST OBJECTIVES AND PERFORMANCE TARGETS

1 Primary objective

LGFA operates with the **primary objective** of optimising the debt funding terms and conditions for participating local authorities. Among other things this includes:

1.1 **Providing debt to participating local authorities at the lowest possible interest rates commensurate with the relevant maturity**

LGFA measures the pricing performance of bond tenders against two key benchmarks:

1. LGFA aims to reduce its margin over New Zealand Government bonds (NZGBs) in accordance with its Statement of Intent (SOI) performance target.
2. LGFA also aims to minimise its margin over swap rates to provide cost effective funding to councils.

LGFA has met its primary objective by continuing to achieve significant improvement in the pricing of our benchmark 15 December 2017 and 15 March 2019 bonds. These bonds are regarded as our benchmark bonds because they have the largest volumes outstanding, the most liquidity and greatest frequency of issuance.

Over the course of the year to 30 June 2013, there were improvements of:

- 17 bps and 28 bps respectively in the margin to NZGBs of our December 2017 and March 2019 bonds.
- 24 bps and 32 bps respectively in the margin to swap of our December 2017 and March 2019 bonds

This secondary market pricing improvement is summarised in the following tables:[2]

Margins – 15 December 2017	30 Jun 2012 (bps)	30 Jun 2013 (bps)	Pricing improvement
LGFA margin to NZ Government Bonds	90	73	17
NZGB margin to swap	(33)	(40)	7
LGFA margin to swap	57	33	24

Margins – 15 March 2019	30 Jun 2012 (bps)	30 Jun 2013 (bps)	Pricing improvement
LGFA margin to NZ Government Bonds	105	77	28
NZGB margin to swap	(33)	(37)	4
LGFA margin to swap	72	40	32

1.2 **Making longer-term borrowings available to participating local authorities**

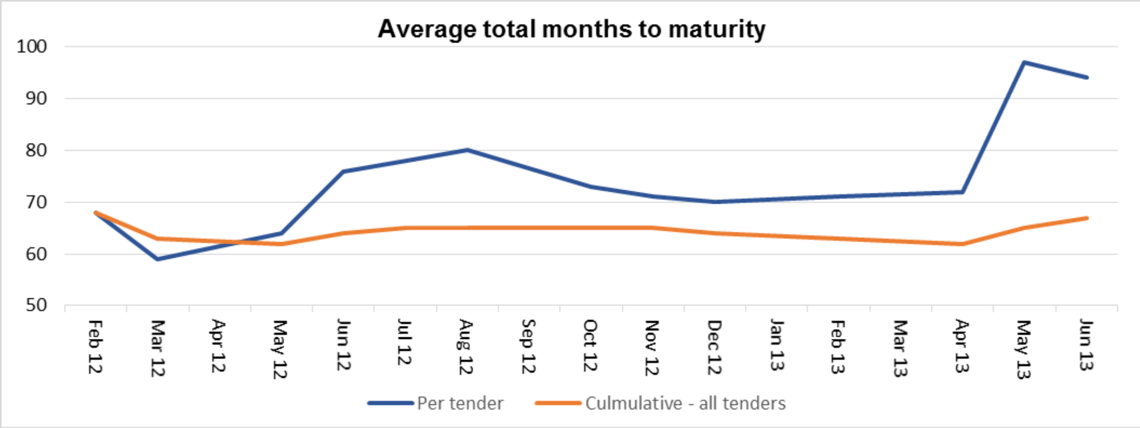
Over the course of the year, LGFA continued to offer two maturities of five years and longer to participating councils:

- 15 March 2019 bond (just under six years), first issued at the fourth bond tender held on 6 June 2012, and
- 15 May 2021 bond (eight years), first issued at the twelfth bond tender held on 15 May 2013.

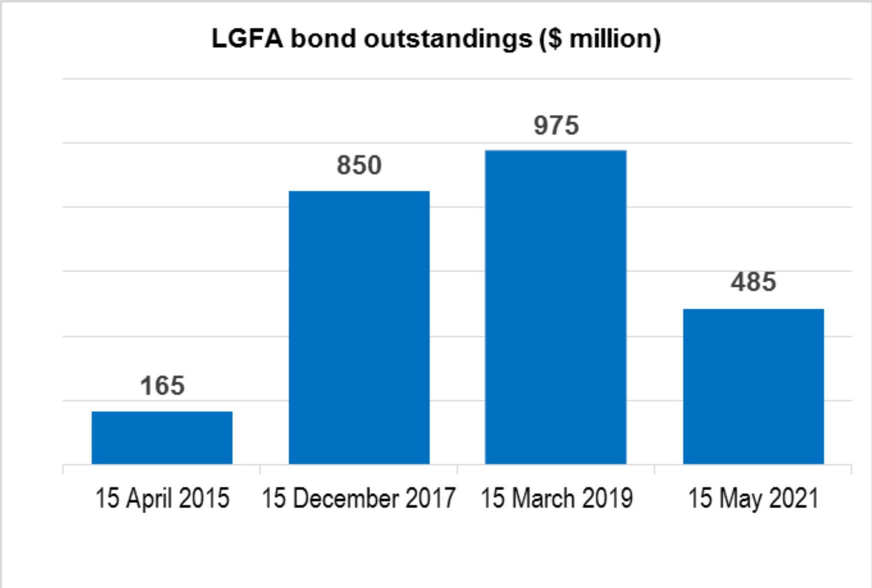
2 Source: PricewaterhouseCoopers

Statement of service performance

The following graph shows the average months to maturity for bonds issued at tender, and the aggregate average months to maturity for all bonds outstanding at each tender:



The following graph shows the total LGFA bond outstandings by maturity as at 30 June 2013:

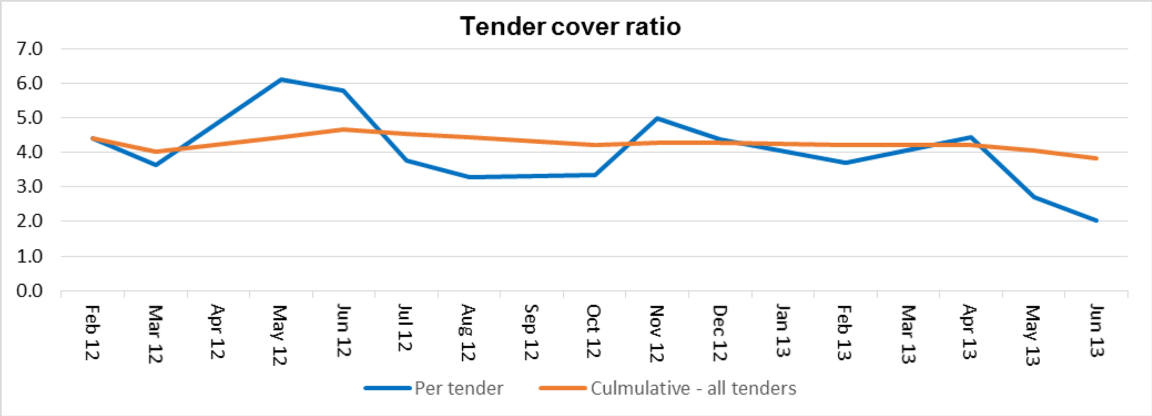


Statement of service performance

1.3 **Enhancing the certainty of access to debt markets for participating local authorities, subject always to operating in accordance with sound business practice**

Access to debt markets has been demonstrated by the cover ratios (ie. ratio of total amount bid to total amount offered) achieved over the 13 LGFA bond tenders to June 2013.

Over those 13 tenders, a total of $9,504 million has been bid for a total bond issuance of $2,475 million, an average cover ratio of 3.8 times. The LGFA cover ratio for each tender and the cumulative ratio for all tenders to 30 June 2013 is shown in the following chart:



The introduction of our new May 2021 bond at the last two tenders has coincided with the two lowest cover ratios recorded. This reduction in coverage ratio is likely to have been driven by the following two factors:

1. The introduction of an 8-year maturity is longer than preferred by many New Zealand bank investors.
2. Market uncertainty following the sharply rising interest rate environment since May 2013 will see many investors switching to shorter maturities to reduce capital losses in their bond portfolios. This increase in investor preference for shorter maturities is at tension with many councils' preference for longer dated funding.

2 Additional objectives

LGFA has a number of additional objectives which complement the primary objective. These additional objectives are to:

2.1 **Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy set out in section 6 of the Statement of Intent**

As at 30 June 2013, bond issuance ($2,475 million) and on-lending activity ($2,481 million) were approximately double the volume anticipated in the original business case for LGFA. As a consequence of this increased volume, LGFA's net profit for the year to 30 June 2013 was $2.6 million, exceeding the budget net profit of $0.7 million.

Following the strong financial result, a dividend of $1.515 million has been declared by the LGFA Board for the year to 30 June 2013.[3] This dividend represents a return of 6.06% for the year and is a significant improvement over the original business case which forecast a dividend of $0.757 million for the year to 30 June 2013.

