Chairperson and Committee Members
OPERATIONS AND FINANCE COMMITTEE

1 DECEMBER 2016

Meeting Status: **Public**

Purpose of Report: For Information

LOCAL GOVERNMENT FUNDING AGENCY 2015/16 ANNUAL REPORT

PURPOSE OF REPORT

1 The purpose of this report is to update the Operations and Finance Committee on the Local Government Funding Agency (LGFA) 2015/16 Annual Report.

DELEGATION

2 While noting that this report is for information, the Operations and Finance Committee, with its role of monitoring and decision-making on all broader financial management matters has the delegation to consider this report.

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 2015/16 year

7 The LGFA performed reasonably well during the year with continued growth in membership (five new members) and revenue (25%). The increased revenue did not result in an equivalent increase in net profit due to a number of non-recurring legal expenses due to new lending products, new council members, NZX listing fees and transition to the Financial Markets Conduct Act.

8 The LGFA has two primary objectives that it aims to achieve for participating local authorities. The first objective is to optimise debt funding terms and conditions and the second is to maintain a high quality offering that meets the needs of all participating local authorities.

9 The LGFA broadly achieved the first objective, by achieving savings for participating local authorities and further expanding the range of its offering. The LGFA estimates that as at 30 June 2016, it was saving AA rated councils between 17 basis points (bps or 0.17%) for a 2019 (three-year) maturity and 33 bps (0.33%) for a 2025 (nine-year) 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.

10 The LGFA has further increased borrowing options for participating local authorities by introducing bespoke lending and short-dated lending which provides councils with flexible lending terms for any maturity from 30 days to 11 years.

11 However, as the below table shows it only achieved one out of four of its key performance measures.

Current performance targets		Target	2015/16 Result	Achieved
1	Average cost of funds on debt issued relative to NZ Government Securities	Less than or equal to 0.50%	0.74%	No
2	Average base on-lending margin above LGFA's cost of funds	Less than or equal to 0.10%	0.106%	No
3	Annualised issuance and operating expenses	Less than or equal to $5.94 million	$5.98 million	No
4	Long-term lending to participating councils	Greater than or equal to $5.885 billion	$6.241 billion	Yes

12 The average cost of funds has increased from 0.64% in 2014/15 to 0.74% in 2015/16. Over the past twelve months there have been a number of factors that have led to a widening in spreads for all non-government borrowers. Investors have been concerned over the global economic outlook, volatility arising from events such as BREXIT and managing investments in a low interest rate environment. As a result, there has been a reduction in risk sentiment and this has reduced demand for NZD investments and for bonds issued by non-government borrowers.

13 Two of the targets were only missed by a small amount; further context is that the average base on-lending margin has decreased from 0.15% in 2014 to just over 0.10% in 2016. Annualised issuance and operating expenses were 0.5% over budget due to one-off legal expenses as mentioned previously.

14 An objective assessment of how the LGFA performed against its second primary objective would require independent discussion with all participating local authorities which is well beyond the scope of this report.

15 From the perspective of the Kāpiti Coast District Council, the LGFA has provided borrowing with interest rates and lending terms that have enabled the Council to meet its financial objectives and to stay within its financial targets.

16 Auckland Council is the LGFA's largest borrower ($2.2 billion), followed by Christchurch City Council ($1.3 billion). As at 30 June 2016, Kāpiti Coast District Council ranked as the 7th largest borrower with $150 million.

17 The full LGFA 2015/16 Annual Report is attached as Appendix 1.

CONSIDERATIONS

Policy considerations

18 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

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

Financial considerations

20 Council is one of 31 Local Authority shareholders of the LGFA which has the objective of operating with a view to making sufficient profit to declare a dividend that provides an annual rate of return to its shareholders equal to LGFA cost of funds plus 2%.

21 On 20 September 2016 the directors declared a dividend for 2016 of $1.393 million ($0.0557 per share). As the holder of 100,000 paid up ordinary shares this will mean a dividend of $5,570 for the Council. The falling interest rates have resulted in a lower cost of funds for the LGFA, and therefore lower borrowing costs for councils however this also means a lower dividend payment.

22 Council also has an obligation in respect of uncalled capital of $100,000. At 30 June 2016, the LGFA had borrowings totalling $6.445 billion (2015: $4.955 billion).

23 Officers consider 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 2016, this would need to be a single council default event that exceeded $570 million, being the sum of:

- cash and deposits of $126 million, and
- LGFA borrower notes of $99 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

24 There are no tāngata whenua considerations.

SIGNIFICANCE AND ENGAGEMENT

Degree of significance

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

Consultation already undertaken

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

Engagement planning

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

Publicity

28 There are no publicity considerations.

RECOMMENDATIONS

29 That the Operations and Finance Committee notes the performance of the Local Government Funding Agency as set out in its 2015/16 Annual Report.

Report prepared by	**Approved for submission by**
Ian Clements **Corporate Advisor**	**Wayne Maxwell** **Group Manager Corporate Services**

Approved for submission by

Kevin Currie
Group Manager Regulatory Services

Appendix 1 – LGFA 2015/16 Annual Report

Appendix 1 Corp-16-035

LGFA

NEW ZEALAND
LOCAL GOVERNMENT
FUNDING AGENCY

ANNUAL REPORT

30 JUNE 2016

Contents

Cover: Victoria Street, Wellington. Upgraded lanes, parking and pedestrian area on Victoria Street. Wellington City Council.

Left: Te Ara I Whiti Cycleway and Walkway – linking Upper Queen Street to Quay Street. Auckland Council. Photo: Hakan Nedjat.

CHAIRMAN'S REPORT

FOR THE YEAR ENDED 30 JUNE 2016

"Over the past four-and-a-half years LGFA has exceeded expectations with strong growth in assets, market share and development of products that have reduced the cost of borrowing, extended the term of the sector debt and provided greater access to markets."

Craig Stobo, Chairman LGFA Board

Directors are pleased to report another strong period of financial and non-financial performance of LGFA to 30 June 2016 and to highlight the following developments over the past year.

Strong Financial and Operational Performance

LGFA total interest income for the financial year of $278 million was a 25% increase over the 2014-15 financial year result of $223 million while net operating profit of $9.55 million for the financial year was a 4% increase on the 2014-15 financial year result of $9.20 million. Net operating profit did not match the growth in interest income as operating expenses were higher due to the listing of LGFA bonds on the NZX; the introduction of short-dated lending to councils; new issuance of LGFA Bills, transition to Financial Markets Conduct Act and the admittance of five new council members. These expenses are largely non-recurring and are an investment in the future business through making LGFA bonds a more attractive investment and delivering longer-dated and cheaper funding to council borrowers.

The financial strength of the LGFA was reaffirmed by credit rating agencies Standard and Poor's and Fitch who both maintained our credit rating at AA+, which is the same as the New Zealand Government.

LGFA successfully transitioned all front, middle and back office activities from the New Zealand Debt Management Office (NZDMO) on 1 July 2015. NZDMO remain the counterparty for derivative transactions.

The performance of the organisation was recognised with LGFA receiving the INFINZ Excellence in Treasury Award for 2015 and Mark Butcher receiving the KangaNews New Zealand Treasurer of the Year Award for the fourth time in the past five years.

Borrowing activity

LGFA issued $1.265 billion of bonds over the year and outstandings now total $6.220 billion across seven maturities from 2017 to 2027. LGFA commenced issuance of an April 2025 bond in June 2016 and continued with its proven issuance strategy of replicating the New Zealand Government Bond curve. LGFA is now one of the largest issuer of NZD securities after the New Zealand Government and our bonds are amongst the largest and most liquid New Zealand dollar (NZD) debt instruments available for investors.

LGFA successfully launched its short-dated LGFA Bill programme in October 2015 and now tenders 3-month and 6-month LGFA Bills on a monthly basis. Outstandings under the programme have reached $225 million. These instruments provide a source of funding for short-dated lending to our council borrowers and also assist LGFA with liquidity management.

NZX listing

On 16 November 2015, LGFA listed its bonds on the NZX Debt Market which was the largest listing in the history of the NZX. This has increased our domestic and offshore investor base and added to the liquidity of our bonds. Since listing, LGFA bonds have accounted for approximately 11% of market turnover on the NZX Debt market.

Wellington Airport, Southern end of Wellington Airport showing the runway. Wellington City Council.

Lending to the sector

LGFA was established four-and-a-half years ago to provide long-dated borrowing, certainty of access to markets and to reduce the borrowing costs for the local government sector. It is pleasing to note the following achievements over the past financial year:

- We added five new members with Buller District Council, Canterbury Regional Council, Gore District Council, Kaipara District Council and South Wairarapa District Council. Total membership is now fifty councils.
- Bespoke lending continues to be popular for councils in that it provides flexibility as to maturity dates of borrowing and the date of drawdown. LGFA lent $407 million on a bespoke basis over the financial year. This was approximately 31% of our total long-dated lending over that period.
- Following the issuance of LGFA Bills we were able to offer short-dated lending (less than 365 day terms) to councils. As at 30 June 2016, LGFA had $158.7 million of short-term loans outstanding to thirteen councils.
- The tenor of lending by LGFA to the sector continued to lengthen with the average term of borrowing by councils for the financial year of 8.1 years.

Milestone – Five years of delivering value to local government in New Zealand

This is the fifth annual report for LGFA and directors and staff are proud of the achievements since we were established in December 2011. Over the past four-and-a-half years LGFA has exceeded expectations with strong growth in assets, market share and development of products that have reduced the cost of borrowing, extended the term of the sector debt and provided greater access to markets.

We are looking forward to the next five-year growth phase of the LGFA. We believe we have the right structures in place to manage this next phase and meet the needs of our various stakeholder groups – council borrowers, local and central government as shareholders, council guarantors and our investor base comprising domestic and offshore institutional and retail investors.

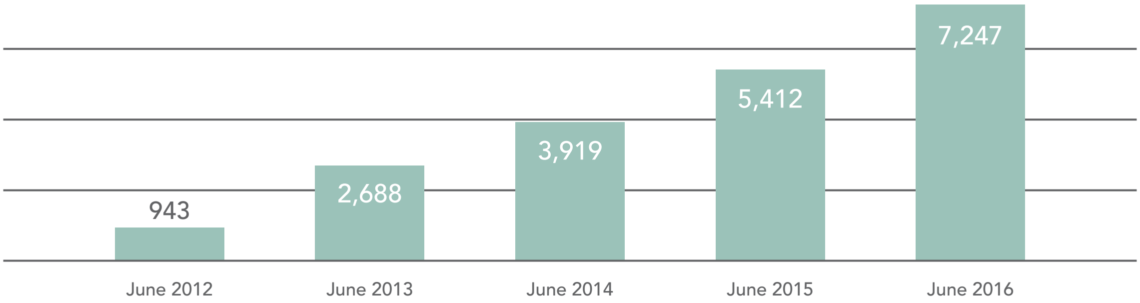
During the growth phase directors will maintain a consistent and conservative approach to our capital management strategy through:

- Providing steady dividends to our shareholders in line with our cost of borrowing, noting that we commenced dividend payments earlier than forecast in the foundation business plan;
- Providing the lowest funding margins for our borrowers; and
- Building our capital base through retained earnings to maintain our credit rating and to minimise risk for our guarantors.

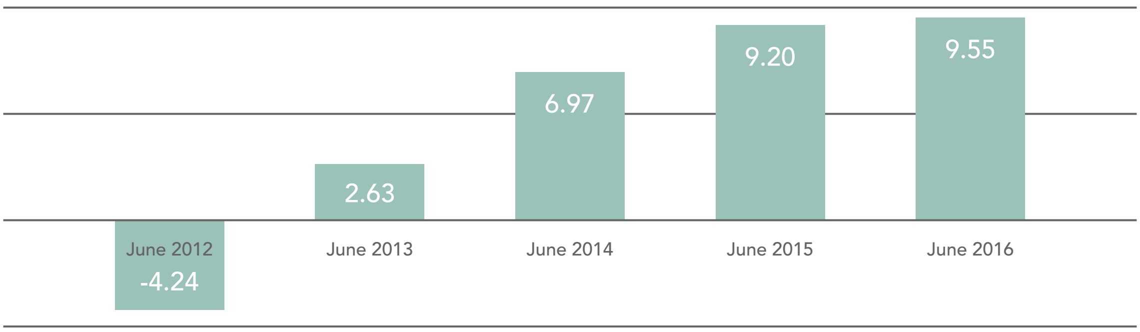
The Agency's work cannot be implemented without the support of our staff and fellow directors all of whose efforts should be acknowledged. In that regard I would like to acknowledge the contribution of your new directors Linda Robertson and Mike Timmer. I would like to also thank Mark Butcher, our Chief Executive for his leadership of the organisation over the past year. Directors believe the Agency's future remains positive and look forward to working with all stakeholders in the year ahead.

