LGFA
New Zealand Local
Government Funding Agency
Te Pūtea Kāwanatanga ā-rohe

LGFA financing for local government water services - December 2025 update

In April 2025, LGFA wrote to the Mayors and CEOs of councils to outline the financial covenant framework that would apply to water CCOs.

Over recent months, water reforms have been progressing with many councils now having had their Water Service Delivery Plans (WSDPs) approved by the Secretary for Local Government.

The sector is now moving at pace to implement Local Water Done Well and therefore we intend to provide regular updates on our approach for lending to water CCOs.

This information sets out:

- An update on the legal discussions to date with water CCOs which would provide the basis for the security arrangements, guarantee structure and accession to LGFA's multi-issuer deed.
- Confirmation of the proposed financial covenant framework for a water CCO.
- The options available for councils to transfer debt to a water CCO.
- Borrowing costs for water CCOs and credit ratings.
- LGFA's ability to provide establishment financing to water CCOs.
- LGFA's ability to provide committed standby facilities to water CCOs.
- GSS lending for water CCOs.
- Governance arrangements for water CCOs.

Further support and information

LGFA continues to work closely with council finance teams, water CCO transitional teams, and the Department of Internal Affairs to provide information and support for councils as you work through the establishment of your water CCO.

We encourage you to contact us directly by emailing cameron.walker@lgfa.co.nz or andrew.michl@lgfa.co.nz if you would like further information.

LGFA is looking to assist you with your decision-making process. We look forward to continuing to support you to enable the successful delivery of water services.

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1.0 Legal Discussions with Water CCOs.

Based on the WSDPs, there are eighteen new water CCOs that are proposed to be formed.

LGFA is currently progressing legal negotiations with Selwyn Water Limited. Once these negotiations are complete, we expect to have a draft legal term sheet that we can provide to other water CCOs that are intending to join LGFA. Some of the key features are likely to be:

- Two financial covenants with a phase in period of up to five years.
- A guarantee from each of the parent councils in respect of LGFA's lending to the water CCO. In addition, LGFA will also have security over water charges.
- For multiply owned water CCOs, each council's share of the guarantee will be based on their number of drinking water connections as at 30 June each year.
- Water CCOs will accede to LGFA's multi-issuer deed. This is the same deed that councils have signed up to.

2.0 LGFA Financial Covenants for Water CCOs.

In April, LGFA provided an indication for what the financial covenants were likely to be for water CCOs. A few minor changes have been made to what was initially proposed.

LGFA can now confirm that there will be two financial covenants and one additional revenue recognition adjustment for water CCOs that wish to join LGFA. The covenants are tiered based on the number of water connections that the water CCO has. These are:

- A Funds from Operation (FFO) to Net Debt ratio of between 8% and 12%.
- A Funds from Operation (FFO) to Cash Interest Coverage of between 1.5 times and 2.0 times.
- The percentage of development contributions recognised in operation revenue.

A more detailed explanation of how these covenants will be applied is set out below:

Water Connections	FFO to Cash Interest Coverage Ratio (times)	FFO to Net Debt Ratio	Percentage of Development Contributions recognised in operating revenue
Less than 5,000	2.00	12%	0%
5,000 - 10,000	2.00	11%	25%
10,000 - 20,000	1.75	10%	50%
20,000 - 50,000	1.50	9%	50%
Greater than 50,000	1.50	8%	75%

2.1 Phase in period for water CCO Financial Covenants.

LGFA recognises that not all water CCOs will be able to comply with the financial covenants in their first year of operation. This might be the case where the initial amount of water debt transferred to the water CCO is high.

If required, a period of up to five years will be agreed on a bespoke basis with each water CCO. For water CCOs that require a phase in period there will be interim financial covenants in place to ensure there is an improving trend in ratios over time.

Any request for a phase in period longer than five years would need to be considered by the LGFA Board.

2.2 Definitions of the water CCO Financial Covenants.

Funds From Operations (FFO) to net debt: FFO to debt is a leverage ratio that LGFA, rating agency or other investor can use to evaluate a water entity's financial risk. It measures a water entity's ability to pay off debt using its net operating income alone. The higher the ratio, the stronger the position the water entity is in to repay its debt. Calculating FFO: Funds from operation is defined as EBITDA, less cash interest expenses and development contributions. The appropriate percentage of development contributions allowable is then added back.

Net Debt: Net debt is gross debt less cash and LGFA borrower notes.

FFO to cash interest: Is an interest coverage multiple calculated as (FFO plus cash interest expense) over cash interest expense. This ratio measures an entity's ability to service its debt through covering interest cost from its available cash flows.

Cash Interest Expense: Cash interest is interest payments less any interest receipts.

3.0 LGFA debt transfer options for a council to a water CCO.

LGFA will offer a range of options for councils to transfer their water debt to a water CCO. The options are:

- The water entity borrows from LGFA and then repays the council. The council is then able to determine how the proceeds are used including the options of buying back loans from LGFA.
- Novation of a council loan or part of a council loan to the water entity.
- A water entity could agree to repay debt owed to the council over a set period of time. This would involve scheduled repayments of principal.

LGFA recommends that water CCOs engage a Treasury Consultant to advise on the debt transfer strategy.

LGFA would expect to engage with water CCOs and councils on their debt transfer strategy well ahead of any proposed transfer dates so that new loan term sheets can be arranged and any cashflow implications managed.

4.0 LGFA borrowing costs for water CCOs and credit ratings.

LGFA is proposing to lend to a water CCO at the same lending margin as it would lend its parent council(s). This will apply even if the water CCO does not have an external credit rating and is consistent to the approach LGFA has when it lends to its existing eight CCTO members.

The benefit of this is that a water CCO does not have to get an external credit rating until it decides that it wants to access financing from sources other than LGFA.

For short term lending, LGFA will lend at the same margin that is applied to a "rated council".

For lending longer than 1-year, LGFA currently has a 25-basis point base lending margin. This will apply to all water CCO lending. In addition, a credit margin will be applied based on the weighted average credit quality of the parent councils. This will be weighted based on drinking water connections. LGFA will round the lending margin to the nearest basis point.

The current credit charge that applies to councils is:

Long term credit margin (+ Base lending margin)	AA+ and AA	AA-	A+ and A	Unrated guarantor	Non-guarantor
	0 bps	5 bps	10 bps	20 bps	30 bps

5.0 LGFA establishment financing for water CCOs.

LGFA's preferred position is to commence lending to a water CCO once it has acceded to LGFA's multi-issuer deed and the water assets have been transferred from councils to the water CCO. At this point the water CCO will then be able to generate revenue.

Until this point LGFA is willing to provide councils with financing for the establishment costs of their water CCO. Once the water CCO can borrow from LGFA, the water CCO will be able to repay the council for the establishment costs.

6.0 Committed Standby Facilities

LGFA will make committed standby facilities available for water CCOs. The terms will be the same as those currently offered to councils. A draft standby agreement is available from LGFA.

7.0 Sustainable lending for water CCOs

LGFA is committed to providing councils and water CCOs with sustainable financing products. Currently LGFA offer councils both Green and Social Loans and Climate Action loans.

LGFA is currently working on a new sustainable lending product for water CCOs. Water CCOs who borrow under this format will be eligible for discounted financing. For further information on sustainable borrowing please contact helen.mahoney@lgfa.co.nz

8.0 Governance arrangements for water CCOs

All water CCO's must have independent Board directors as per s48 (3) of the Local Government (Water Services) Act 2025.