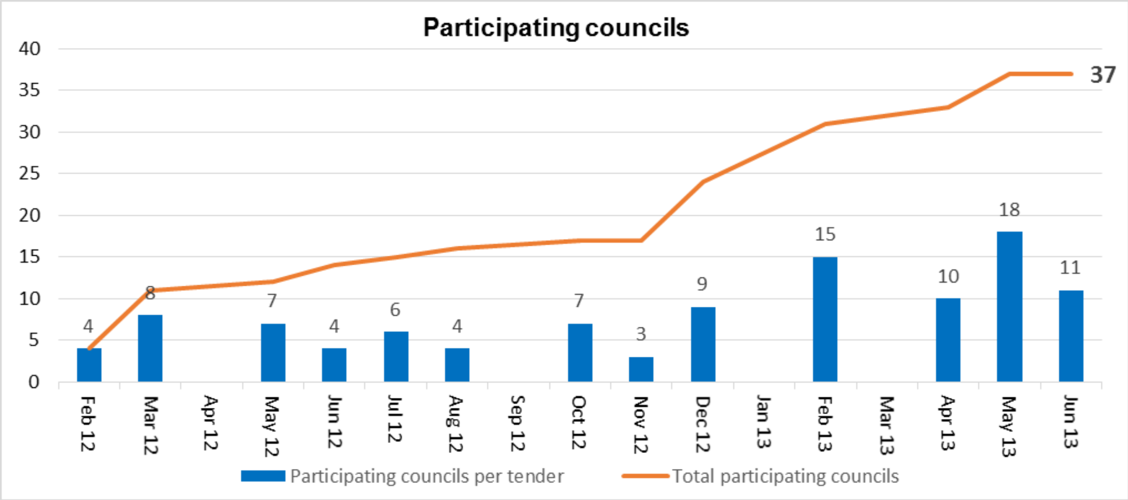
[3] The LGFA Foundation Policies state that the policy is to pay a dividend that provides an annual rate of return to Shareholders equal to the Company's cost of funds plus 2 % over the medium term, recognising that, to assist in the start-up period, the initial expectation is for no dividend for the part period to 30 June 2012, and for a dividend equal to 50% of the target dividend in the two periods to 30 June 2014.

Statement of service performance

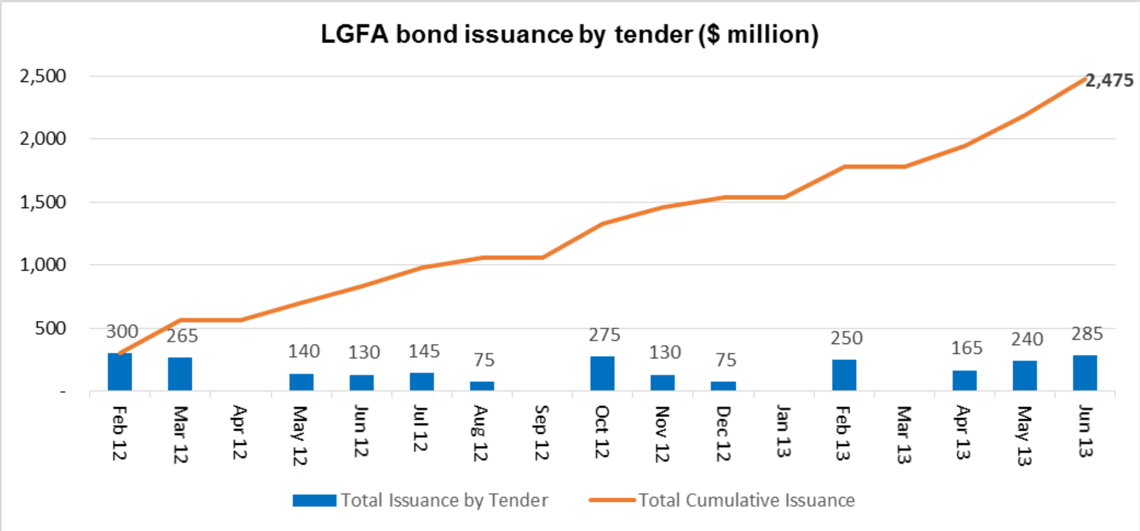
2.2 Become the primary source of debt funding for participating local authorities

Councils have strongly supported LGFA. To date, 17 (out of 18) inaugural participating councils have borrowed from us. By 30 June 2013, another 21 councils had joined LGFA (12 as shareholders at the Second Opening on 30 November 2012, and 9 as borrowers in two 'intakes' on 18 February and 5 April 2013). After the 19 June tender, 20 of these 21 new members had borrowed from LGFA. In all, 37 out of 39 participating councils had borrowed from LGFA by 30 June 2013.

The strong council support for LGFA is demonstrated in the following graph which shows the progression of council participation from LGFA's commencement of issuance in February 2012:



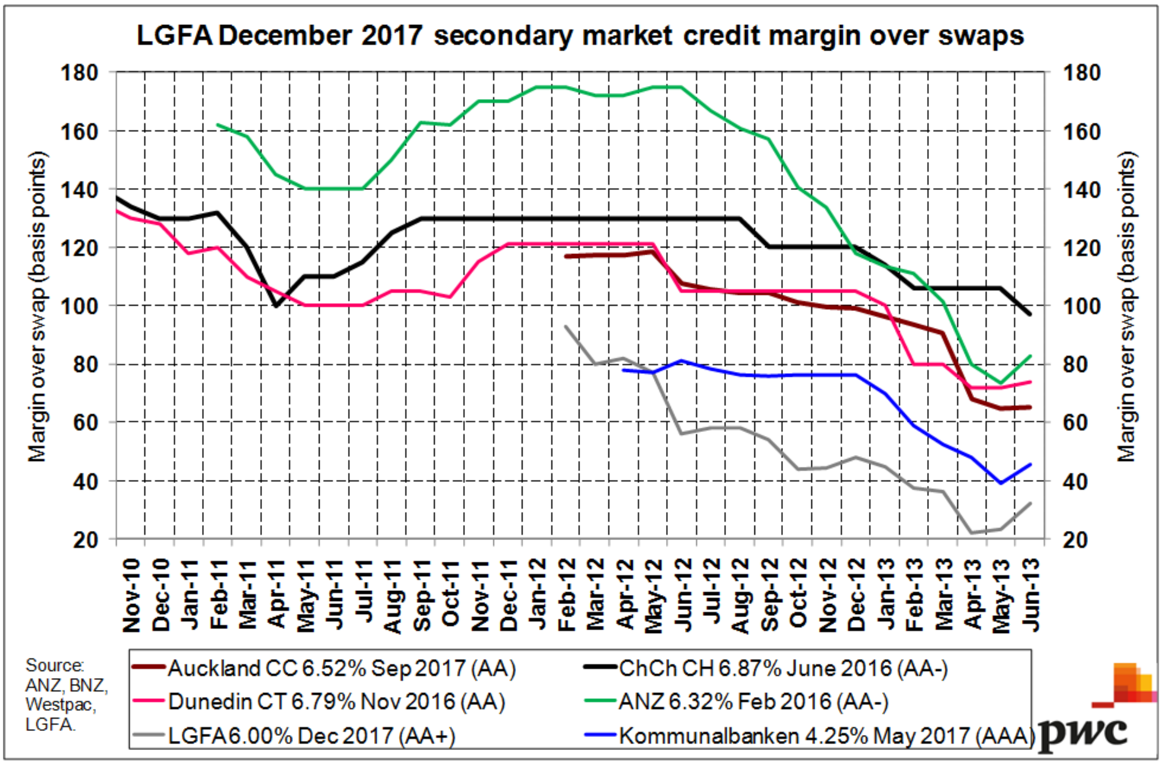
The following graph shows the aggregate level of LGFA bond issuance by tender:



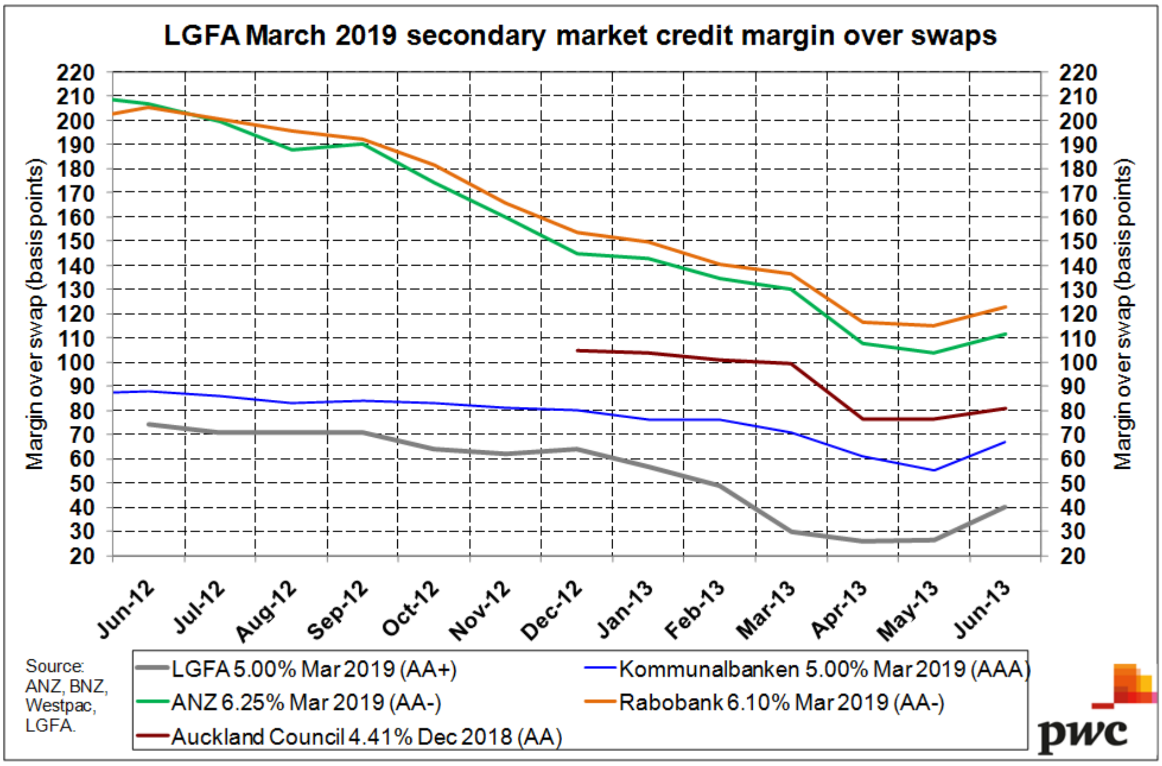
Statement of service performance

2.3 Operate in a manner to ensure LGFA is successful and sustainable in the long-term

The key to LGFA's long-term sustainability is to ensure that it can always fund councils at lower rates and for longer maturities than they can fund from other means. The following two graphs demonstrate LGFA's performance against this objective. These charts compare LGFA's spread to swap against a number of other issuers for our December 2017 and March 2019 maturities:



Source: PricewaterhouseCoopers



Source: PricewaterhouseCoopers

Statement of service performance

From the previous charts, we estimate that, as at 30 June 2013, LGFA was saving AA rated councils approximately:

- 20 to 30 bps in annual interest costs on a December 2017 maturity, and
- 30 bps in annual interest costs on a March 2019 maturity.