Craig Stobo
Chairman, LGFA Board

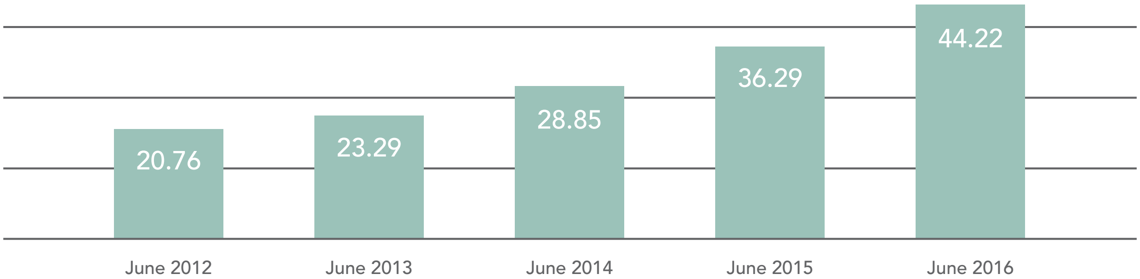
Total Assets (NZ$m)



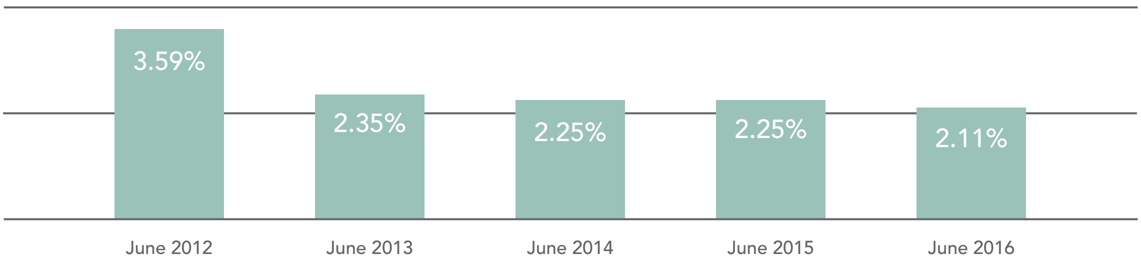
Profit and Loss (NZ$m)



Shareholder Equity (NZ$m)



Shareholder Funds / Total Assets (%)



CORPORATE GOVERNANCE

Corporate Governance Best Practice Code

LGFA supports the NZX Corporate Governance Best Practice Code. Although the company considers its governance practices have not materially differed from the NZX Code for the year-ended 30 June 2016, the specific areas where LGFA governance practices have differed from the NZX Code are as follows:

<table>
<tr><th>NZX Corporate Governance Best Practice Code</th><th>LGFA Governance Practice</th></tr>
<tr><td>An Issuer should formulate a code of ethics to govern its conduct (1.1)</td><td>LGFA requires high standards of conduct for directors and staff, the expectations of which are documented in:
• The Constitution of New Zealand Local Government Funding Agency Limited
• LGFA Board Charter
• Conflicts of Interest Policy
• Gifts and Entertainment Policy</td></tr>
<tr><td>An Issuer should establish a nomination committee to recommend Director appointments to the Board (3.11,3.12,3.13)</td><td rowspan="2">The process for the nomination and remuneration of directors is documented in the Constitution of New Zealand Local Government Funding Agency Limited and outlined in the section below.</td></tr>
<tr><td>An Issuer should establish remuneration committee to recommend a remuneration packages for Directors to shareholders (3.8,3.9,3.10).</td></tr>
</table>

Left: A floating platform to host a pumping structure capable of supplying 70 million litres of water daily to the Hamilton water treatment plant is lifted into the Waikato River for testing. Hamilton City Council.

This section sets out the Company's commitment to sound governance practices.

The LGFA governance structure comprises the LGFA shareholders, the LGFA Shareholders' Council and the LGFA Board of Directors.

LGFA Shareholders

LGFA has 31 Shareholders, comprising the New Zealand Government (20%) and thirty councils (80%).

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

LGFA Shareholders' Council

The LGFA Shareholders' Council comprises five to ten appointees from the Council Shareholders and the Crown. The role of the Shareholders' Council comprises the following:

- Review and report performance of LGFA and the Board;
- Recommendations to Shareholders as to the appointment, removal, replacement and remuneration of directors;
- Recommendations to Shareholders as to any changes to policies, or the Statement of Intent (SOI), requiring their approval;
- Update Shareholders on LGFA matters and to coordinate Shareholders on governance decisions.

As at the date of this Annual Report, the members of the LGFA Shareholders' Council are:

- Alan Adcock, Whangarei District Council, Chairman
- John Bishop, Auckland Council, Deputy Chairman
- David Bryant, Hamilton City Council
- Mohan De Mel, Tauranga City Council
- Mike Drummond, Tasman District Council
- Douglas Marshall, Selwyn District Council
- Brian McMillan, New Zealand Government
- Matt Potton, Western Bay of Plenty District Council
- Martin Read, Wellington City Council
- Mat Taylor, Bay of Plenty Regional Council

LGFA Board

LGFA Board Charter

The LGFA Board has adopted a Board Charter which describes the Board's role and responsibilities and regulates the Board's procedures. The Board Charter states that the role of the Board is to ensure the Company achieves the Company Goals. Having regard to its role the Board will direct, and supervise the management of, the business and affairs of the Company including, in particular:

- ensuring that the Company Goals are clearly established, and that strategies are in place for achieving them (such strategies being expected to originate, in the first instance, from Management);
- establishing policies for strengthening the performance of the Company;
- ensuring strategies are in place for meeting expectations set out in the current Statement of Intent and monitoring performance against those expectations, in particular the Company's primary objective of optimising the debt funding terms and conditions for participating local authorities;
- monitoring the performance of Management;
- appointing the CEO, setting the terms of the CEO's employment contract and, where necessary, terminating the CEO's employment with the Company;
- deciding on whatever steps are necessary to protect the Company's financial position and the ability to meet its debts and other obligations when they fall due, and ensuring that such steps are taken;
- ensuring that the Company's financial statements are true and fair and otherwise conform with law;
- ensuring that the Company adheres to high standards of ethics and corporate behaviour; and
- ensuring that the Company has appropriate risk management/regulatory compliance policies in place. In the normal course of events, day-to-day management of the Company will be in the hands of Management. The Board will satisfy itself that the Company is achieving the Company Goals; and engaging and communicating with Shareholders Council.

Conflicts of interest

The Company recognises impartiality and transparency in governance and administration are essential to maintaining the integrity of the LGFA. Accordingly, LGFA has formally adopted a conflicts of interest policy which provides guidance to employees and directors of the LGFA in relation to conflicts of interest and potential conflicts of interest, including specific guidence on the process for managing potential conflicts that may arise for non-independent directors. Directors and employees are expected to avoid all actions, relationships and other circumstances that may impact on their ability to exercise their professional duties.

Board composition

The LGFA Board must comprise between four and seven directors, the majority of which are required to be independent. An independent director is a director who, within five years prior to appointment, was not an employee of any shareholder, employee of a CCO owned by a shareholder, or a councillor of any local authority which is a shareholder.

The Directors of LGFA as at the date of this Annual Report are:

Craig Stobo. Independent Chair

BA (Hons) Economics. First Class, Otago

Craig has worked as a diplomat, economist, investment banker and Chief Executive Officer of BT Funds Management (NZ) Limited. He has completed the Advanced Management Programme at Wharton Business School in Philadelphia, authored reports to the New Zealand Government on the Taxation of Investment Income (which led to the PIE regime) and the creation of New Zealand as a funds domicile. He currently chairs Precinct Properties New Zealand Limited, AIG Insurance New Zealand Limited and Fliway Group Limited and is a director of Bureau Limited. He has private equity interests in financial services and other businesses. He was chair of the Establishment Board and acting Chief Executive of LGFA. He is chair of the Establishment Board of the Local Government Risk Agency.

John Avery. Independent Director

LLB, C.F.Inst.D

John was managing partner, then chairman of Hesketh Henry. He was a director of The Warehouse Group Limited, Signify Limited, several start-up businesses and an industry cooperative "ITM." He is currently an independent director of Fund Managers Auckland Limited, Regional Facilities Auckland Limited, Spider Tracks Limited and Strategic Pay Limited and a trustee of the New Zealand School of Dance.

Philip Cory-Wright. Independent Director

LLB (Hons), BCA Business Management, INFINZ (Cert), C.F.Inst.D

Philip is a solicitor of the High Court of New Zealand and Victoria. He has worked as a corporate finance adviser in New Zealand to the corporate sector on debt and equity matters for more than 25 years. He is currently a director of South Port New Zealand Limited and Matariki Forests Limited and strategic adviser to clients in the energy and infrastructure sectors. He was a member of the Local Government Infrastructure Expert Advisory Group tasked with advising the Minister of Local Government on improvements in local government infrastructure efficiency.

Abby Foote. Independent Director and Chair, Audit and Risk Committee

LLB (Hons), BCA Business Management, INFINZ (Cert), C.M.Inst.D

Abby is an experienced director of both publicly listed and Crown companies. Based in Christchurch, she has worked in a range of corporate, treasury and legal roles over the last 20 years. Abby is a director of a number of companies including The Museum of New Zealand Te Papa Tongarewa, Z Energy Limited, BNZ Life Insurance Limited and Livestock Improvement Corporation Limited.

Abby's previous directorships include Transpower New Zealand Limited and Diligent Corporation.

Linda Robertson. Independent Director

B.Com, Dip Banking, INFINZ (Fellow), C.F.Inst.D, GAICD

Linda is a professional Director with over 30 years experience in executive finance roles, having worked in the banking and energy sector in New Zealand. She is currently a director of Auckland Council Investments Limited, Dunedin City Holdings Limited, Dunedin City Treasury Limited, NZ Registry Services Limited, NZPM Group Limited, Crown Irrigation Investments Limited and King Country Energy Limited. Linda is also a member of the Audit & Risk Committee for the Ministry of Social Development, a member of the Treasury Advisory Committee of the New Zealand Export Credit Office and Chairman of the Audit and Risk Committee for Central Otago District Council. Her previous directorship roles include New Zealand Post Limited, Kiwibank Limited, the Earthquake Commission, Catalyst Risk Management Limited and Speirs Group Limited.

Right: Eva Street, Wellington. Upgrade to Eva Street Laneway. Wellington City Council.


Eva
Street

Mike Timmer. Non Independent Director

CA, BBS, BAgrSci, INFINZ (Cert), M.Inst.

Mike has worked for Citibank in its financial market section and held accountancy and treasury roles in the Health Sector and is presently Treasurer at the Greater Wellington Regional Council. He is Chairman of the Finance Committee of Physiotherapy New Zealand Incorporated and past Deputy Chair of the LGFA Shareholders' Council.

Nomination of Directors

Director nominations can only be made by a shareholder by written notice to the Company and Shareholders' Council, with not more than three months, nor less than two months before a meeting of shareholders. All valid nominations are required to be sent by the Company to all persons entitled to attend the meeting.

Retirement and re-election of Directors

Directors are appointed to the Board by an Ordinary Resolution of shareholders. At each Annual General Meeting, two directors must retire and, if desired, seek re-election. The directors who retire each year are one each of the independent and non-independent those, who have been longest in office since their last appointment or, if there are more than one of equal term, those determined by lot, unless the Board resolves otherwise.

Director tenure

Director	Originally appointed	Last reappointed/elected
Craig Stobo (Chair)	1 December 2011	19 November 2013
John Avery	1 December 2011	24 November 2015
Philip Cory-Wright	1 December 2011	1 December 2011
Abby Foote	1 December 2011	25 November 2014
Linda Robertson	24 November 2015	24 November 2015
Mike Timmer	24 November 2015	24 November 2015

Meetings of the Board

The table below shows attendances at Board, committee and strategy meetings by directors during the year ended 30 June 2016. In addition to the scheduled meetings, additional meetings are convened as necessary to consider specific issues.

