Chairperson and Committee Members
CORPORATE BUSINESS COMMITTEE

19 NOVEMBER 2015

Meeting Status: **Public**

Purpose of Report: For Information

LOCAL GOVERNMENT FUNDING AGENCY 2014/15 ANNUAL REPORT

PURPOSE OF REPORT

1 The purpose of this report is to update the Corporate Business Committee on the Local Government Funding Agency (LGFA) 2014/15 Annual Report.

DELEGATION

2 While noting that this report is for information, the Corporate Business Committee has the following delegation in the Governance Structure, Section B.3: Without limiting the generality of this delegation the Committee has the following functions, duties and powers:

Financial and Asset Management

7.5 Authority to monitor performance of the Council's financial activities, including income, operating and capital expenditure against budgets, remissions, key financial indicators and investment and debt/borrowings management.

BACKGROUND

3 On 30 November 2012, Council became a Principal Shareholding Local Authority in the LGFA. The LGFA was incorporated on 1 December 2011 with the primary objective of optimising the debt funding terms and conditions for Participating Local Authorities. This includes providing savings in annual interest costs, making longer-term borrowings available and enhancing the certainty of access to debt markets.

4 The LGFA issues bonds to wholesale and retail investors and on-lends the funds raised to participating local authorities with borrowing needs. The quality of the LFGA's credit rating, and the liquidity created by issuing homogenous local authority paper, ensures that participating councils can raise funds on better terms than if they were issuing in their own name.

5 The LGFA meets the Local Government Act (LGA) 2002 definition of a Council Controlled Organisation (CCO) as one or more local authorities have the right, directly or indirectly, to appoint 50% or more of the directors.

6 As a shareholder in a CCO, the Council must regularly undertake performance monitoring of that organisation to evaluate its contribution to the achievement of the Council's desired outcomes.

Issues and Options

LGFA performance for the 2014/15 year

7 The LGFA performed strongly in the 2014/15 year with new lending to council borrowers of $1.5 billion (2014: $1.2 billion) resulting in total council borrowings of $4.96 billion as at 30 June 2015 (2014: $3.7 billion). This has resulted in increased interest income of $222.8 million (2014: $149.1 million) and while operating expenses have increased too, the LGFA still reported an operating profit of $9.2 million (2014: $7 million).

8 The increase in operating expenses is mainly due to the significant increase in Approved issuer levies, a direct consequence of the increased holding of LGFA bonds by offshore investors. The offshore investor base is now estimated at 28.5% and this is supporting the margin contraction for LGFA Bonds.

9 The strong support of the LGFA from local authorities and continued investor support, including increased offshore investment allied with favourable market conditions has allowed the LGFA to further reduce the base lending margin to councils from 0.15% in 2014 to 0.13% in 2015 and also extend the longest dated available borrowing to 2027.

10 During the year, the LGFA also introduced bespoke lending, introduced a new treasury management system and brought in-house the middle and back office services previously undertaken by the NZ Debt Management Office.

11 While the LGFA has still not achieved its primary objective of 30 bps of savings, it has undoubtedly produced savings for all participating councils. At 30 June 2015, the LGFA estimates that it was saving AA rated councils approximately 16 to 19 bps for the 2017 dated maturity and 2019 dated maturity. The Kāpiti Coast District Council has a Standard and Poor's credit rating of A+, slightly lower than AA, suggesting a lower but comparable quantum of savings.

12 The LGFA has met most of its other performance targets, most notably enhancing the certainty of access to debt markets for and making longer-term borrowings available to Participating Local Authorities. It has also met its target of making a profit sufficient to pay a dividend equal to the LGFA cost of funds plus 2%. This is discussed further in the financial considerations section.

13 The LGFA was not compliant with its Treasury Policy for the period July 2014 to November 2014 when its two largest borrowing councils had borrowings maturing in a 12-month period that were greater than both $100 million and 25% of their total borrowing from the LGFA. The LGFA shareholders have subsequently approved a change to the Treasury Policy to increase the limit to 33% of borrowings.

14 Auckland Council is the LGFA's largest borrower ($1.8 billion), followed by Christchurch City Council ($0.9 billion). As at 30 June 2015, Kāpiti Coast District Council ranked as the 7th largest borrower with $130 million.

15 The full LGFA 2014/15 Annual Report is attached as Appendix 1.

CONSIDERATIONS

Policy considerations

16 In accordance with the LGA 2002, the Council must provide information on all of its CCOs in its Long Term Plan (LTP). Accordingly the 2015/35 LTP contains information on the LGFA, including key performance targets and other performance metrics.

Legal considerations

17 There are no legal considerations arising from the matters in this report.

Financial considerations

18 Council is one of 30 local authority shareholders of the LGFA and has an obligation in respect of uncalled capital of $100,000.

19 At 30 June 2015, the LGFA had borrowings totalling $4.96 billion.

20 Council considers the risk of the LGFA defaulting on repayment of interest or capital to be very low on the basis that:

a) The only circumstance where LGFA would default on its debt is the event where a council defaulted on a loan obligation that exceeded LGFA's available liquidity assets. As at 30 June 2015, this would need to be a single council default event that exceeded $570 million, being the sum of:

- cash and deposits of $70 million, and
- LGFA borrower notes of $80 million, and
- LGFA credit facility of $400 million, and
- uncalled share capital of $20 million from LGFA shareholders.

b) In the event of an LGFA default, the call on the guarantee is made on council's proportion of their share of the underlying rate base.

c) In the event of a default exceeding the LGFA's available liquid assets, the council would be called for 1.2% of the overall call (less than the council's 2.5% of LGFA's loan assets).

Tāngata whenua considerations

21 There are no tāngata whenua considerations.

SIGNIFICANCE AND ENGAGEMENT

Degree of significance

22 This matter has a low level degree of significance under Council policy, and it is not significant.

Consultation already undertaken

23 There is no need to consult on the matters discussed in this report.

Engagement planning

24 An engagement plan is not needed for this report to be considered.

Publicity

25 There are no publicity considerations.

RECOMMENDATIONS

26 That the Corporate Business Committee notes the performance of the Local Government Funding Agency in its 2015 Annual Report.

Report prepared by	**Approved for submission by**
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Approved for submission by	**Approved for submission by**
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ATTACHMENTS

Appendix 1 – LGFA 2015 Annual Report