The basis for these estimates is set out in the table below:

Margins as at 30 June 2013	December 2017 maturity (bps)	March 2019 maturity (bps)
AA rated councils margin to swap*	63 to 73	80
Less: LGFA margin to swap	(33)	(40)
LGFA Funding Advantage	30 to 40	40
Less*:* LGFA Base Margin	(20)	(20)
LGFA Net Funding Advantage	10 to 20	20
Add: 'LGFA Effect' **	10	10
Total saving for AA rated councils	**20 to 30**	**30**

* *For the 2017 bond, the benchmark councils are Auckland (63 bps) and Dunedin (73 bps). For the 2019 bond, the benchmark is Auckland. Dunedin does not have a 2019 bond on issue.*

** *The 'LGFA effect' represents the estimated conservative reduction in AA rated councils margin to swap as a result of LGFA operations. From May to June 2012, the margin to swap for AA rated councils fell by 10 bps, with no corresponding move in swap spreads for other borrowers. This suggests that potential access to cost-effective LGFA funding has enabled these councils to reduce their borrowing margin by around 10 bps.*

2.4 **Educate and inform all local authorities (both participating and non-participating) on matters within the scope of LGFA's operations**

During the year to 30 June 2013, LGFA:

- Organised a New Borrowers Forum held in Wellington on 31 July 2012, attended by 18 councils (and their advisers) to learn about the process involved in becoming a new borrower from LGFA.
- Participated in the Fiscal Thresholds Working Party convened by Local Government New Zealand in November 2012, as part of the Better Local Government reform programme.
- Wrote to non-participating councils seeking firm commitments from those wishing to join LGFA as a shareholder in the Second Opening held on 30 November 2012.
- Visited Queenstown Lakes District Council, Invercargill City Council and Dunedin City Council in March 2013. As a result of discussions with these councils, we are investigating ways of simplifying and streamlining the process for joining LGFA.
- Participated in the annual Local Authority Workshop arranged by Bancorp. This event was held in Auckland in May 2013, and enabled LGFA to discuss its performance with a wide range of councils (both members and non-members of LGFA).
- Introduced an update to all participating councils on the results of the LGFA bond tenders. This initiative is designed to provide timely information to our borrowers to assist them in formulating their debt management strategies.
- Held regular discussions with PricewaterhouseCoopers and Bancorp (as key advisers to the local government sector) on various matters of interest to their council clients.
- Provided support to the work of the Local Government Infrastructure Expert Advisory Group (where one of our Directors was a member of the Advisory Group).

Statement of service performance

- Issued press releases to inform all local authorities that:
    - LGFA won New Zealand Domestic Issuer of the Year at the KangaNews Awards 2012.
    - 12 new shareholders had joined LGFA (with eight of them borrowing at the December bond tender).
    - LGFA had responded to media reports that Kaipara District Council had joined LGFA by publicly clarifying the terms and conditions of membership, and the responsibility that LGFA has to lend to participating councils on a prudent basis.

2.5 **Become a leading participant in the New Zealand capital markets**

Market commentary from industry publications demonstrates interest in LGFA's activities from both the domestic market and our international peer organisations.

- LGFA won 'Debt Issue of the Year' at the INFINZ Annual Awards held in Auckland on 8 May 2013 (attended by over 770 market participants). Our inaugural $300 million bond tender held on 15 February 2012 was judged as the best debt issue of the 2012 year.
- LGFA was presented with the award of New Zealand Domestic Issuer of the Year at the KangaNews Awards 2012 in Sydney on 18 March 2013.
- KangaNews coverage of LGFA over the year included:
    - A roundtable discussion between corporate and local government issuers, and investors, in its September 2012 edition.
    - A feature article on LGFA's performance during its first six months of operation, also in the September 2012 edition.
    - A New Zealand update featuring NZDMO and LGFA was published in the December 2012 Supplement edition.
    - An article on the winners of the KangaNews Awards 2012, featuring LGFA as the New Zealand Domestic Issuer of the Year was published in the December 2012/January 2013 edition.

Over the course of the year, LGFA undertook regular meetings with investors and intermediaries to promote support for LGFA bonds, including:

- The Chairman and Chief Executive of LGFA undertook a significant European investor marketing mission in June to the UK, Switzerland and Germany where they met with a number of private banks and institutional investors in these countries.
- Met with one of Asia's largest central banks in Sydney in May (at their request) to update them on LGFA's performance in its first 18 months of operation.
- Presented the LGFA story at Deutsche Bank's Investor Mission in Wellington during March (which brings a significant number of offshore investors to New Zealand every year).
- Participated as a speaker in October 2012 in a New Zealand presentation series with New Zealand Debt Management Office (NZDMO) and the Reserve Bank of New Zealand at the fifth Annual Australasian Fixed Income Conference in Sydney, organised by the Commonwealth Bank of Australia. This provided an opportunity to highlight LGFA's performance in 2012 to a group of approximately 50 investors from Australia, New Zealand, Asia, Europe and the United States.
- Participated in an Investor Roundtable discussion in August 2012 organised by KangaNews and the Bank of New Zealand.

Statement of service performance

2.6 **Provide excellent service to participating local authorities**

Over the course of the year to 30 June 2013, LGFA provided 105 new loans to councils totalling $1,662 million.

Of the 105 loans, 21 were fixed rate, which represented 20% of the loans provided. We were also able to provide bespoke rate reset dates when requested to match some councils existing swap reset dates.

2.7 **Ensure excellent communication exists and be professional in its dealings with all its stakeholders**

During the year to 30 June 2013, LGFA:

- Met with the Chairman of the Shareholders' Council, the Shareholders' Council Monitoring Group, as well as the full Shareholders' Council on several occasions throughout the year to discuss the draft SOI 2013/14 and other relevant issues. These meetings proved to be constructive and focused on ways for LGFA to continuously improve its reporting to shareholders, particularly on the more technical aspects of our business.
- Participated in a Local Government Funding Agency Roundtable in London on 25 June 2013. The meeting was organised by ANZ and KangaNews and enabled two established agencies (Kommuninvest from Sweden and LGFA from New Zealand) to share experiences and ideas with representatives from the UK and France (who are looking to set up similar entities).
- Arranged meetings with senior staff from the Office of the Auditor-General (OAG) to discuss several matters of interest to OAG in their role as auditors of the local government sector.
- Conducted regular media interviews (eg. interest.co.nz, Bloomberg News) and contributed to KangaNews articles to ensure that markets (both domestically and internationally) are well informed about LGFA's activities and operations.
- Held our inaugural Annual General Meeting on 13 November 2012. At the meeting, shareholders approved an amendment to the Shareholders' Agreement to reduce the utilisation commitment period for new shareholders (joining at the Second Opening) to approximately two years (from three years). Useful feedback on LGFA's dividend and margin policies was also received from shareholders.
- Successfully completed the Second Opening on 30 November 2012. At the end of this process, $1.3 million of LGFA shares were transferred from twelve existing 'sell-down' shareholders to twelve new shareholders, with all transactions settled smoothly.
- Developed processes, in conjunction with councils, for the admission of new shareholders, borrowers and guarantors into LGFA.
- Maintained regular communication with intermediaries and investors to review and revise its debt issuance strategies.

2.8 **Ensure its products and services are delivered in a cost-effective manner**

During the period to 30 June 2013, LGFA:

- Charged a base margin to councils that averaged 26 bps throughout the year. At 30 June 2013, the base margin charged had reduced to 20 bps being half of the permitted 40 bps.[4]
- Restricted annual operating costs to $3.0 million for 2012/13; below the SOI target of $3.2 million.

---

4 30 bps: July 2012. Reduced to 25 bps February 2013. Further reduced to 20 bps June 2013. Subsequent to 30 June 2013 the margin was reduced further in September 2013 to 15 bps.

Statement of service performance

2.9 **Consult with Shareholders regarding the potential requirement for LGFA Borrowers to obtain comprehensive insurance cover**

Following settlement of the thirteenth bond tender on 19 June 2013, LGFA had on-lent $2,481 million to councils. To date, there has been no requirement for borrowers to obtain or retain comprehensive insurance cover.

LGFA's current credit assessment approach is to consider insurance cover along with various business interruption risks (including risks to physical assets) as part of an overall credit risk assessment of individual councils. In this regard, LGFA is aware that self-insurance arrangements (eg. via the accumulation of financial assets) may be as effective as external insurance cover.