Number of meetings	Board, including Strategy Day	Audit & Risk Committee
Craig Stobo	8/8	--
Paul Anderson	4/4	3/3
John Avery	8/8	2/2
Philip Cory-Wright	8/8	4/4
Abby Foote	8/8	4/4
Linda Robertson	4/4	1/1
Mike Timmer	4/4	1/1

Diversity

The Board does not have a formal policy on diversity. Appointments to the LGFA Board are made in accordance with the Constitution of New Zealand Local Government Funding Agency and the Shareholders Agreement dated 7 December 2011. As at balance date, the gender diversity of directors and officers is as follows:

	Female	Male
As at 30 June 2016*	2	5
As at 30 June 2015*	1	5

* For the purpose of this disclosure, Mark Butcher, Chief Executive, is deemed the sole officer of the company.

Remuneration

Board remuneration is determined by an Ordinary Resolution of shareholders. The current Board remuneration was approved by shareholder resolution at the 2015 Annual General Meeting on 24 November 2015.

Indemnities and insurance

Under the Company's constitution, LGFA has indemnified directors for potential liabilities and costs they may incur for acts of omission in their capacity as directors.

LGFA has arranged Directors' and Officers' liability insurance covering directors and management acting on behalf of the Company. Cover is for damages, judgements, fines, penalties, legal costs awarded and defence costs arising from wrongful acts committed while acting for the Company. The types of acts that are not covered are dishonest, fraudulent, malicious acts, or omissions, wilful breach of statute or regulation, or duty to the Company, improper use of information to the detriment of the Company, or breach of professional duty.

Audit and Risk Committee

The LGFA Audit and Risk Committee (ARC) is a committee of the Board.

The ARC is governed by an Audit and Risk Committee Charter, which states that the purpose of ARC is to provide advice, assurance and observations to the Board relating to the effectiveness and adequacy of internal control and risk management systems, processes and activities across the LGFA. It assists the Board to fulfil its duties by considering, reviewing, monitoring and approving:

- Risk management framework and processes;
- Internal control environment and mechanisms;
- Processes relating to the preparation and audit of financial statements of the LGFA;
- The integrity of performance information (including financial reporting);
- The governance framework and process;
- Policies, processes and activities to ensure compliance with legislation, policies and procedures; and
- Statutory/regulatory disclosure and reporting and performance against Statement of Intent targets.

ARC composition

ARC members are to be appointed by the Board. Membership will comprise at least three directors, the majority of whom must be independent. The members of the ARC as at the date of this Annual Report are:

- Abby Foote (Chair)
- Philip Cory-Wright
- Linda Robertson
- Mike Timmer

STATEMENT OF SERVICE PERFORMANCE

The decommissioning of the 250mm pipe from above Tempsky Road to Glover Road and reinstatement of pipe bridge. South Taranaki District Council.

Performance Against Objectives and Performance Targets

1 PRIMARY OBJECTIVES

LGFA operates with two primary objectives

1. Optimising the debt funding terms and conditions for participating local authorities.
2. LGFA will monitor the quality of the asset book so that it remains of a high standard by ensuring it understands each Participating Local Authority's financial position and the general issues confronting the Local Government sector.

1.1 **Optimising the debt funding terms and conditions for participating local authorities**

(i) Providing savings in annual interest costs for all participating local authorities

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

- LGFA aims to reduce its margin over New Zealand Government bonds (NZGBs)
- LGFA aims to minimise its margin over swap rates to provide cost effective funding to councils.

The LGFA margin to swap and NZGB will depend upon a number of factors including the relative demand and supply of high grade bonds, general credit market conditions, performance of NZGBs and swap rates, investor perceptions of LGFA and the issuance volume and tenor of LGFA bonds.

Given that LGFA tends to match fund its on-lending to councils, i.e. tends to issue bonds in the same tenor and volume as its on-lending, LGFA only has direct influence over investor perception amongst the above factors that determine LGFA spreads to NZGB and swap.

There will be periods within the interest rate and credit market cycles when LGFA bonds will outperform its benchmarks (spread narrowing) and there will be periods of time when LGFA bonds underperform (spread widening).

LGFA spreads to its benchmarks have consistently narrowed since it first began issuing bonds in February 2012, but these spreads have widened from the historic lows over the past twelve months.

Over the course of the twelve-month period to 30 June 2016:

- LGFA margins to NZGB widened by between 4 bps (2017s) and 35 bps (2027s)
- LGFA margins to swap widened by between 14 bps (2017s) and 39 bps (2027s)

These secondary market pricing movements are summarised in the following tables:

MARGINS – 15 December 2017	As at 30 June 2015 (bps)	As at 30 June 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	36	40	4
NZGB margin to swap	(29)	(19)	10
LGFA margin to swap	7	21	14

MARGINS – 15 MARCH 2019	As at 30 June 2015 (bps)	As at 30 June 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	44	54	10
NZGB margin to swap	(33)	(21)	12
LGFA margin to swap	11	33	22

MARGINS – 15 APRIL 2020	As at 30 June 2015 (bps)	As at 30 June 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	49	61	12
NZGB margin to swap	(34)	(23)	11
LGFA margin to swap	15	38	23

MARGINS – 15 MAY 2021	As at 30 June 2015 (bps)	As at 30 June 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	58	72	14
NZGB margin to swap	(42)	(29)	13
LGFA margin to swap	16	43	27

MARGINS – 15 APRIL 2023	As at 30 June 2015 (bps)	As at 30 June 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	67	89	22
NZGB margin to swap	(47)	(39)	8
LGFA margin to swap	20	50	30

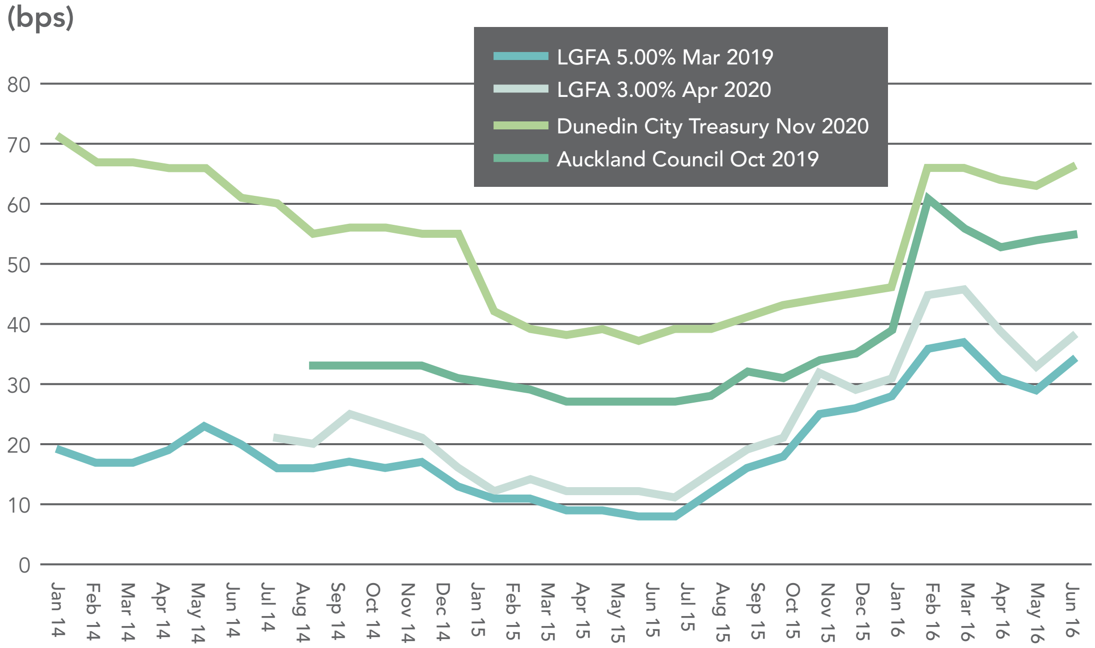
MARGINS – 15 APRIL 2027	As at 30 June 2015 (bps)	As at 30 June 2016 (bps)	Pricing movement
LGFA margin to NZ Government Bonds	71	106	35
NZGB margin to swap	(40)	(36)	4
LGFA margin to swap	31	70	39

The widening in our margin to swap and NZGB over the past twelve months has reversed the improvement in the 2014-15 year. Until July 2015, credit market conditions were strong and margins on LGFA bonds to NZGB or swap were at or near historic lows.

Over the past twelve months there have been a number of factors that have led to a widening in spreads for all non-government borrowers. Investors have been concerned over the global economic outlook, volatility arising from events such as BREXIT and managing investments in a low interest rate environment. As a result, there has been a reduction in risk sentiment and this has reduced demand for NZD investments and for bonds issued by non-government borrowers.

LGFA has delivered on increased borrowing cost savings for councils over the past year based upon our estimate of savings for AA-rated councils. We compare our secondary market spreads on LGFA bonds to those of Auckland Council and Dunedin City Treasury. The implied pricing advantage of LGFA is unchanged over the past year in the 2019 maturity but has improved by 4 bps in the 2021 maturity and 8 bps in the 2025 maturity. Both Auckland and Dunedin Councils have been active in borrowing over the past year in the domestic capital markets.

LGFA March 2019 and April 2020 secondary market credit margin over swap (bps)



Source PwC and LGFA

From the table below we estimate that as at 30 June 2016, LGFA was saving AA-rated councils between 17 bps for a 2019 (three-year) maturity and 33 bps for a 2025 (nine-year) maturity.

30 June 2016	Auckland 2019	Dunedin 2020	Dunedin 2021	Auckland 2022	Auckland 2025
AA-rated councils margin to swap	49	63	70	78	91
Less LGFA margin to swap	(33)	(38)	(43)	(47)	(57)
LGFA Gross Funding Advantage	16	25	27	31	34
Less LGFA Base Margin	(9)	(10)	(10)	(10.5)	(11)
LGFA Net Funding Advantage	7	15	17	20.5	23
Add 'LGFA Effect' *	10	10	10	10	10
Total Saving	**17 bps**	**25 bps**	**27 bps**	**30.5 bps**	**33 bps**

* *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.*

These costs savings for the sector have improved over the past twelve months as the margins on the higher-rated LGFA bonds have not widened as much as the single name council bonds. LGFA remains the cheapest source of borrowing for the sector as illustrated in the chart below which shows the widening borrowing cost for banks

LGFA March 2019 and May 2021 secondary market credit margin over swap and 5-year senior bank bonds credit swap (bps)

Source PwC and LGFA

(ii) **Making longer-term borrowings available to participating local authorities**

Over the past twelve months, LGFA issued bonds into three maturity dates in excess of six years:

- 15 April 2023 bond (six years). This maturity has comprised 22% of total issuance in the twelve-month period to 30 June 2016
- 15 April 2027 (ten years). This maturity comprised 37% of total issuance in the twelve-month period to 30 June 2016
- 15 April 2025 (eight years). In June 2016, LGFA commenced issuance of a 2025 bond.

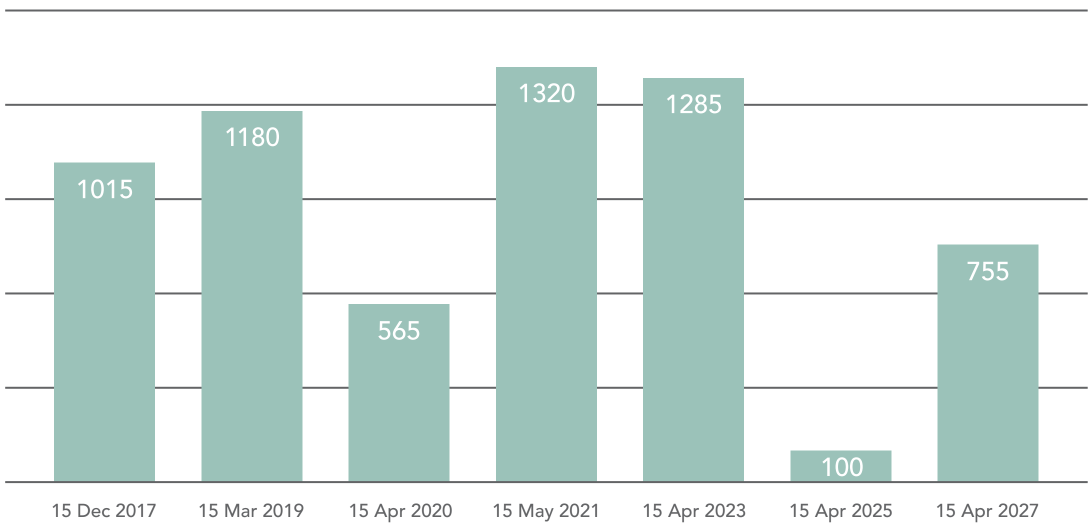
Over the twelve-month period to 30 June 2016, LGFA issued $1,265 million of debt with a weighted average maturity of 8.0 years. This is also similar to the average maturity for the 2014-15 year of 7.9 years. Nearly 67% of LGFA bond issuance for the twelve-month period was in the three longest dated maturities – 2023, 2025 and 2027.

2015-16 financial year issuance ($ milllion)

Mar 19	Apr 20	May 21	Apr 23	Apr 25	Apr 27	Total
$70 million	$200 million	$150 million	$275 million	$100 million	$470 million	$1265 million
5.5%	15.8%	11.9%	21.7%	7.9%	37.2%	100%

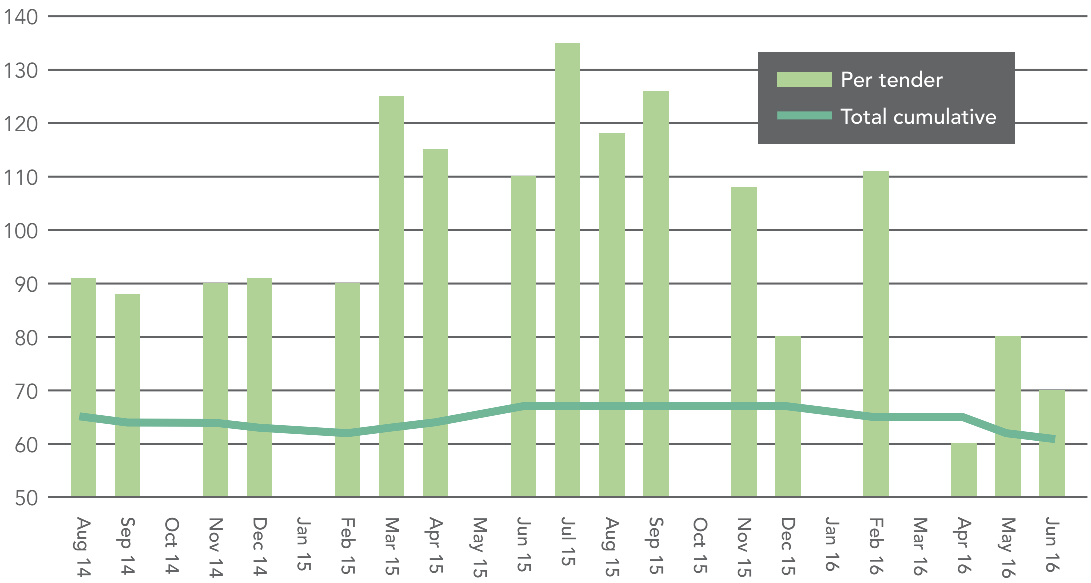
The following chart shows the total LGFA bond outstandings by maturity as at 30 June 2016.

LGFA bonds outstandings as at 30 June 2106



The following chart shows the average months to maturity for on-lending to councils at each tender, and the average months to maturity for all LGFA on-lending to councils as at each tender.

Average total months to maturity – On-lending to councils

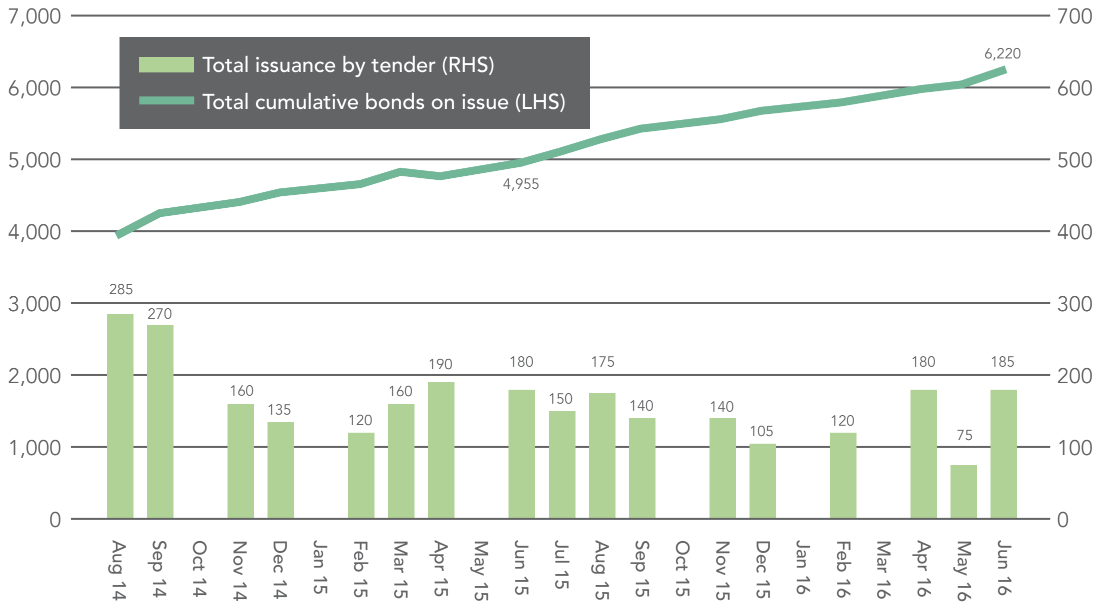


The average term of borrowing by councils from LGFA was 8.08 years for the twelve-month period to 30 June 2016. This is similar to the 8.12 years average term for the 2014-15 year.

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

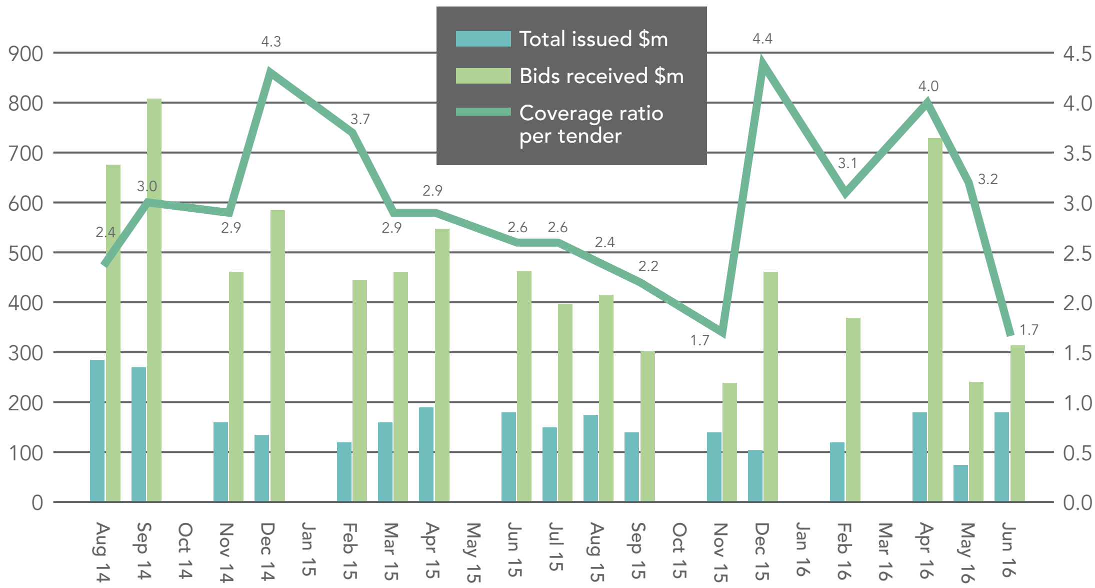
LGFA held nine tenders during the twelve-month period to 30 June 2016, with an average tender volume of $141 million. The volume offered at each tender ranged from $75 million to $180 million and all tenders were successful and fully subscribed. Total issuance during the twelve-month period of $1,265 million resulted in outstandings of LGFA bonds of $6,220 million as at 30 June 2016.

LGFA bond issuance by tender ($ million)



Over the twelve-month period, total bids received across the nine tenders was $3.466 billion for the $1.265 billion of LGFA bonds offered resulting in a coverage ratio of 2.7 times. The LGFA cover ratio for each tender over the past two years is shown in the following chart.

Tender bid/offer summary



While the coverage ratio for the past twelve months is lower than the average coverage ratio of 3.2 times since LGFA first commenced issuing in February 2012, this is not surprising given the longer duration of LGFA bonds being currently tendered, the smaller tranche sizes being offered, relatively tight spreads to both NZGB and swap and low outright yields. Furthermore, offshore investor demand for LGFA bonds has been noted in the secondary market rather than at LGFA tenders.

While LGFA issues fixed coupon debt to investors, councils were provided the choice of either fixed or floating rate borrowing for their borrowing from LGFA. Councils tend to borrow predominantly on a floating rate basis from LGFA.

Certainty of access for councils was improved with the commencement of bespoke lending in February 2015 and short-dated lending (less than one-year terms) in November 2015.

Bespoke lending allows councils to have flexibility in the tenor of their borrowing and the timing of their drawdown.

(iv) **Offering more flexible lending terms to participating local authorities**

The successful introduction of bespoke lending and short-dated lending has provided councils with flexible lending terms for any maturity from 30 days to 11 years.

- LGFA first offered bespoke lending in February 2015 where council borrowers could select their preferred borrowing maturity date and their preferred date of borrowing drawdown. In the twelve-month period to 30 June 2016 LGFA lent $407 million on a bespoke basis for 41 transactions. Total nominal bespoke lending outstanding as at 30 June 2016 was $486 million.
- LGFA first offered short-dated lending to councils in November 2015 and as at 30 June 2016 there were loans of $159 million outstanding to thirteen councils. Councils can now borrow out to 364 days where previously the shortest borrowing maturity was to December 2017

1.2 **LGFA will monitor the quality of the asset book so that it remains of a high standard by ensuring it understands each participating local authority's financial position and the general issues confronting the Local Government sector. This includes:**

(i) **LGFA will review each participating local authority's financial position, its financial head-room under LGFA policies and visit each Participating Local Authority on an annual basis;**

LGFA undertakes a detailed financial assessment on each of its borrowers and meets with all member councils on an annual basis while monitoring council performance throughout the year. LGFA reviews the Annual and Long Term Plans for each council and the annual financial statements. LGFA assigns an internal credit rating to each of its council members as part of the review exercise. All council members were compliant with LGFA covenants at June 2015.

(ii) **LGFA will commence work on analysing finances at the Council group level in addition to parent level. Previously the analysis was undertaken at the Council parent level**

LGFA reviews the financial position of each council on a Group basis where appropriate, e.g. where council services are delivered through subsidiaries or the council holds substantial investments in subsidiaries.

(iii) **LGFA will work closely with the Department of Internal Affairs (DIA), Office of the Auditor General (OAG) and Local Government New Zealand (LGNZ) on sector and individual council issues**

LGFA staff and directors have met with the OAG during the past twelve months and staff have met with DIA. LGFA presented at LGNZ quarterly media briefings during the year and authored the LGNZ report on local government sector finances in December 2015.

www.lgnz.co.nz/assets/LGNZ-Financial-Sector-Report.pdf

2 ADDITIONAL OBJECTIVES

LGFA has a number of additional objectives which complement the primary objectives. 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 (SOI)

The LGFA's policy is to pay a dividend that provides an annual rate of return to shareholders equal to LGFA cost of funds plus 2%.

On 20 September 2016, the directors of LGFA declared a dividend for the year to 30 June 2016 of $1,392,500.00 ($0.0557 per share). This is calculated on the LGFA cost of funds for the 2015-16 year of 3.57% plus the 2% margin.