If this becomes an issue, LGFA will undertake future consultation with shareholders on the appropriate level of insurance cover for borrowers.

2.10 **Review the appropriateness of LGFA's 'broker' business model**

The success of the 'broker' business model is evident from three key factors:

- Overall profitability (ie. the retained earnings position) has significantly exceeded budget in the first 18 months of operations.
- Profitability has been achieved without the need for LGFA to take on significant interest rate risk (eg. Value-at-Risk[5] is currently running at only 30% of policy limits).
- Significant improvement in the pricing of LGFA bonds has generated corresponding savings for AA rated council borrowers estimated to be around 20 bps in annual interest costs on a December 2017 maturity, and around 30 bps on a March 2019 maturity.

2.11 **Maintain LGFA's credit rating equal to the New Zealand Government sovereign rating where both entities are rated by the same Rating Agency**

On 30 November 2012, Fitch affirmed LGFA's local currency credit rating at AA+ and foreign currency credit rating at AA. The outlook on both ratings is stable.

On 20 December 2012, Standard & Poor's affirmed LGFA's local currency credit rating at AA+ and foreign currency credit rating at AA. The outlook on both ratings is stable.

LGFA's credit ratings from both Fitch and Standard & Poor's are the same as the New Zealand sovereign ratings.

2.12 **Achieve the Financial Forecasts set out in section 4 of the Statement of Intent**

LGFA's financial results for key items set out in section 4 of the SOI for the year to 30 June 2013 are:

In $ million	30 Jun 2013 Actual	SOI Forecast
Total Net Income (net of borrower notes)	6.5	3.9
Overheads	(3.0)	(2.7)
Borrower Notes Interest	(0.9)	(0.5)
Net Profit	**2.6**	**0.7**

2.13 **Achieve the Dividend Policy set out in section 6 of the SOI**

Refer to comments in 2.1

[5] Value-at-Risk (VaR) is a statistical market risk management tool which seeks to determine the largest dollar loss likely to be suffered by LGFA over a 1 day period with a 95% confidence level.

Statement of service performance

3 Performance Targets

Six performance targets are specified for LGFA in the SOI. Progress against each of these targets is discussed below, including an explanation of any material variances.

Current performance targets		Target	Result	Outcome
1	Average cost of funds relative to NZGS	<0.50%	0.84%	No
2	Average base on-lending margin above LGFA's cost of funds	<0.40%	0.26%	Yes
3	Annualised operating overheads	<$3.2 million	$3.0 million	Yes
4	Lending to participating councils	>$900 million	$2,481 million	Yes
5	Number of shareholder councils	≥30	30	Yes
6	Number of eligible borrowers	≥40	39	No

(i) Average cost of funds

LGFA's relative cost of funds was trending towards the target level of 50 bps until the June quarter 2013.

	Sep quarter 2012	Dec quarter 2012	Mar quarter 2013	Jun quarter 2013
Average cost of funds relative to NZGS	0.98%	0.84%	0.76%	0.84%

There are two key reasons for LGFA's relative cost of funds rising in the June quarter 2013:

- We introduced a new May 2021 bond at our 15 May 2013 tender. Longer dated bonds price at a relatively higher margin above NZGS than shorter dated bonds, as the following table shows.

LGFA margins to NZGS as at 30 June 2013

Maturity	Margin (bps)
Apr 2015	45
Dec 2017	73
Mar 2019	77
May 2021	80

- Market uncertainty following a sharp rise in global bond yields during June 2013 (created by comments from US monetary authorities on their potential exit path from quantitative easing) adversely affected LGFA's margins at the 19 June 2013 bond tender.

(ii) Number of eligible borrowers

Although only 39 councils had joined LGFA as at 30 June 2013, three councils had also been approved as borrowers by the LGFA Board, but had not completed the necessary legal documentation to become members of LGFA by financial year-end. When this is completed, there will be a total of 42 eligible borrowers signed up with LGFA.

New Zealand Local Government Funding Agency Limited

Financial statements

Contents

Directors' declaration

In the opinion of the directors of the New Zealand Local Government Funding Agency Limited, the financial statements and notes on pages 23 to 42:

- comply with New Zealand generally accepted accounting practice and give a true and fair view of the financial position of the Company as at 30 June 2013, and
- have been prepared using appropriate accounting policies, which have been consistently applied and supported by reasonable judgements and estimates.

The directors believe that proper accounting records have been kept which enables, with reasonable accuracy, the determination of the financial position of the Company and facilitates the compliance of the financial statements with the Financial Reporting Act 1993.

The directors consider that they have taken adequate steps to safeguard the assets of the Company, and to prevent and detect fraud and other irregularities. Internal control procedures are also considered to be sufficient to provide a reasonable assurance as to the integrity and reliability of the financial statements.

For and on behalf of the Board of Directors:

C. Stobo	A. Foote
Director	Director
27 September 2013	27 September 2013

NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY LIMITED

Statement of comprehensive income

For the year ended 30 June 2013
in $000s

	Note	12 months ended **2013**	7 months ended 2012
Interest income from			
Cash and cash equivalents		577	173
Loans to local government		59,544	8,090
Marketable securities		208	152
Deposits		834	373
Derivatives		12,564	2,106
Fair value hedge ineffectiveness	2(d)	-	-
Total interest income		**73,727**	10,894
Interest expense on			
Bonds		67,195	9,793
Borrower notes		859	117
Total interest expense		**68,054**	9,910
Net interest income		**5,673**	984
Operating expenses			
Issuance and on-lending expenses	3	1,199	567
Pre-establishment expenses		-	3,843
Operating expenses	4	1,843	817
Total expenses		**3,042**	5,227
Net operating profit (loss)		**2,632**	(4,243)
Total comprehensive income (deficit) for the period		**2,632**	(4,243)

Statement of changes in equity

For the year ended 30 June 2013
in $000s

	Note	Share Capital	Retained earnings	Total equity
Opening balance at 1 December 2011				
Deficit for the period (7 months ended 30 June 2012)		-	(4,243)	(4,243)
Total comprehensive income / (deficit) for the period		-	(4,243)	(4,243)
Share capital issued		25,000	-	25,000
Equity as at 30 June 2012	9	25,000	(4,243)	20,757
Surplus for the period		-	2,632	2,632
Total comprehensive income / (deficit) for the period		**-**	**2,632**	**2,632**
Equity as at 30 June 2013	9	**25,000**	**(1,611)**	**23,389**

These statements are to be read in conjunction with the notes to the financial statements

NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY LIMITED

Statement of financial position

As at 30 June 2013
in $000s

	Note	2013	2012
Assets			
Financial assets			
Cash and cash equivalents		41,932	18,363
Trade and other receivables		51	87
Loans to local government	5	2,514,946	832,715
Marketable securities		-	10,708
Deposits		24,322	23,693
Derivatives in gain	2	106,725	57,261
Non-financial assets			
Prepayments		238	179
Property, plant and equipment		9	13
Total assets		**2,688,223**	943,019
Equity			
Share capital		25,000	25,000
Retained earnings		(1,611)	(4,243)
Total equity		**23,389**	20,757
Liabilities			
Financial liabilities			
Trade and other payables		436	79
Accrued expenses		137	98
Bonds	6	2,623,589	908,864
Borrower notes	7	40,672	13,221
Total liabilities		**2,664,834**	922,262
Total equity and liabilities		**2,688,223**	943,019

These statements are to be read in conjunction with the notes to the financial statements

Statement of cash flows

For the year ended 30 June 2013
in $000s

	Note	12 months ended **2013**	7 months ended 2012
Cash flow from operating activities			
Cash applied to loans to local government		(1,679,276)	(830,094)
Interest paid on bonds issued		(67,346)	(7,708)
Interest received from cash and cash equivalents		577	169
Interest received from loans to local government		56,588	5,470
Interest received from marketable securities		666	237
Interest received on deposits		804	81
Net interest on derivatives		15,315	2,557
Payments to suppliers and employees		(2,669)	(5,317)
Net cash flow from operating activities	8	**(1,675,341)**	(834,605)
Cash flow from investing activities			
Maturity (Purchase) of marketable securities		10,250	(10,793)
Purchase of deposits		(600)	(23,400)
Purchase of plant and equipment		-	(13)
Net cash flow from investing activities		**9,650**	(34,206)
Cash flow from financing activities			
Cash from initial equity		-	25,000
Cash proceeds from borrower notes		26,592	13,104
Cash proceeds from bonds issued		1,769,012	892,566
Cash applied to derivatives		(106,344)	(43,496)
Net cash flow from financing activities		**1,689,260**	887,174
Net (decrease) / increase in cash		**23,569**	18,363
Cash and cash equivalents at beginning of year		18,363	-
Cash and cash equivalents at end of year		**41,932**	18,363

These statements are to be read in conjunction with the notes to the financial statements

Notes to the financial statements

1 Statement of accounting policies

a Reporting Entity

The New Zealand Local Government Funding Agency Limited (LGFA) is a company registered under the Companies Act 1993 and is subject to the requirements of the Local Government Act 2002.

LGFA is controlled by participating local authorities and is a council-controlled organisation as defined under section 6 of the Local Government Act 2002. LGFA is a limited liability company incorporated and domiciled in New Zealand.

The primary objective of LGFA is to optimise the debt funding terms and conditions for participating local authorities.

The registered address of LGFA is Level 13, 342 Lambton Quay, Wellington Central, Wellington 6011.