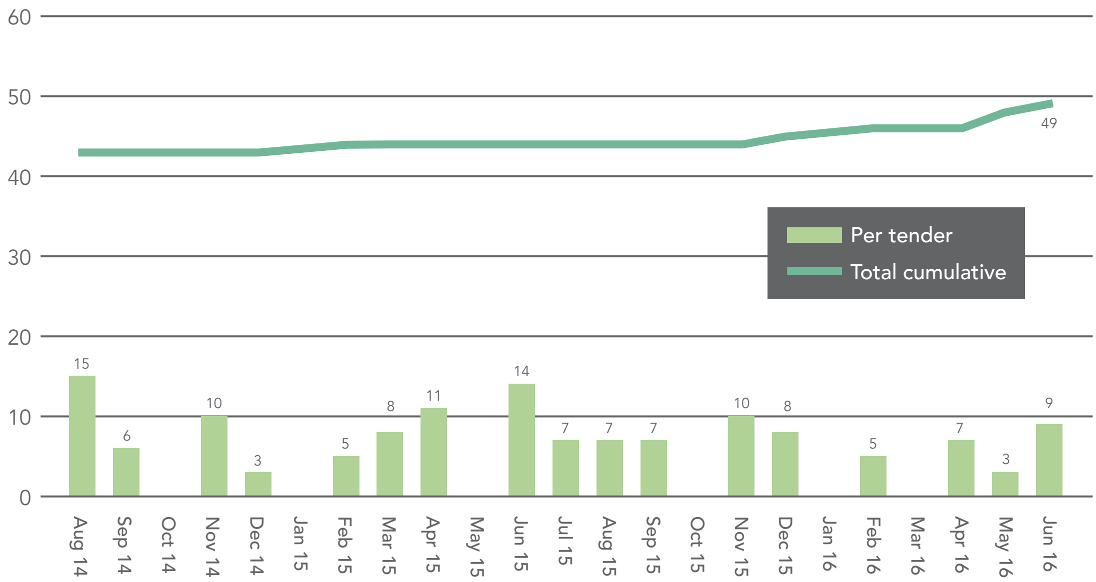
The impact from falling interest rates is that LGFA has a lower cost of funds than previous years. While council borrowers benefit from lower borrowing costs, the dividend payment, calculated on the above guidance, is lower than previous years.

2.2 Provide at least 50% of aggregate long-term debt funding for participating local authorities

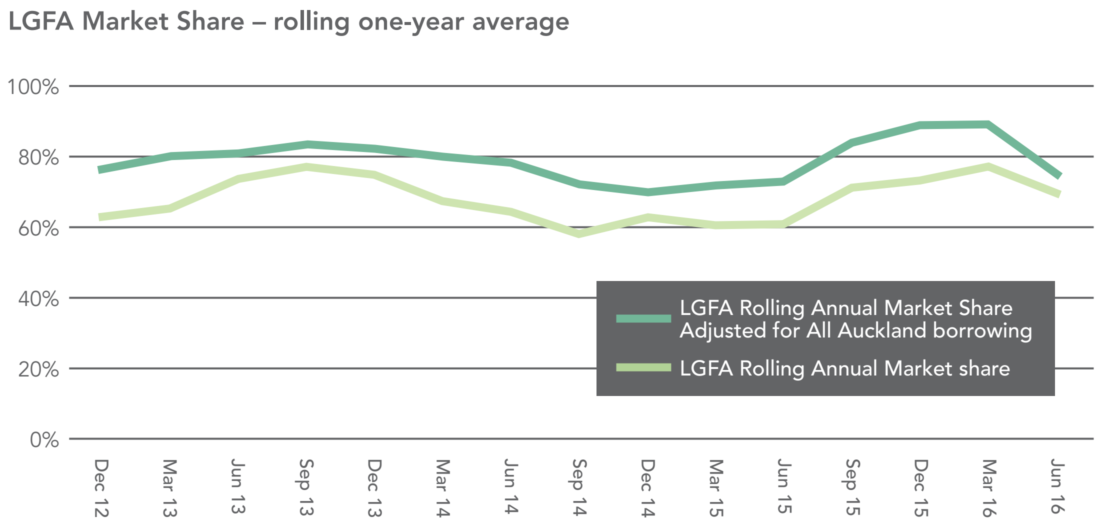
Five councils joined LGFA in the twelve-month period, Buller District Council as a borrower, Environment Canterbury as a borrower and guarantor, Gore District Council as a borrower, Kaipara District Council as a borrower and guarantor, and South Wairarapa District Council as a borrower, bringing the total number of council members to 50. Councils have strongly supported LGFA and by 30 June 2016, 49 participating councils have borrowed from LGFA.

The strong council support for LGFA is demonstrated in the following chart which shows the progression of council participation in each bond tender.

Participating councils



The following chart shows LGFA's share of new local government long-term debt issuance. Our share of long-term borrowing by the sector including non-members of LGFA was 70% for the twelve-month period to 30 June 2016. The market share is influenced by the amount of debt issued by the sector's largest borrower, Auckland Council in its own name in the domestic market. Auckland Council is required to issue debt under their own name as LGFA is restricted by its foundation policies to a maximum of 40% of total loans outstanding to Auckland. If Auckland Council's external borrowing is excluded from the data, then our estimated market share for the twelve-month period to 30 June 2016 was 75%.



Source PwC

2.3 **Ensure its products and services are delivered at a cost that does not exceed the forecast for issuance and operating expenses set out in section 4 of the Statement of Intent**

Issuance and Operating Expenses for the twelve-month period to June 2016 were $5.98 million compared to a full year SOI budget of $5.94 million.

Legal costs and expenses associated with the listing of LGFA bonds on the NZX debt markets, transition to the Financial Markets Conduct Act (FMCA), admitting five new member councils and the introduction of short-dated lending were higher than planned. These additional expenses are predominantly non-recurring and were offset by lower than forecast expenditure on Approved Issuer Levy (AIL), NZDMO facility fee and general operating expenses.

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

LGFA met with both S&P and Fitch rating agencies in September 2015 as part of their annual review process. S&P subsequently affirmed the long-term rating of LGFA at AA+ (stable outlook) on 10th November 2015 and Fitch affirmed the long-term rating as AA+ (positive outlook) on 13th November 2015.

Fitch subsequently lowered the rating outlook of LGFA from positive to stable on 1 February 2016 following the lowering of the New Zealand Government outlook from positive to stable.

Both the S&P and Fitch ratings are the same as, and are capped by, New Zealand's sovereign credit ratings. Fitch has defined LGFA as a credit-linked Public Sector Entity and our credit rating is now explicitly linked to the New Zealand Sovereign credit rating.

2.5 **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 twelve-month period to 30 June 2016 are:

In $ million	30 June 2016 Actual	30 June 2016 SOI
Net interest revenue	15.53	16.36
Issuance and operating expenses	(5.98)	(5.94)
Net Profit	9.55	10.42

Net interest revenue was $830k lower than the SOI due to lower than forecast interest rates reducing returns on investment assets, amortisation differences on transition from the NZDMO treasury system to the LGFA treasury management system and timing differences associated with bespoke lending.

Issuance and operating expenses were $40k greater than the SOI forecast due to higher than expected legal and NZX costs associated with listing the LGFA bonds on the NZX, transition to the FMCA, admitting five new member councils and larger take up of short-dated and bespoke lending than planned.

2.6 **Meet or exceed the Performance Targets outlined in section 5**

	Current performance targets	Target	Result for 12-month period to 30 June 2016	Outcome
1	Average cost of funds on debt issued relative to New Zealand Government Securities for the 12-month period[1]	≤0.50%	0.74%	No
2	Average base on-lending margin above LGFA's cost of funds	≤0.10%	0.106%	No
3	Annualised issuance and operating expenses[3]	≤$5.94 million	$5.98 million	No
4	Long-term lending to participating councils	≥$5,885 million	$6,241 million	Yes

1. The average cost of funds of all issuance for the twelve-month period ending 30 June 2016 relative to NZGS was 0.74%. This compares to a spread of 0.64% for the twelve-month period to 30 June 2015. The widening in the margin is due to a softening in credit market sentiment for non-government bonds and the disproportionate amount of longer dated bonds issued (which have a wider margin) over the past six months.
2. The margin is a function of duration of council borrowing as the current margin is 0.09% for council borrowing to March 2019, 0.10% from April 2020 to May 2021 and 0.11% for terms longer than April 2023. Given that councils have been borrowing for longer tenors, the average margin is above the average margin offered of 0.10%
3. As mentioned previously, expenses exceeded budget by $40k or 0.5% of the budget due to non-recurring legal expenses due to new lending products, new council members, NZX listing fees and transition to the FMCA.

2.7 **Comply with its Treasury Policy, as approved by the Board**

LGFA was compliant at all times with the Treasury Policy for the twelve-month period ending 30 June 2016.

FINANCIAL STATEMENTS

Wainui Hill Pukeatua Bridge – providing greater pedestrian access from the Eastern Hill and East Harbour Regional Park. Hutt City Council.

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 32 to 57:

- Comply with New Zealand generally accepting accounting practice and give a true and fair view of the financial position of the Company as at 30 June 2016, 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 positon 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, Director
20 September 2016

A. Foote, Director
20 September 2016

Statement of Comprehensive Income

For the year ended 30 June 2016 in $000s

	Note	Year Ended 2016	Year Ended 2015
Interest income from			
Cash and cash equivalents		1,153	1,472
Loans to local government		212,438	201,352
Marketable securities		3,333	283
Deposits		3,991	3,467
Derivatives		57,237	16,207
Fair value hedge ineffectiveness	2c	-	-
Total interest income		**278,152**	**222,781**
Interest expense on			
Bills		3,224	-
Bonds		256,247	205,908
Borrower notes		3,150	3,000
Total interest expense		**262,621**	**208,908**
Net interest income		**15,531**	**13,873**
Operating expenses			
Issuance and on-lending expenses	3	3,166	2,526
Operating expenses	4	2,820	2,143
Total expenses		**5,986**	**4,669**
Net operating profit		**9,545**	**9,204**
Total comprehensive income for the year		**9,545**	**9,204**

For the year ended 30 June 2016 in $000s

	Note	Share capital	Retained Earnings	Total equity
Equity as at 30 June 2014	10	25,000	3,848	28,848
Net operating profit			9,204	9,204
Total comprehensive income for the year			9,204	9,204
Transactions with owners				-
Dividend paid			(1,765)	(1,765)
Equity as at 30 June 2015	10	**25,000**	**11,287**	**36,287**
Net operating profit		-	9,545	9,545
Total comprehensive income for the year		-	9,545	9,545
Transactions with owners				
Dividend paid	10	-	(1,608)	(1,608)
Equity as at 30 June 2016		**25,000**	**19,224**	**44,224**

Statement of Financial Position

As at 30 June 2016 in $000s

	Note	2016	2015
Assets			
Financial assets			
Cash and bank balances		37,084	31,708
Trade and other receivables		-	38
Borrower notes receivable	13	800	-
Loans to local government	5	6,451,332	5,031,942
Marketable securities		139,339	5,345
Deposits		89,828	70,896
Derivatives in gain	2	537,379	270,503
Non-financial assets			
Prepayments		535	324
Other assets	12	955	1,081
Total assets		**7,257,252**	**5,411,838**
Equity			
Share capital		25,000	25,000
Retained earnings		19,224	11,287
Total equity		**44,224**	**36,287**
Liabilities			
Financial liabilities			
Trade and other payables		182	444
Loans to local government not yet advanced	13	50,000	-
Accrued expenses		593	344
Bills	6	223,916	-
Bonds	7	6,819,658	5,274,319
Borrower notes	8	108,415	85,120
Derivatives in loss	2	10,264	15,324
Total liabilities		**7,213,028**	**5,375,551**
Total equity and liabilities		**7,257,252**	**5,411,838**

For the year ended ended 30 June 2016 in $000s

	Note	Year Ended 2016	Year Ended 2015
Cash flow from operating activities			
Cash applied to loans to local government		(1,374,440)	(1,284,042)
Interest paid on bonds issued		(296,800)	(231,648)
Interest paid on bills issued		(3,224)	-
Interest paid on borrower notes		-	(292)
Interest paid on loans		(25)	-
Interest received from cash & cash equivalents		1,142	1,472
Interest received from loans to local government		218,821	195,923
Interest received from marketable securities		1,076	464
Interest received from deposits		4,059	3,114
Net interest on derivatives		89,718	44,657
Payments to suppliers and employees		(6,165)	(4,426)
Net cash flow from operating activities	9	**(1,365,838)**	**(1,274,778)**
Cash flow from investing activities			
Purchase of marketable securities		(133,068)	(5,525)
Purchase of deposits		(19,000)	(24,000)
Purchase of plant and equipment		125	(1,081)
Net cash flow from investing activities		**(151,943)**	**(30,606)**
Cash flow from financing activities			
Dividends paid		(1,608)	(1,765)
Cash proceeds from borrower notes		19,346	20,520
Cash proceeds from bonds issued		1,349,468	1,296,179
Cash proceeds from bills issued		223,916	-
Cash applied to derivatives		(67,964)	(32,968)
Net Cashflow from financing activities		**1,523,158**	**1,281,966**
Net (decrease) / increase in cash		**5,377**	**(23,418)**
Cash, cash equivalents and bank overdraft at beginning of year		31,708	55,126
Cash, cash equivalents and bank overdraft at end of year		**37,084**	**31,708**

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 8, City Chambers, 142 Featherston Street, Wellington Central, Wellington 6011.

The financial statements are as at and for the year ended 30 June 2016.

These financial statements were authorised for issue by the Directors on 20 September 2016.

B. STATEMENT OF COMPLIANCE

LGFA is an issuer in terms of the Financial Reporting Act 1993. The financial statements comply with the Financial Reporting Act 1993, in accordance with the transitional provisions under Section 55 of the Financial Reporting Act 2013 and Schedule 4 of the Financial Markets Conduct Act 2013.

LGFA is a profit orientated entity as defined under the New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS).

The financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice (NZ GAAP). They comply with NZ IFRS and other applicable Financial Reporting Standard, as appropriate for Tier 1 for-profit entities. The financial statements also comply with International Financial Reporting Standards (IFRS).

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

NZ IFRS 9: Financial Instruments. The first two phases of this new standard were approved by the Accounting Standards Review Board in November 2009 and November 2010. These phases address the issues of classification and measurement of financial assets and financial liabilities.

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:

- NZ IFRS 9: Financial Instruments (2014) – Effective for periods beginning on or after 1 January 2018. This standard aligns hedge accounting more closely with the risk management activities of the entity and adds requirements relating to the accounting for an entity's expected credit losses on its financial assets and commitments to extend credit.

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.

Intangible Assets

Intangible assets comprise software and project costs incurred for the implementation of the treasury management system. Capitalised computer software costs are amortised on a straight line basis over the estimated useful life of the software (3 to 7 years). Costs associated with maintaining computer software are recognised as expenses.

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.

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.

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.

2 Analysis of financial assets and financial liabilities

A. CATEGORIES OF FINANCIAL INSTRUMENTS

Derivative financial instruments are the only instrument recognised in the Statement of Financial position at fair value.

Derivative financial instruments are valued under level 2, 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 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.

Financial instruments recognised in the Statement of Financial Position at amortised cost

Fair values of financial instruments not recognised in the Statement of Financial Position at fair value are determined for note disclosure as follows:

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

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

Marketable securities and bonds

The fair value of bonds and marketable securities are determined using the quoted price for the instrument (Fair value hierarchy level 1).

Deposits

The fair value for deposits is determined using a discounted cash flow analysis. The interest rates used to discount the estimated cash flows are based on current market interest rates (Fair value hierarchy level 2).

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 (Fair value hierarchy level 2).

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 (Fair value hierarchy level 2).

Fair value of financial assets and financial liabilities

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 2016 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 balances	-	37,084	-	37,084
Trade and other receivables	-	-	-	
Loans to local government	-	6,451,332	-	6,692,415
Marketable securities	-	139,339	-	139,661
Deposits	-	89,828	-	90,016
Derivatives	-	-	537,379	537,379
		6,717,583	**527,115**	**7,496,555**
Financial liabilities				
Trade and other payables	182	-	-	182
Loans payable	50,000	-	-	50,000
Bills	223,916	-	-	223,898
Bonds	6,819,658	-	-	6,869,372
Borrower notes	107,615	-	-	108,044
Derivatives	-	-	10,264	10,264
	7,201,371	**-**	**10,264**	**7,261,760**

As at 30 June 2015 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 balances	-	31,708	-	31,708
Trade and other receivables	-	38	-	38
Loans to local government	-	5,031,942	-	5,163,921
Marketable securities	-	5,345	-	5,383
Deposits	-	70,896	-	70,986
Derivatives	-	-	270,503	270,503
	-	**5,139,929**	**270,503**	**5,542,539**
Financial liabilities				
Trade and other payables	(444)	-	-	(444)
Loans payable	-	-	-	-
Bonds	(5,274,319)	-	-	(5,379,311)
Borrower notes	(85,120)	-	-	(85,776)
Derivatives in loss	-	-	(15,324)	(15,324)
	5,359,883	**-**	**(15,324)**	**35,480,855**

B. 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.

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

As at 30 June 2016 in $000s	Face Value	Less than 6 Months	6 months - 1 Year	1-2 Years	2-5 Years	Over 5 Years
Financial Assets						
Cash and Bank Balances	37,084	37,084	-	-	-	-
Loans to Local Government	6,400,918	5,309,071	5,147	155,500	687,200	244,000
Marketable Securities	137,200	95,000	1,200	31,000	10,000	-
Deposits	89,000	89,000	-	-	-	-
Financial Liabilities						
Loans payable	(50,000)	(50,000)	-	-	-	-
Bills	(225,000)	(225,000)	-	-	-	-
Bonds	(6,220,000)	-	-	(1,015,000)	(3,065,000)	(2,140,000)
Borrower Notes	(99,059)	(81,672)	-	(2,488)	(10,995)	(3,904)
Derivatives	-	(5,114,200)	-	865,500	2,329,450	1,919,250
Total	**70,142**	**59,283**	**6,347**	**34,512**	**(49,345)**	**19,346**

As at 30 June 2015 in $000s	Face Value	Less than 6 Months	6 months - 1 Year	1-2 Years	2-5 Years	Over 5 Years
Financial Assets						
Cash and Bank Balances	31,708	31,708	-	-	-	-
Loans to Local Government	4,978,500	4,037,000	-	-	439,500	502,000
Marketable Securities	5,000	-	-	-	5,000	-
Deposits	70,000	70,000	-	-		
Financial Liabilities						
Loans payable	-	-	-	-	-	-
Bills	-	-	-	-	-	-
Bonds	(4,955,000)	-	-	-	(2,490,000)	(2,465,000)
Borrower Notes	(79,656)	(64,592)	-	-	(7,032)	(8,032)
Derivatives		(4,015,700)	-	-	2,045,450	1,970,250
Total	**50,552**	**58,416**	**-**	**-**	**(7,082)**	**(782)**

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.

For the period ending 30 June 2016 in $000s	2016		2015	
	100 bps increase $000s	100 bps decrease $000s	100 bps increase $000s	100 bps decrease $000s
Fair value sensitivity analysis				
Fixed rate assets			-	-
Fixed rate liabilities	260,219	(264,820)	188,425	(201,409)
Derivative financial instruments	(260,219)	264,820	(188,425)	201,409
	-	-	-	-
Cash flow sensitivity analysis				
Variable rate assets	51,295	(51,295)	40,370	(40,370)
Variable rate liabilities	(820)	820	(646)	646
Derivative financial instruments	(52,172)	52,172	(40,157)	40,157
	(1,697)	**1,697**	**(433)**	**433**

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.

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 2016 in $000s	NZ Government Agencies	NZ Local Authorities	NZ Registered Banks	Other counter-parties	Total carrying value
Financial assets					
Cash and bank balances	36,834	-	250	-	37,084
Trade and other receivables	-	-	-	-	-
Loans to local government	-	6,451,332	-	-	6,451,332
Marketable securities	26,644	-	70,039	42,657	139,339
Deposits	-	-	89,828	-	89,828
Derivatives	527,615	-	-	-	527,615
	591,093	**6,451,332**	**160,117**	**42,657**	**7,245,198**

As at 30 June 2015 in $000s	NZ Government Agencies	NZ Local Authorities	NZ Registered Banks	Other counter-parties	Total carrying value
Financial assets					
Cash and bank balances	31,078	-	630	-	31,708
Trade and other receivables	-	-	-	38	38
Loans to local government	-	5,031,942	-	-	5,031,942
Marketable securities	5,345	-	-	-	5,345
Deposits	-	-	70,896	-	70,896
Derivatives	270,503	-	-	-	270,503
	306,926	**5,031,942**	**71,526**	**38**	**5,410,432**

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 (NZDMO) also provide a committed liquidity facility that LGFA can draw upon to meet any exceptional and temporary liquidity shortfall. As at 30 June 2016, the undrawn committed liquidity facility was $400 million (2015: $400 million).

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 2016 in $000s	On demand	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total contractual cash flows	Total carrying value
Financial assets							
Cash and bank balances	37,084					37,084	37,084
Trade and other receivables						-	
Loans to local government		220,061	204,136	4,611,787	2,432,363	7,468,347	6,451,332
Marketable securities		86,608	11,824	42,957		141,389	139,339
Deposits		30,494	60,137			90,631	89,828
Financial liabilities							
Trade and other payables							
Loans payable		(50,000)				(50,000)	(50,000)
Bills		(150,000)	(75,000)			(225,000)	(223,916)
Bonds		(29,500)	(293,950)	(5,025,700)	(2,496,200)	(7,845,350)	(6,819,658)
Borrower notes				(76,719)	(45,234)	(121,953)	(108,415)
Derivatives		(13,051)	131,464	348,914	130,946	598,273	527,115
	36,834	**94,612**	**38,611**	**(98,761)**	**21,875**	**93,171**	**42,709**

As at 30 June 2015 in $000s	On demand	Up to 3 months	3 months to 1 year	1 year to 5 years	More than 5 years	Total contractual cash flows	Total carrying value
Financial assets							
Cash and bank balances	31,708	-	-	-	-	31,708	31,708
Trade and other receivables	-	38	-	-	-	38	38
Loans to local government	-	48,627	160,884	3,148,926	2,859,955	6,218,392	5,031,942
Marketable securities	-	-	300	5,450	-	5,750	5,345
Deposits	-	40,813	30,855	-	-	71,668	70,896
Financial liabilities							
Trade and other payables	-	(444)	-	-	-	(444)	(444)
Loans payable	-	-	-	-	-	-	-
Bills	-	-	-	-	-	-	-
Bonds	-	(27,750)	(238,175)	(3,345,950)	(2,791,625)	(6,403,500)	(5,274,319)
Borrower notes		-	-	(47,647)	(55,358)	(103,005)	(85,120)
Derivatives	-	(18,294)	86,213	185,705	25,604	279,228	255,180
	31,708	**42,990**	**40,078**	**(53,516)**	**38,575**	**99,835**	**35,227**

C. 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 year ended ended 30 June 2016 in $000s	2016 Gain/(loss)	2015 Gain/(loss)
Hedging instruments – interest rate swaps	236,449	178,578
Hedged items attributable to the hedged risk – fixed rate bonds	(236,449)	(178,578)
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.

D. OFFSETTING

NZ IAS 32: Financial Instruments Presentation allows financial assets and liabilities to be offset only when there is a current legally enforceable right to set off the amounts and there is an intention either to settle on a net basis, or to realise the asset and settle the liability simultaneously. LGFA does not offset any amounts. The following table shows amounts subject to an enforceable master netting arrangement or similar agreement that are not offset in the statement of financial position:

As at 30 June 2016 in $000s	Derivative assets	Derivative liabilities
Gross amounts	537,379	10,264
Amounts offset	-	-
Carrying amounts	537,379	10,264
Amounts that don't qualify for offsetting		
Financial Assets & liabilities	(10,264)	(10,264)
Collateral	-	-
Net Amount	**527,115**	**-**

As at 30 June 2015 in $000s	Derivative assets	Derivative liabilities
Gross amounts	270,503	15,324
Amounts offset		
Carrying amounts	270,503	15,324
Amounts that don't qualify for offsetting		
Financial Assets & liabilities	(15,324)	(15,324)
Collateral		
Net Amount	**255,179**	**-**

3 Issuance and on-lending expenses

Issuance and on-lending expenses are those costs that are incurred as a necessary expense to facilitate the ongoing issuance of LGFA debt securities.