The financial statements are as at and for the year ended 30 June 2013. The comparatives are for the seven month period to 30 June 2012 as LGFA was first registered as a company on 1 December 2011.

These financial statements were authorised for issue by the Directors on 27 September 2013.

b Statement of compliance

LGFA is registered under the Companies Act 1993 and is a reporting entity as defined by the Financial Reporting Act 1993. LGFA is a profit orientated entity as defined under the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS).

The financial statements and accounting policies comply with the specific recognition, measurement and disclosure requirements of NZ IFRS and New Zealand Generally Accepted Accounting Practice (NZGAAP). The financial statements comply with International Financial Reporting Standards.

c Basis of Preparation

Measurement base

The financial statements have been prepared on a historical cost basis modified by the revaluation of certain assets and liabilities.

The financial statements are prepared on an accrual basis.

Functional and presentation currency

The financial statements are presented in New Zealand dollars rounded to the nearest thousand, unless separately identified. The functional currency of LGFA is New Zealand dollars.

Foreign currency conversions

Transactions denominated in foreign currency are translated into New Zealand dollars using exchange rates applied on the trade date of the transaction.

Changes in accounting policies

There have been no changes in accounting policies.

Early adoption standards and interpretations

The following accounting standard has been early adopted by LGFA.

NZ IFRS 9: *Financial Instruments*. The first two phases of this new standard (which is incomplete as at 30 June 2013) were approved by the Accounting Standards Review Board in November 2009 and November 2010. The standard addresses the issues of classification and measurement of financial assets and financial liabilities and becomes effective for annual reporting periods commencing on or after 1 January 2015.

Notes to the financial statements

Standards not yet adopted

LGFA does not consider any standards or interpretations in issue but not yet effective to have a significant impact on its financial statements. Those which may be relevant to LGFA are as follows:

- Amendments to NZ IAS 32: Financial Instruments: Disclosures. Effective for periods beginning on or after 1 January 2014. This amendment provides clarification on the ability to set-off financial instruments.

- NZ IFRS 13: Fair Value Measurement. Effective for periods beginning on or after 1 January 2013. This standard provides a single source of guidance on determining fair value.

d Financial instruments

Financial assets

Financial assets, other than derivatives, are recognised initially at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest rate method.

Cash and cash equivalents include cash on hand; cash in transit, bank accounts and deposits with an original maturity of no more than three months.

Purchases and sales of all financial assets are accounted for at trade date.

At each balance date an assessment is made whether a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Financial liabilities

Financial liabilities, other than derivatives, are recognised initially at fair value less transaction costs and subsequently measured at amortised cost using the effective interest rate method.

Derivatives

Derivative financial instruments are recognised both initially and subsequently at fair value. They are reported as either assets or liabilities depending on whether the derivative is in a net gain or net loss position respectively.

Fair value hedge

Where a derivative qualifies as a hedge of the exposure to changes in fair value of an asset or liability (fair value hedge) any gain or loss on the derivative is recognised in profit and loss together with any changes in the fair value of the hedged asset or liability.

The carrying amount of the hedged item is adjusted by the fair value gain or loss on the hedged item in respect of the risk being hedged. Effective parts of the hedge are recognised in the same area of profit and loss as the hedged item.

e Other assets

Property, plant and equipment (PPE)

Items of property, plant and equipment are initially recorded at cost.

Depreciation is charged on a straight-line basis at rates calculated to allocate the cost or valuation of an item of property, plant and equipment, less any estimated residual value, over its remaining useful life.

f Other liabilities

Employee entitlements

Employee entitlements to salaries and wages, annual leave and other similar benefits are recognised in the profit and loss when they accrue to employees.

Notes to the financial statements

g Revenue and expenses

Revenue

Interest income

Interest income is accrued using the effective interest rate method.

The effective interest rate exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount. The method applies this rate to the principal outstanding to determine interest income each period.

Expenses

Expenses are recognised in the period to which they relate.

Interest expense

Interest expense is accrued using the effective interest rate method.

The effective interest rate exactly discounts estimated future cash payments through the expected life of the financial liability to that liability's net carrying amount. The method applies this rate to the principal outstanding to determine interest expense each period.

Income tax

LGFA is exempt from income tax under Section 14 of the Local Government Borrowing Act 2011.

Goods and services tax

All items in the financial statements are presented exclusive of goods and service tax (GST), except for receivables and payables, which are presented on a GST-inclusive basis. Where GST is not recoverable as input tax, then it is recognised as part of the related asset or expense.

The net amount of GST recoverable from, or payable to, the IRD is included as part of receivables or payables in the statement of financial position.

The net GST paid to, or received from the IRD, including the GST relating to investing and financing activities, is classified as a net operating cash flow in the statement of cash flows.

Commitments and contingencies are disclosed exclusive of GST.

h Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

i Segment reporting

LGFA operates in one segment being funding of participating local authorities in New Zealand.

j Judgements and estimations

The preparation of these financial statements requires judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. For example, the present value of large cash flows that are predicted to occur a long time into the future depends critically on judgements regarding future cash flows, including inflation assumptions and the risk free discount rate used to calculate present values. Refer note 2b for fair value determination for financial instruments.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

Notes to the financial statements

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Where these judgements significantly affect the amounts recognised in the financial statements they are described below and in the following notes.

Notes to the financial statements

2 Analysis of financial assets and financial liabilities

a Categories of financial instruments

The fair value of financial assets and financial liabilities, together with the carrying amounts shown in the Statement of Financial Position, are as follows:

As at 30 June 2013 *in $000s*	Financial liabilities at amortised cost	Financial assets at amortised cost	Financial assets measured at fair value in accordance with IFRS 9	Fair value
Financial assets				
Cash and bank	-	41,932	-	41,932
Trade & other receivables	-	51	-	51
Loans to local government	-	2,514,946	-	2,544,753
Deposits	-	24,322	-	24,322
Derivatives	-	-	106,725	106,725
		2,581,251	**106,725**	**2,717,783**
Financial liabilities				
Trade & other payables	436	-	-	436
Bonds	2,623,589	-	-	2,638,742
Borrower notes	40,672	-	-	40,581
	2,664,697	**-**	**-**	**2,679,759**

As at 30 June 2012 *in $000s*	Financial liabilities at amortised cost	Financial assets at amortised cost	Financial assets measured at fair value in accordance with IFRS 9	Fair value
Financial assets				
Cash and bank	-	18,363	-	18,363
Trade & other receivables	-	87	-	87
Loans to local government	-	832,715	-	844,147
Marketable securities	-	10,708	-	10,712
Deposits	-	23,693	-	23,717
Derivatives	-	-	57,261	57,261
		885,566	57,261	954,287
Financial liabilities				
Trade & other payables	79	-	-	79
Bonds	908,864	-	-	918,553
Borrower notes	13,221	-	-	13,299
	922,164	-	-	931,931

Cash and bank, trade & other receivables, deposits, trade & other payables

The carrying value of cash and bank, trade & other receivables, deposits, trade & other payables approximate their fair value as they are short-term instruments.

Marketable securities and bonds

The fair value of marketable securities and bonds is determined using the quoted price for the instrument.

Loans to local government

The fair value of loans to local government authorities is determined using a discounted cash flow analysis. The interest rates used to discount the estimated cash flows are based on LGFA bond yields at the reporting date plus an appropriate credit spread to reflect the counterparty's credit risk.

Notes to the financial statements

Borrower notes

The fair value of borrower notes is determined using a discounted cash flow analysis. The interest rates used to discount the estimated cash flows are based on LGFA bond yields at the reporting date.

Derivative financial instruments

The fair value of derivative financial instruments is determined using a discounted cash flow analysis. Interest rates represent the most significant assumption used in valuing derivative financial instruments. The interest rates used to discount estimated cash flows are based on the New Zealand dollar swap curves at the reporting date.

b Fair value

The fair values of financial instruments recognised in the statement of financial position are determined according to the following hierarchy:

- *Level 1* - Quoted market prices: Fair value based on quoted prices in active markets for identical assets or liabilities.
- *Level 2* - Valuation techniques using observable market inputs: Fair value based on a valuation technique using other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices).
- *Level 3* - Valuation techniques using significant non-observable market inputs: Fair value based on a valuation technique using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level in the fair value hierarchy within which the fair value is categorised shall be determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

As at 30 June 2013 *in $000s*	Level 1	Level 2	Level 3	Total fair value
Financial assets				
Derivatives	-	106,725	-	106,725
	-	**106,725**	**-**	**106,725**

As at 30 June 2012 *in $000s*	Level 1	Level 2	Level 3	Total fair value
Financial assets				
Derivatives	-	57,261	-	57,261
	-	57,261	-	57,261

c Financial risk management

The Board of Directors has overall responsibility for carrying out the business of LGFA in accordance with risk management policies, including those relating to investing, lending, borrowing and treasury activities. The use of financial instruments exposes LGFA to a number of financial risks, the most significant being market risk, credit risk, and liquidity risk. The exposure and management of these risks is outlined below.

Market risk

Market risk is the risk that changes in market prices will affect LGFA's income or value of financial instruments. The most significant market risk which LGFA is exposed to is interest rate risk. LGFA has no significant exposure to foreign exchange risk.

Interest rate risk

Interest rate risk is the risk that future cash flows or the fair value of financial instruments will decrease because of a change in market interest rates. LGFA is exposed to interest rate risk through its interest-bearing financial assets and liabilities. Interest rate risk is managed by matching the interest rate repricing profile of its assets against the repricing profile of its liabilities. Where mismatches occur, interest rate swaps are used to economically convert the repricing profile of financial liabilities.