For the year ended 30 June 2016 in $000s	2016	2015
NZDMO facility fee[1]	400	283
NZDMO processing fees	-	149
NZX	177	-
Rating agency fees	527	500
Legal fees for issuance	144	203
Regulatory, registry, other fees	52	23
Trustee fees	100	101
Approved issuer levy[2]	1,628	1,192
Promotion/roadshow	18	11
Information Services	120	64
	3,166	**2,526**

1. The increased cost for NZDMO facility fee followed a contractual price increase in February 2015.
2. The amount of Approved Issuer Levy is a function of the number of offshore holders of LGFA bonds.

4 Operating expenses

Operating expenses are all other expenses that are not classified as 'Issuance and on-lending expenses.'

For the year ended 30 June 2016 in $000s	2016	2015
Consultants[1]	164	95
Directors fees[2]	307	257
Insurance	61	63
Legal fees[3]	327	94
Other Expenses[1]	698	532
Auditors' Remuneration		
Statutory Audit	86	80
Personnel	1,163	998
Recruitment	14	24
	2,820	**2,143**

1. The key driver for increased costs for Consultants and Other Expenses are costs associated with the treasury management system implemented on 1 July 2015.
2. The number of directors increased from five to six in the 2015-16 year.
3. Legal expenses included legal costs associated with the listing on LGFA bonds on the NZX, transition to the Financial Markets Conduct Act and the introduction of short-dated lending to councils. These expenses are predominantly non-recurring.

5 Loans to local government

For the year ended 30 June 2016 in $000s	Face value	Unamortised Premium / (Discount)	Accrued Interest	Total
Ashburton District Council	25,125	705	(4)	25,825
Auckland Council	2,132,000	14,580	12,034	2,158,614
Buller District Council	20,000	-	2	20,002
Canterbury Regional Council	25,000	-	36	25,036
Christchurch City Council	1,266,889	2,909	5,048	1,274,846
Far North District Council	10,000	-	40	10,040
Gisborne District Council	22,000	-	30	22,030
Gore District Council	12,037	-	30	12,068
Greater Wellington Regional Council	255,000	-	660	255,660
Grey District Council	20,000	497	159	20,655
Hamilton City Council	230,000	-	663	230,663
Hastings District Council	50,000	-	175	50,175
Hauraki District Council	34,000	-	133	34,133
Horizons Regional Council	10,000	-	15	10,015
Horowhenua District Council	54,084	520	274	54,877
Hurunui District Council	17,000	-	69	17,069
Hutt City Council	79,000	210	501	79,711
Kaipara District Council	35,000	-	156	35,156
Kapiti Coast District Council	150,000	-	471	150,471
Manawatu District Council	51,000	(270)	305	51,035
Marlborough District Council	28,000	(104)	171	28,067
Masterton District Council	47,032	-	139	47,171
Matamata-Piako District Council	24,500	-	73	24,573
Nelson City Council	45,041	-	137	45,178
New Plymouth District Council	61,000	-	193	61,193
Opotiki District Council	5,000	168	42	5,210
Otorohanga District Council	9,000	171	75	9,246
Palmerston North City Council	77,000	-	295	77,295
Porirua City Council	33,500	-	103	33,603
Queenstown Lakes District Council	75,000	909	462	76,371
Rotorua District Council	98,700	437	888	100,025
Selwyn District Council	35,000	-	56	35,056
South Taranaki District Council	72,000	-	224	72,224
South Wairarapa District Council	7,500	-	36	7,536
Tararua District Council	9,000	-	33	9,033
Tasman District Council	90,000	-	314	90,314
Taupo District Council	125,000	-	431	125,431
Tauranga City Council	275,000	697	1,312	277,009
Thames-Coromandel District Council	35,000	-	69	35,069
Timaru District Council	60,876	30	155	61,062
Upper Hutt City Council	24,500	-	91	24,591
Waikato District Council	60,000	-	212	60,212
Waimakariri District Council	85,115	275	476	85,866
Waipa District Council	13,000	-	18	13,018
Wellington City Council	233,000	-	884	233,884
Western Bay of Plenty District Council	70,000	-	233	70,233
Whakatane District Council	31,019	-	72	31,091
Whanganui District Council	41,000	-	162	41,162
Whangarei District Council	132,000	38	488	132,526
	6,400,918	**21,771**	**28,643**	**6,451,332**

For the year ended 30 June 2015 in $000s	Face value	Unamortised Premium / (Discount)	Accrued Interest	Total
Ashburton District Council	15,000	829	113	15,941
Auckland Council	1,725,000	16,818	11,396	1,753,214
Buller District Council	-	-	-	-
Canterbury Regional Council	-	-	-	-
Christchurch City Council	932,500	3,219	5,463	941,183
Far North District Council	10,000	-	55	10,055
Gisborne District Council	17,000	-	51	17,051
Gore District Council	-	-	-	-
Greater Wellington Regional Council	155,000	-	741	155,741
Grey District Council	20,000	592	163	20,754
Hamilton City Council	225,000	-	771	225,771
Hastings District Council	50,000	-	204	50,204
Hauraki District Council	34,000	-	184	34,184
Horizons Regional Council	10,000	-	18	10,018
Horowhenua District Council	47,000	618	366	47,985
Hurunui District Council	12,000	-	67	12,067
Hutt City Council	49,000	281	401	49,682
Kaipara District Council	-	-	-	-
Kapiti Coast District Council	130,000	-	480	130,480
Manawatu District Council	41,000	27	303	41,330
Marlborough District Council	28,000	-129	175	28,046
Masterton District Council	40,000	-	194	40,194
Matamata-Piako District Council	24,500	-	98	24,598
Nelson City Council	25,000	-	150	25,150
New Plymouth District Council	56,000	-	221	56,221
Opotiki District Council	3,500	49	25	3,574
Otorohanga District Council	9,000	235	73	9,308
Palmerston North City Council	77,000	-	376	77,376
Porirua City Council	20,000	-	140	20,140
Queenstown Lakes District Council	60,000	1,096	444	61,539
Rotorua District Council	55,000	599	573	56,172
Selwyn District Council	35,000	-	66	35,066
South Taranaki District Council	62,000	-	234	62,234
South Wairarapa District Council	-	-	-	-
Tararua District Council	9,000	-	45	9,045
Tasman District Council	90,000	-	428	90,428
Taupo District Council	100,000	-	423	100,423
Tauranga City Council	215,000	525	1,062	216,587
Thames-Coromandel District Council	35,000	-	89	35,089
Timaru District Council	51,000	45	334	51,378
Upper Hutt City Council	18,000	-	72	18,072
Waikato District Council	50,000	-	215	50,215
Waimakariri District Council	55,000	324	409	55,733
Waipa District Council	13,000	-	22	13,022
Wellington City Council	138,000	-	712	138,712
Western Bay of Plenty District Council	70,000	-	127	70,127
Whakatane District Council	28,000	-	101	28,101
Whanganui District Council	41,000	-	182	41,182
Whangarei District Council	98,000	43	507	98,550
	4,978,500	**25,170**	**28,272**	**5,031,942**

6 Bills issued

As at 30 June 2016 in $000's	Face Value	Unamortised Premium	Accrued Interest	Total
13 July 2016	50,000	(42)	-	49,958
17 August 2016	50,000	(156)	-	49,844
14 September 2016	50,000	(238)	-	49,762
12 October 2016	25,000	(163)	-	24,837
16 November 2016	25,000	(219)	-	24,781
14 December 2016	25,000	(266)	-	24,734
	225,000	**(1,084)**	**-**	**223,916**

7 Bonds Issued

As at 30 June 2016 in $000's		Face Value	Unamortised Premium	Accrued Interest	Fair Value Hedge Adjustment	Total
15 December 2017	6% coupon	1,015,000	24,292	2,662		
15 March 2019	5% coupon	1,180,000	29,129	17,315		
15 April 2020	3% coupon	565,000	(18,322)	3,566		
15 May 2021	6% coupon	1,320,000	79,629	10,115		
15 April 2023	5.5% coupon	1,285,000	70,428	14,869		
15 April 2025	2.75% coupon	100,000	(3,157)	579		
15 April 2027	4.5% coupon	755,000	23,373	7,148		
Total		**6,220,000**	**205,372**	**56,254**	**338,032**	**6,819,658**

As at 30 June 2015 in $000's		Face Value	Unamortised Premium	Accrued Interest	Fair Value Hedge Adjustment	Total
15 December 2017	6% coupon	1,015,000	40,097	2,496		
15 March 2019	5% coupon	1,110,000	33,719	16,137		
15 April 2020	3% coupon	365,000	(21,839)	2,274		
15 May 2021	6% coupon	1,170,000	72,162	8,775		
15 April 2023	5.5% coupon	1,010,000	41,034	11,535		
15 April 2027	4.5% coupon	285,000	8,683	2,663		
		4,955,000	**173,856**	**43,880**	**101,583**	**5,274,319**

8 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 2016 in $000's	Face value	Accrued Interest	Total
Ashburton District Council	240	30	270
Auckland Council	34,112	3,118	37,230
Buller District Council	320	6	326
Canterbury Regional Council	400	5	405
Christchurch City Council	19,224	1,508	20,732
Far North District Council	160	17	177
Gisborne District Council	272	20	292
Gore District Council	96	1	97
Greater Wellington Regional Council	4,080	257	4,337
Grey District Council	320	38	358
Hamilton City Council	3,680	434	4,114
Hastings District Council	800	85	885
Hauraki District Council	544	43	587
Horizons Regional Council	160	16	176
Horowhenua District Council	752	81	833
Hurunui District Council	272	15	287
Hutt City Council	1,264	79	1,343
Kaipara District Council	560	3	563
Kapiti Coast District Council	2,400	236	2,636
Manawatu District Council	816	62	878
Marlborough District Council	448	38	486
Masterton District Council	704	75	779
Matamata-Piako District Council	392	37	429
Nelson City Council	560	38	598
New Plymouth District Council	976	94	1,070
Opotiki District Council	80	3	83
Otorohanga District Council	144	20	164
Palmerston North City Council	1,232	103	1,335
Porirua City Council	376	23	399
Queenstown Lakes District Council	1,200	119	1,319
Rotorua District Council	1,579	124	1,703
Selwyn District Council	560	86	646
South Taranaki District Council	992	86	1,078
South Wairarapa District Council	120	0	120
Tararua District Council	144	11	155
Tasman District Council	1,440	150	1,590
Taupo District Council	2,000	182	2,182
Tauranga City Council	4,400	394	4,794
Thames-Coromandel District Council	560	52	612
Timaru District Council	816	89	905
Upper Hutt City Council	392	21	413
Waikato District Council	960	76	1,036
Waimakariri District Council	1,200	71	1,271
Waipa District Council	208	21	229
Wellington City Council	3,728	216	3,944
Western Bay of Plenty District Council	1,120	107	1,227
Whakatane District Council	448	45	493
Whanganui District Council	656	55	711
Whangarei District Council	1,952	165	2,117
	99,859	**8,556**	**108,415**

As at 30 June 2015 in $000s	Face value	Accrued Interest	Total
Ashburton District Council	240	19	259
Auckland Council	27,600	1,999	29,599
Buller District Council	-	-	-
Canterbury Regional Council	-	-	-
Christchurch City Council	14,920	920	15,840
Far North District Council	160	12	172
Gisborne District Council	272	11	283
Gore District Council	-	-	-
Greater Wellington Regional Council	2,480	153	2,633
Grey District Council	320	24	344
Hamilton City Council	3,600	311	3,911
Hastings District Council	800	58	858
Hauraki District Council	544	26	570
Horizons Regional Council	160	11	171
Horowhenua District Council	752	50	802
Hurunui District Council	192	7	199
Hutt City Council	784	40	824
Kaipara District Council	-	-	-
Kapiti Coast District Council	2,080	161	2,241
Manawatu District Council	656	37	693
Marlborough District Council	448	19	467
Masterton District Council	640	51	691
Matamata-Piako District Council	392	25	417
Nelson City Council	400	22	422
New Plymouth District Council	896	61	957
Opotiki District Council	56	1	57
Otorohanga District Council	144	14	158
Palmerston North City Council	1,232	63	1,295
Porirua City Council	320	11	331
Queenstown Lakes District Council	960	74	1,034
Rotorua District Council	880	77	957
Selwyn District Council	560	66	626
South Taranaki District Council	992	53	1,045
South Wairarapa District Council	-	-	-
Tararua District Council	144	6	150
Tasman District Council	1,440	101	1,541
Taupo District Council	1,600	117	1,717
Tauranga City Council	3,440	259	3,699
Thames-Coromandel District Council	560	34	594
Timaru District Council	816	57	873
Upper Hutt City Council	288	11	299
Waikato District Council	800	49	849
Waimakariri District Council	880	30	910
Waipa District Council	208	15	223
Wellington City Council	2,208	115	2,323
Western Bay of Plenty District Council	1,120	126	1,246
Whakatane District Council	448	30	478
Whanganui District Council	656	34	690
Whangarei District Council	1,568	102	1,670
	79,656	**5,464**	**85,120**

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

For the year ended 30 June 2016 in $000's	2016	2015
Net profit/(loss) for the period	9,545	9,204
Cash applied to loans to local government	**(1,374,440)**	**(1,284,042)**
Non-cash adjustments		
Amortisation and depreciation	(756)	(185)
Working capital movements		
Net change in trade debtors and receivables	(224)	192
Net change in prepayments	(212)	(98)
Net change in accruals	248	151
Net Cash From Operating Activities	**(1,365,838)**	**(1,274,778)**

10 Share Capital

As at 30 June 2016 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 have a face value of $1 per share.