Notes to the financial statements

The table below indicates the effective interest rate and the earliest period in which interest-bearing financial instruments reprice.

As at 30 June 2013 *in $000s*	Total nominal value	Less than 6 months	6 months to 1 year	1 year to 2 years	2 years to 5 years	More than 5 years
Financial assets						
Cash and bank	41,932	41,932	-	-	-	-
Loans to local government	2,481,000	1,962,000	-	25,000	130,500	363,500
Deposits	24,000	24,000	-	-	-	-
Financial liabilities						
Bonds	(2,475,000)	-	-	(165,000)	(850,000)	(1,460,000)
Borrower notes	(39,696)	(31,392)	-	(400)	(2,088)	(5,816)
Derivatives	-	(1,960,700)	-	140,000	720,500	1,100,200
Total	**32,236**	**35,840**	**-**	**(400)**	**(1,088)**	**(2,116)**

As at 30 June 2012 *in $000s*	Total nominal value	Less than 6 months	6 months to 1 year	1 year to 2 years	2 years to 5 years	More than 5 years
Financial assets						
Cash and bank	18,363	18,363	-	-	-	-
Loans to local government	819,000	616,000	-	-	25,000	178,000
Marketable securities	10,250	-	10,250	-	-	-
Deposits	23,400	23,400		-	-	-
Financial liabilities						
Bonds	(835,000)	-	-	-	(155,000)	(680,000)
Borrower notes	(13,104)	(9,856)	-	-	(400)	(2,848)
Derivatives	-	(634,000)	-	-	130,000	504,000
Total	22,909	13,907	10,250	-	(400)	(848)

Interest rate sensitivity

Changes in interest rates impact the fair value of fixed rate assets and liabilities, cash flows on floating rate assets and liabilities, and the fair value and cash flows of interest rate swaps. A change of 100 basis points in interest rates at the reporting date would have increased/(decreased) profit or loss and equity by the amounts shown in the following table. This analysis assumes that all other variables remain constant.

As at 30 June 2013 *in $000s*	**2013** Profit and loss		2012 Profit and loss	
	100 bps increase	100 bps decrease	100 bps increase	100 bps decrease
Fair value sensitivity analysis				
Derivatives	(89,519)	95,132	(28,366)	29,995
Fixed rate liabilities	89,519	(95,132)	28,366	(29,995)
	-	**-**	-	-
Cash flow sensitivity analysis				
Variable rate assets	19,620	(19,620)	6,160	(6,160)
Variable rate liabilities	(314)	314	(99)	99
Derivatives	(19,607)	19,607	(6,340)	6,340
	(301)	**301**	(279)	279

Credit risk

Credit risk is the risk of financial loss if a counterparty to a financial instrument fails to meet its contractual obligations. LGFA is exposed to credit risk through its lending and investing activities.

Notes to the financial statements

Credit risk associated with lending activities is managed by requiring local authorities that borrow from LGFA to meet specific credit lending criteria and to provide security against the borrowing. The LGFA's credit risk framework restricts credit exposures to specific counterparties.

Credit risk associated with investing activities, excluding on-lending, is managed by only investing with New Zealand Government Agencies or counterparties that meet a minimum credit rating of A (Standard & Poor's equivalent). The LGFA's credit risk framework limits concentrations of credit risk for any particular counterparty.

Exposure to credit risk

LGFA monitors the concentration of credit risk by the type of counterparty. The carrying value and maximum exposure to credit risk at the reporting date, before taking account of collateral or other credit enhancements, for significant counterparty types are shown in the table below.

As at 30 June 2013 *in $000s*	NZ Government agencies	NZ local authorities	NZ registered banks	Other counter-parties	Total carrying value
Financial assets					
Cash and bank balances	41,401	-	531	-	41,932
Trade & other receivables	51	-	-	-	51
Loans to local government	-	2,514,946	-	-	2,514,946
Deposits	-	-	24,322	-	24,322
Derivatives	106,725	-	-	-	106,725
	148,177	**2,514,946**	**24,853**	**-**	**2,687,976**

As at 30 June 2012 *in $000s*	NZ Government agencies	NZ local authorities	NZ registered banks	Other counter-parties	Total carrying value
Financial assets					
Cash and bank balances	17,930	-	433	-	18,363
Trade & other receivables	-	-	-	87	87
Loans to local government	-	832,715	-	-	832,715
Marketable securities	10,708	-	-	-	10,708
Deposits	-	-	23,693	-	23,693
Derivatives	57,261	-	-	-	57,261
	85,899	832,715	24,126	87	942,827

Collateral and credit enhancements

LGFA holds collateral against borrowings from local authorities in the form of debenture securities and guarantees.

Credit quality of financial assets

All financial assets are neither past due or impaired. The carrying value of the financial assets is expected to be recoverable.

Liquidity risk

Liquidity risk is the risk that LGFA will encounter difficulty in meeting the obligations of its financial liabilities. LGFA manages liquidity risk by holding cash and a portfolio of liquid assets to meet obligations when they fall due.

The New Zealand Debt Management Office also provide a committed liquidity facility that LGFA can draw upon to meet any exceptional and temporary liquidity shortfall. As at 30 June 2013, the committed liquidity facility was $400 million (2012: $500 million).[6]

6 The facility's maximum aggregate principal amount is currently set at $700 million and will incrementally increase to $1,000 million by February 2015, unless LGFA selects a lower amount. LGFA has selected a maximum aggregate principal amount of $400 million for the period from 20 August 2013 to 20 February 2014.

Notes to the financial statements

Contractual cash flows of financial instruments

The contractual cash flows associated with financial assets and liabilities are shown in the table below.

As at 30 June 2013 *in $000s*	On demand	Up to 3 months	3 months to 1 year	1 to 5 years	More than 5 years	Total contract cash flows	Total carrying value
Financial assets							
Cash	41,932	-	-	-	-	41,932	41,932
Trade & other receivables		51	-	-	-	51	51
Loans to local government		22,848	78,540	1,465,664	1,614,711	3,181,764	2,514,946
Deposits		24,415	-	-	-	24,415	24,322
Financial liabilities							
Trade & other payables		(436)	-	-	-	(436)	(436)
Bonds		(24,375)	(114,375)	(1,514,800)	(1,596,050)	(3,249,600)	(2,623,589)
Borrower notes		-	-	(19,504)	(31,064)	(50,568)	(40,672)
Derivatives		3,193	41,005	59,713	11,719	115,629	106,725
Total	**41,932**	**25,696**	**5,170**	**(8,927)**	**(684)**	**63,187**	**23,279**

As at 30 June 2012 *in $000s*	On demand	Up to 3 months	3 months to 1 year	1 to 5 years	More than 5 years	Total contract cash flows	Total carrying value
Financial assets							
Cash	18,363	-	-	-	-	18,363	18,363
Trade & other receivables	-	87	-	-	-	87	87
Loans to local government	-	7,300	27,691	273,850	713,359	1,022,200	832,715
Marketable securities	-	-	10,916	-	-	10,916	10,708
Deposits	-	23,781	-	-	-	23,781	23,693
Financial liabilities							
Trade & other payables		(79)				(79)	(79)
Bonds	-	(1,875)	(47,475)	(333,800)	(705,650)	(1,088,800)	(908,864)
Borrower notes	-	-	-	(2,303)	(13,693)	(15,996)	(13,221)
Derivatives	-	(4,975)	21,108	42,879	2,909	61,921	57,261
Total	18,363	24,239	12,240	(19,374)	(3,075)	32,393	20,663

d Hedge accounting

LGFA is exposed to interest rate risk from fixed rate borrowing and variable rate lending to Councils. LGFA manages this interest rate risk through the use of interest rate swaps. For hedge accounting purposes, LGFA has designated these swaps in fair value relationships to its fixed rate borrowing.

The gain or loss on the hedging instrument and the hedged item attributable to the hedged risk for fair value hedge relationships is shown in the table below.

For the period ended 30 June 2013 *in $000s*	**2013** Gain/(loss)	2012 Gain/(loss)
Hedging instruments – interest rate swaps	(54,135)	14,242
Hedged item attributable to the hedged risk – fixed rate bonds	54,135	(14,242)
Ineffectiveness recognised in profit or loss from fair value hedges	**-**	**-**

The gains or losses on the hedging instrument (interest rate swaps) and the hedged item (bonds) are mapped to the same fair value account. For this reason, the statement of comprehensive income will only report any ineffectiveness arising from the fair value hedge.

Notes to the financial statements

3 Issuance and on-lending expenses

For the period ended 30 June 2013 *in $000s*	12 months ended **2013**	7 months ended 2012
NZDMO processing fees	146	61
NZDMO standby facility fee	233	83
Rating agencies fees	555	290
Legal fees for issuance	106	101
Regulatory, registry, other fees	20	8
Trustee fees	86	24
Approved issuer levy	53	-
	1,199	567

4 Operating expenses

For the period ended 30 June 2013 *in $000s*	12 months ended **2013**	7 months ended 2012
Consultants	2	35
Directors fees	303	142
Insurance	61	32
Legal fees	264	28
Other expenses	291	177
Auditor's remuneration		
Statutory audit	80	77
Advisory services*	21	25
Personnel	821	238
Recruitment	-	63
	1,843	817

* Auditor's remuneration for advisory services relates to work performed over accounting policy options

Notes to the financial statements

5 Loans to local government

As at 30 June 2013 *in $000s*	Face value	Unamortised premium	Accrued interest	Total
Auckland Council	860,000	19,300	4,559	883,859
Ashburton District Council	10,000	940	75	11,015
Christchurch City Council	390,000	-	415	390,415
Far North District Council	10,000	-	39	10,039
Gisborne District Council	5,000	-	6	5,006
Greater Wellington Regional Council	75,000	-	246	75,246
Grey District Council*	15,000	836	108	15,943
Hamilton City Council	195,000	-	444	195,444
Hastings District Council	30,000	-	79	30,079
Hauraki District Council	14,000	-	28	14,028
Horowhenua District Council	23,000	652	190	23,843
Hutt City Council	10,000	376	145	10,522
Kapiti Coast District Council	100,000	-	114	100,114
Manawatu District Council	14,000	408	65	14,473
Masterton District Council	25,000	-	31	25,031
Matamata-Piako District Council	11,000	-	14	11,014
Nelson City Council	10,000	-	24	10,024
New Plymouth District Council	21,000	-	26	21,026
Otorohanga District Council	6,000	266	51	6,317
Palmerston North City Council	32,000	-	47	32,047
Queenstown Lakes District Council	40,000	1,323	245	41,568
Rotorua District Council	20,000	291	291	20,582
Selwyn District Council	35,000	-	49	35,049
South Taranaki District Council	20,000	-	26	20,026
Tasman District Council	36,000	-	61	36,061
Taupo District Council	80,000	-	272	80,272
Tauranga City Council	110,000	308	335	110,642
Thames-Coromandel District Council	12,000	-	12	12,012
Timaru District Council	25,000	73	124	25,197
Waikato District Council	35,000	-	34	35,034
Waimakariri District Council	5,000	470	38	5,508
Waipa District Council	6,000	-	7	6,007
Wanganui District Council	19,000	-	38	19,038
Wellington City Council	30,000	-	84	30,084
Western Bay of Plenty District Council	70,000	-	93	70,093
Whakatane District Council	12,000	-	16	12,016
Whangarei District Council	70,000	-	273	70,273
	2,481,000	**25,242**	**8,704**	**2,514,946**

* Borrower only. All other councils are guarantors of LGFA. In addition, Bay of Plenty Regional Council and Marlborough District Council are guarantors of LGFA, but had not borrowed from LGFA as at 30 June 2013.

Notes to the financial statements

As at 30 June 2012 *in $000s*	Face value	Unamortised premium	Accrued interest	Total
Auckland Council	350,000	10,627	1,585	362,212
Christchurch City Council	50,000	-	79	50,079
Greater Wellington Regional Council	50,000	-	225	50,225
Hamilton City Council	100,000	-	231	100,231
Hastings District Council	15,000	-	24	15,024
Masterton District Council	10,000	-	17	10,017
Otorohanga District Council	3,000	181	7	3,188
Selwyn District Council	20,000	-	33	20,033
Tasman District Council	16,000	-	26	16,026
Taupo District Council	50,000	-	240	50,240
Tauranga City Council	50,000	-	142	50,142
Wellington City Council	15,000	-	2	15,002
Western Bay of Plenty District Council	45,000	-	74	45,074
Whangarei District Council	45,000	-	222	45,222
	819,000	10,808	2,907	832,715

6 Bonds issued

As at 30 June 2013 *in $000s*		Face value	Unamortised premium	Accrued interest	Fair value hedge adjustment	Total
15 April 2015	6% coupon	165,000	6,262	2,056		
15 December 2017	6% coupon	850,000	58,372	2,090		
15 March 2019	5% coupon	975,000	47,614	14,174		
15 May 2021	6% coupon	485,000	54,276	3,638		
		2,475,000	**166,524**	**21,958**	**(39,893)**	**2,623,589**

As at 30 June 2012 *in $000s*		Face value	Unamortised premium	Accrued interest	Fair value hedge adjustment	Total
15 April 2015	6% coupon	155,000	8,849	1,931		
15 December 2017	6% coupon	605,000	42,253	1,488		
15 March 2019	5% coupon	75,000	4,011	1,090		
		835,000	55,113	4,509	14,242	908,864

Notes to the financial statements

7 Borrower notes

Borrower notes are subordinated debt instruments (which are required to be held by each local authority that borrows from LGFA in an amount equal to 1.6% of the aggregate borrowings by that local authority).

LGFA may convert borrower notes into redeemable shares if it has made calls for all unpaid capital to be paid in full and the LGFA Board determines it is still at risk of imminent default.

As at 30 June 2013 *in $000s*	Face value	Accrued interest	Total
Auckland Council	13,760	414	14,174
Ashburton District Council	160	1	161
Christchurch City Council	6,240	103	6,343
Far North District Council	160	1	161
Gisborne District Council	80	1	81
Greater Wellington Regional Council	1,200	40	1,240
Grey District Council	240	1	241
Hamilton City Council	3,120	86	3,206
Hastings District Council	480	9	489
Hauraki District Council	224	2	226
Horowhenua District Council	368	4	372
Hutt City Council	160	3	163
Kapiti Coast District Council	1,600	27	1,627
Manawatu District Council	224	3	227
Masterton District Council	400	11	411
Matamata-Piako District Council	176	2	178
Nelson City Council	160	1	161
New Plymouth District Council	336	6	342
Otorohanga District Council	96	3	99
Palmerston North City Council	512	5	517
Queenstown Lakes District Council	640	5	645
Rotorua District Council	320	5	325
Selwyn District Council	560	20	580
South Taranaki District Council	320	7	327
Tasman District Council	576	14	590
Taupo District Council	1,280	47	1,327
Tauranga City Council	1,760	53	1,813
Thames-Coromandel District Council	192	1	193
Timaru District Council	400	3	403
Waikato District Council	560	4	564
Waimakariri District Council	80	0	80
Waipa District Council	96	0	96
Wanganui District Council	304	4	308
Wellington City Council	480	16	496
Western Bay of Plenty District Council	1,120	38	1,158
Whakatane District Council	192	3	195
Whangarei District Council	1,120	35	1,155
	39,696	**976**	**40,672**

Notes to the financial statements

As at 30 June 2012 *in $000s*	Face value	Accrued interest	Total
Auckland Council	5,600	54	5,654
Christchurch City Council	800	8	808
Greater Wellington Regional Council	800	10	810
Hamilton City Council	1,600	10	1,610
Hastings District Council	240	0	240
Masterton District Council	160	2	162
Otorohanga District Council	48	0	48
Selwyn District Council	320	2	322
Tasman District Council	256	2	258
Taupo District Council	800	7	807
Tauranga City Council	800	7	807
Wellington City Council	240	-	240
Western Bay of Plenty District Council	720	10	730
Whangarei District Council	720	5	725
	13,104	117	13,221

8 Reconciliation of net profit/(loss) to net cash flow from operating activities

For the period ended 30 June 2013 *in $000s*	12 months ended **2013**	7 months ended 2012
Net profit/(loss) for the year	**2,632**	(4,243)
Cash applied to loans to local government	(1,679,276)	(830,094)
Non-cash adjustments		
Amortisation and depreciation	930	(179)
Working capital movements		
Net change in trade debtors and receivables	393	(8)
Net change in prepayments	(59)	(179)
Net change in accruals	39	98
Net cash flows from operating activities	**(1,675,341)**	(834,605)

Notes to the financial statements

9 Share capital

Share capital

As at 30 June 2013 LGFA had 45 million ordinary shares on issue, 20 million of which remain uncalled. All ordinary shares rank equally with one vote attached to each ordinary share. Ordinary shares are deemed to be valued at $1 each.

Second share opening

On 30 November 2012, 12 new shareholders joined LGFA as part of the second share opening. At the conclusion of the second opening, $1.3 million of paid up ordinary shares were transferred from 12 existing ‘sell-down’ shareholders to the 12 new shareholders.

Shareholder information

Registered holders of equity securities as at 30 June 2013

	2013		2012	
New Zealand Government	5,000,000	11.1%	5,000,000	11.1%
Auckland Council	3,731,960	8.3%	4,000,000	8.9%
Christchurch City Council	3,731,960	8.3%	4,000,000	8.9%
Hamilton City Council	3,731,960	8.3%	4,000,000	8.9%
Bay of Plenty Regional Council	3,731,958	8.3%	4,000,000	8.9%
Greater Wellington Regional Council	3,731,958	8.3%	4,000,000	8.9%
Tasman District Council	3,731,958	8.3%	4,000,000	8.9%
Tauranga City Council	3,731,958	8.3%	4,000,000	8.9%
Wellington City Council	3,731,958	8.3%	4,000,000	8.9%
Western Bay of Plenty District Council	3,731,958	8.3%	4,000,000	8.9%
Whangarei District Council	1,492,784	3.3%	1,600,000	3.6%
Hastings District Council	746,392	1.7%	800,000	1.8%
Marlborough District Council	400,000	0.9%	-	-
Selwyn District Council	373,196	0.8%	400,000	0.9%
Gisborne District Council	200,000	0.4%	-	-
Hauraki District Council	200,000	0.4%	-	-
Horowhenua District Council	200,000	0.4%	-	-
Hutt City Council	200,000	0.4%	-	-
Kapiti Coast District Council	200,000	0.4%	-	-
Manawatu District Council	200,000	0.4%	-	-
Masterton District Council	200,000	0.4%	200,000	0.4%
New Plymouth District Council	200,000	0.4%	200,000	0.4%
Otorohanga District Council	200,000	0.4%	200,000	0.4%
Palmerston North City Council	200,000	0.4%	-	-
South Taranaki District Council	200,000	0.4%	200,000	0.4%
Taupo District Council	200,000	0.4%	200,000	0.4%
Thames-Coromandel District Council	200,000	0.4%	-	-
Waimakariri District Council	200,000	0.4%	-	-
Waipa District Council	200,000	0.4%	200,000	0.4%
Wanganui District Council	200,000	0.4%	-	-
Whakatane District Council	200,000	0.4%	-	-
	45,000,000		45,000,000	

Notes to the financial statements

Capital management

LGFA's capital is equity, which comprises share capital and retained earnings. LGFA's equity is largely managed as a result of its revenues, expenses, assets and liabilities incurred in the normal day to day operations of the entity. The objective of managing LGFA's equity is to ensure LGFA achieves its goals and objectives for which it has been established, whilst remaining a going concern.

10 Operating leases

The future aggregate minimum lease payments to be made under non-cancellable operating leases are as follows:

in $000s	**2013**	2012
Less than one year	42	-
Between one and five years	366	-
Total non-cancellable operating leases	**408**	-

The non-cancellable operating lease expense relates to the lease of the thirteenth floor of 342 Lambton Quay, Wellington. For the year to 30 June 2013, total payments under the lease were $14,089.

11 Capital commitments

As at 30 June 2013, there are no capital commitments.

12 Contingencies

There are no material contingent liabilities at balance date.

13 Related parties

Identity of related parties

The Company is related to the local authorities set out in the Shareholder Information by shareholding.

The Company operates under a Statement of Intent with the respective local authorities that requires the Company to provide debt to them at the lowest possible interest rates and to enhance their certainty of access to debt markets.

Shareholding local authorities, and non-shareholder local authorities who borrow more than $20 million, are required to enter into a guarantee when they join or participate in LGFA. The guarantee is in respect of the payment obligations of other guaranteeing local authorities to the LGFA (cross guarantee) and of the LGFA itself.

Related party transactions

LGFA was established for the purpose of raising funds from the market to lend to participating councils. The lending to individual councils is disclosed in note 5, and interest income recognised on this lending is shown in the statement of comprehensive income.

The purchase of LGFA borrower notes by participating councils is disclosed in note 7, and the interest expense on these is shown in the statement of comprehensive income.

LGFA has contracted the NZDMO to provide outsourced treasury services for LGFA. Services include operational processing associated with debt issuance, lending to local authorities, settlement services, investments, hedging and measuring risk. In addition, NZDMO provide some accounting services. The NZDMO is an operating unit of the Treasury and provide LGFA with a committed liquidity facility.

OCG were contracted during the financial year to provide recruitment and payroll services.[7]

Transactions with key management personnel

Salaries $532,950

Fees paid to Directors are disclosed in operating expenses in note 4.

---

[7] C Stobo, Director, is a Director of OCG Consulting Ltd.

Notes to the financial statements

14 Subsequent events

There have been no significant events after balance date that have affected the accuracy of these financial statements.

Subsequent to balance date, LGFA has issued $310 million in bonds through two tenders.

Subsequent to balance date, on 24 September 2013, the Directors of LGFA declared a dividend of $1,515,000 ($0.0606 per share).

Auditors' Report

INDEPENDENT AUDITOR'S REPORT

**TO THE READERS OF
NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY LIMITED'S
FINANCIAL STATEMENTS AND STATEMENT OF SERVICE PERFORMANCE
FOR THE YEAR ENDED 30 JUNE 2013**

The Auditor-General is the auditor of New Zealand Local Government Funding Agency Limited (the company). The Auditor-General has appointed me, Graeme Edwards, using the staff and resources of KPMG, to carry out the audit of the financial statements and statement of service performance of the company on her behalf.

We have audited:

- the financial statements of the company on pages 23 to 42, that comprise the statement of financial position as at 30 June 2013, the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date and the notes to the financial statements that include accounting policies and other explanatory information; and
- the statement of service performance of the company on pages 9 to 18.

Opinion

Financial statements and statement of service performance

In our opinion,

- the financial statements of the company on pages 23 to 42:
    - comply with generally accepted accounting practice in New Zealand;
    - comply with International Financial Reporting Standards; and
    - give a true and fair view of the company's:
        - financial position as at 30 June 2013; and
        - financial performance and cash flows for the year ended on that date; and
- the statement of service performance of the company on pages 9 to 18:
-
    - complies with generally accepted accounting practice in New Zealand; and
    - gives a true and fair view of the company's service performance achievements measured against the performance targets adopted for the year ended 30 June 2013

Other legal requirements

In accordance with the Financial Reporting Act 1993 we report that, in our opinion, proper accounting records have been kept by the company as far as appears from an examination of those records.

Our audit was completed on 27 September 2013. This is the date at which our opinion is expressed.

The basis of our opinion is explained below. In addition, we outline the responsibilities of the Board of Directors and our responsibilities, and explain our independence.

Basis of opinion

We carried out our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and carry out our audit to obtain reasonable assurance about whether the financial statements and statement of service performance are free from material misstatement.

Material misstatements are differences or omissions of amounts and disclosures that, in our judgement, are likely to influence readers' overall understanding of the financial statements and statement of service performance. If we had found material misstatements that were not corrected, we would have referred to them in our opinion.

KPMG

An audit involves carrying out procedures to obtain audit evidence about the amounts and disclosures in the financial statements and statement of service performance. The procedures selected depend on our judgement, including our assessment of risks of material misstatement of the financial statements and statement of service performance whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the preparation of the company's financial statements and statement of service performance that give a true and fair view of the matters to which they relate. We consider internal control in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.

An audit also involves evaluating:

- the appropriateness of accounting policies used and whether they have been consistently applied;
- the reasonableness of the significant accounting estimates and judgements made by the Board of Directors;
- the adequacy of all disclosures in the financial statements and statement of service performance; and
- the overall presentation of the financial statements and statement of service performance.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements and statement of service performance. Also we did not evaluate the security and controls over the electronic publication of the financial statements and statement of service performance.

In accordance with the Financial Reporting Act 1993, we report that we have obtained all the information and explanations we have required. We believe we have obtained sufficient and appropriate audit evidence to provide a basis for our audit opinion.

Responsibilities of the Board of Directors

The Board of Directors is responsible for preparing financial statements and a statement of service performance that:

- comply with generally accepted accounting practice in New Zealand;
-
- give a true and fair view of the company's financial position, financial performance and cash flows; and
- give a true and fair view of its service performance.

The Board of Directors is also responsible for such internal control as it determines is necessary to enable the preparation of financial statements and a statement of service performance that are free from material misstatement, whether due to fraud or error. The Board of Directors is also responsible for the publication of the financial statements and statement of service performance, whether in printed or electronic form.

The Board of Directors' responsibilities arise from the Local Government Act 2002 and the Financial Reporting Act 1993.

Responsibilities of the Auditor

We are responsible for expressing an independent opinion on the financial statements and statement of service performance and reporting that opinion to you based on our audit. Our responsibility arises from section 15 of the Public Audit Act 2001 and section 69 of the Local Government Act 2002.

Independence

When carrying out the audit, we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.

Other than the audit and accounting policy advisory work, which are compatible with those independence requirements, we have no relationship with or interests in the company.

G Edwards

Graeme Edwards
KPMG
On behalf of the Auditor-General
Wellington, New Zealand

Board of Directors

Interests Register

Name of Director	Nature and extent of interest	
Craig Stobo (Chair)	General disclosure: Director Precinct Properties New Zealand Ltd OCG Consulting Ltd Elevation Capital Management Ltd Saturn Portfolio Management Ltd Stobo Group Ltd	AIG Insurance NZ Ltd General Disclosure LGNZ Review of insurance arrangements in the Local Government Sector
Paul Anderson	Officer CEO, NZ Ski Ltd Christchurch City Council*	General disclosure: Director Creative Licence Ltd Ecocentral Ltd Ellerslie International Flower Show Ltd* CCC One Ltd* Tuam Ltd*
John Avery	General disclosure: Director Signify Ltd Spider Tracks Ltd Fund Managers Auckland Ltd Regional Facilities Auckland Ltd Strategic Pay Ltd Office Products Depot	The New Zealand Guardian Trust Company Ltd* Comprehensive Health Services Ltd* General disclosure: Trustee The New Zealand School of Dance Stinger Trust Saint Joseph Mercy Hospice Foundation
Mark Butcher	General disclosure: Officer Office of Auckland Council.	
Philip Cory-Wright	General disclosure: Director South Port New Zealand Ltd	Member Local Government Infrastructure Expert Advisory Group*
Abigail Foote	General disclosure: Director BNZ Life Insurance Limited Transpower New Zealand Ltd Z Energy Limited	General disclosure: Other Gambling Commissioner

* Position held during the year, no longer current.

Remuneration

Non-Executive Directors	2013 ($)
Craig Stobo (Chair)	$75,000
Paul Anderson	$42,500
John Avery	$42,500
Mark Butcher	$55,500 [1]
Philip Cory-Wright	$42,500
Abby Foote	$45,000
Total	$303,000

1 Director fees for Mark Butcher are paid to Auckland Council. Includes $20,500 fees for the 2011/2012 year.

Staff Total remuneration	Staff Numbers 2013
$150,000 to $159,999	1
$210,000 to $219,999	1
$310,000 to $319,999	1
Total staff receiving $100,000 or more	3

Our shareholders

Directory

Postal address
P.O. Box 5704
Lambton Quay
Wellington 6145

Street address
Level 13
342 Lambton Quay
Wellington 6011

Office hours
Monday through Friday, 09.00-17.30 hrs.
Except Public Holidays

Main Phone
+64 4 974 6530

Personnel e-mail addresses
firstname.lastname@lgfa.co.nz