Shareholder Information

Registered holders of equity securities as at 30 June 2016.

	2016		2015	
New Zealand Government	5,000,000	11.1%	5,000,000	11.1%
Auckland Council	3,731,960	8.3%	3,731,960	8.3%
Christchurch City Council	3,731,960	8.3%	3,731,960	8.3%
Hamilton City Council	3,731,960	8.3%	3,731,960	8.3%
Bay of Plenty Regional Council	3,731,960	8.3%	3,731,960	8.3%
Greater Wellington Regional Council	3,731,960	8.3%	3,731,960	8.3%
Tasman District Council	3,731,960	8.3%	3,731,960	8.3%
Tauranga City Council	3,731,960	8.3%	3,731,960	8.3%
Wellington City Council	3,731,960	8.3%	3,731,960	8.3%
Western Bay of Plenty District Council	3,731,960	8.3%	3,731,960	8.3%
Whangarei District Council	1,492,784	3.3%	1,492,784	3.3%
Hastings District Council	746,392	1.7%	746,392	1.7%
Marlborough District Council	400,000	0.9%	400,000	0.9%
Selwyn District Council	373,196	0.8%	373,196	0.8%
Gisborne District Council	200,000	0.4%	200,000	0.4%
Hauraki District Council	200,000	0.4%	200,000	0.4%
Horowhenua District Council	200,000	0.4%	200,000	0.4%
Hutt City Council	200,000	0.4%	200,000	0.4%
Kapiti Coast District Council	200,000	0.4%	200,000	0.4%
Manawatu District Council	200,000	0.4%	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%	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%	200,000	0.4%
Waimakariri District Council	200,000	0.4%	200,000	0.4%
Waipa District Council	200,000	0.4%	200,000	0.4%
Whakatane District Council	200,000	0.4%	200,000	0.4%
Whanganui District Council	200,000	0.4%	200,000	0.4%
	45,000,000	**100%**	**45,000,000**	**100%**

Capital Management

LGFA's capital is equity, which comprises share capital and retained earnings. 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.

Dividend

During the year LGFA paid a dividend of $1,607,500 ($0.06826 per paid up share) on 15 October 2015. (2015: $1,765,000 ($0.0706 per paid up share).

11 Operating Leases

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

For the year ended 30 June 2016 in $000's	2016	2015
Less than one year	69	67
Between one and five years	89	133
Total non-cancellable operating leases	**158**	**200**

12 Other Assets

As at 30 June 2016 in $000s	2016	2015
Property, plant and equipment	43	46
Intangible Assets[1]	912	1,035
Total Other Assets	**955**	**1,081**

1. Intangible assets comprise acquired and internally developed software costs incurred for the implementation of LGFA's treasury management system.

13 Loans to local government not yet advanced

As at 30 June 2016, loans to local government totalling $50 million, and corresponding borrower notes for $800,000, had been contractually agreed for forward settlement in July 2016.

14 Capital Commitments

As at 30 June 2016, there are no capital commitments.

15 Contingencies

There are no material contingent liabilities at balance date.

16 Related parties

Identity of related parties

The Company is related to the local authorities set out in the Shareholder Information in note 10.

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 8, and the interest expense on these is shown in the Statement of comprehensive income.

Transactions with key management personnel

Salaries $704,084 (2015: $563,231)

Fees paid to directors are disclosed in operating overheads in Note 4.

17 Subsequent events

Subsequent to balance date, LGFA has issued $215 million in bonds through two tenders.

Subsequent to balance date, on 20 September 2016, the Directors of LGFA declared a dividend of $1,392,500.00 ($0.0557) per paid up share

INDEPENDENT AUDITOR'S REPORT
TO THE SHAREHOLDERS OF
NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY LIMITED
REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS AND
PERFORMANCE INFORMATION FOR THE YEAR ENDED 30 JUNE 2016.

The Auditor-General is the auditor of New Zealand Local Government 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 the performance information of the company on her behalf.

Opinion on the financial statements and the performance information

We have audited:

- the financial statements of the company on pages 32 to 57, that comprise the statement of financial position as at 30 June 2016, 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 performance information of the company on pages 18 to 27.

In our opinion:

- the financial statements of the company:
  - present fairly, in all material respects:
    - its financial position as at 30 June 2016; and
    - its financial performance and cash flows for the year then ended; and
  - comply with generally accepted accounting practice in New Zealand in accordance with New Zealand equivalents to International Financial Reporting Standards.
- the performance information of the company presents fairly, in all material respects, the company's actual performance compared against the performance targets and other measures by which performance was judged in relation to the company's objectives for the year ended 30 June 2016.

Our audit was completed on 20 September 2016. 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 the performance information are free from material misstatement.

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

An audit involves carrying out procedures to obtain audit evidence about the amounts and disclosures in the financial statements and in the performance information. The procedures selected depend on our judgement, including our assessment of risks of material misstatement of the financial statements and the performance information, 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 performance information in order to design audit procedures that are

KPMG

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 appropriateness of the reported performance information within the company's framework for reporting performance;
- the adequacy of the disclosures in the financial statements and in the performance information; and
- the overall presentation of the financial statements and the performance information.

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

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 the preparation and fair presentation of financial statements for the company that comply with generally accepted accounting practice in New Zealand. The Board of Directors is also responsible for preparation of the performance information for the company.

The Board of Directors' responsibilities arise from the Local Government Act 2002 and the Financial Markets Conduct Act 2013.

The Board of Directors is responsible for such internal control as it determines is necessary to enable the preparation of financial statements and performance information 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 the performance information, whether in printed or electronic form.

Responsibilities of the Auditor

We are responsible for expressing an independent opinion on the financial statements and the performance information and reporting that opinion to you based on our audit. Our responsibility arises from the Public Audit Act 2001.

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, we have no relationship with or interests in the company.

G Edwards

Graeme Edwards

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

Credit Rating

As at 30 June 2016, LGFA has the following credit ratings:

Rating Agency	Local currency		Foreign currency	
	Long term	Short term	Long term	Short term
Standard & Poors	AA+	A-1+	AA	A-1+
Fitch	AA+	F1+	AA	F1+

Board of Directors

INTERESTS REGISTER

Name of Director	Nature and extent of interest	
Craig Stobo	**Director** Precinct Properties New Zealand Limited Elevation Capital Management Limited Saturn Portfolio Management Limited Stobo Group Limited AIG Insurance NZ Limited Fliway Group Limited Bureau Limited	**General disclosure** Chair, Establishment Board, Local Government Risk Agency
John Avery	**Director** Spider Tracks Limited Fund Managers Auckland Limited Regional Facilities Auckland Limited Strategic Pay Limited Strategic Pay Trustee Service Limited	**General disclosure** The New Zealand School of Dance (Trustee) Stinger Trust (Trustee)
Philip Cory-Wright	**Director** South Port New Zealand Limited Matariki Forests Limited	
Abby Foote*	**Director** Z Energy Limited BNZ Life Insurance Limited Livestock Improvement Corporation Limited	
Linda Robertson	**Director** RML Consulting Limited Dunedin City Holdings Limited Dunedin City Treasury Limited King Country Energy Limited NZ Registry Services Limited NZPM Group Limited Auckland Council Investments Limited Crown Irrigation Investments Limited	**General disclosure** Audit and Risk Committee, Ministry of Social Development Technical Advisory Committee, NZ Export Credit Office Chair, Audit and Risk Committee, Central Otago District Council
Mike Timmer		**General disclosure** Officer, Greater Wellington Regional Council Chairman of Finance Committee, Physiotherapy New Zealand

* Subsequent to balance date: Director, The Museum of New Zealand Te Papa Tongarewa

DIRECTOR REMUNERATION

Director	2016($)
Craig Stobo	$84,000
Paul Anderson*	$19,833
John Avery	$47,600
Philip Cory-Wright	$47,600
Abby Foote	$50,400
Mike Timmer**	$28,692
Linda Robertson**	$28,692
Total	$306,817

* Resigned during year.
** Commenced during year.

STAFF REMUNERATION

Total remuneration	2016
$100,000 to $109,999	1
$190,000 to $199,999	1
$240,000 to $249,999	1
$450,000 to $459,999	1
Total staff receiving $100,000 or more	4

DONATIONS

No donations were made by LGFA during the year ended 30 June 2016.

WAIVERS FROM NZX LIMITED (NZX)

LGFA's fixed rate bonds are quoted on the NZX Debt Market (**LGFA Bonds**). NZX has granted LGFA a number of waivers from the NZX Listing Rules.

Waiver from Rule 3.2.1

NZX has granted LGFA a waiver from NZX Listing Rule 3.2.1(a) to the extent that this requires the trust deed under which the LGFA Bonds are issued (**Trust Deed**) to provide that the appointment of a new trustee is to be approved by an extraordinary resolution of the holders of the Securities to which the Trust Deed relates. Effective from 10 May 2016, LGFA ceased to rely on this waiver as the Trust Deed was amended to comply with NZX Listing Rule 3.2.1(a).

Waiver from Rule 5.2.3

NZX has granted LGFA a waiver from NZX Listing Rule 5.2.3 to the extent that this requires the LGFA Bonds to be held by at least 100 members of the public holding at least 25% of the number of securities of that class issued.

The waiver from NZX Listing Rule 5.2.3 was provided on the conditions that:

a. LGFA clearly and prominently disclose the waiver, its conditions and its implications in its annual reports and in each profile or offering Document for the LGFA Bonds;
b. LGFA will disclose market liquidity as a risk in each offering document (excluding any offering document referred to in paragraph (f) of the definition of "Offering Document" under NZX Listing Rule 1.6.1) for the LGFA Bonds; and
c. the nature of LGFA's business and operations do not materially change from its business and operations as at the date of the waiver decision.

The effect of the waiver is that the LGFA Bonds may not be widely held and there may be reduced market liquidity in the LGFA Bonds.

Waiver from Rule 6.3.2

NZX has granted LGFA a waiver from NZX Listing Rule 6.3.2 so that the deemed date of receipt of notices for a holder of LGFA Bonds who has supplied LGFA with an address outside of New Zealand, will be five working days after that notice is posted to that physical address.

NET TANGIBLE ASSETS

Net tangible asset per $1,000 of listed bonds as at 30 June 2016 is $1.17 (2015: $1.09)

EARNINGS PER SECURITY

$1.53 (2015: $1.85)

AMOUNT PER SECURITY OF FINAL DIVIDENDS

Not applicable

SPREAD OF QUOTED SECURITY HOLDERS

Spread of bondholders (LGF010, LGF020, LGF030, LGF040, LGF050, LGF060 and LGF070) as at 31 August 2016

Nominal Holding Range	Holder Count	Nominal Holding Quantity	Holding Quantity %
10,000 to 50,000	659	16,774,000	0.3%
50,001 to 100,000	154	11,357,000	0.2%
100,001 to 500,000	234	54,341,000	0.8%
500,001 to 1,000,000	37	28,546,000	0.4%
Over 1,000,000	175	6,323,982,000	98.3%
Total	1,259	6,435,000,000	100.0%

LGFA Board of Directors. From left. Craig Stobo (Chair), John Avery, Abby Foote, Mike Timmer, Linda Robertson, Philip Cory-Wright.

LGFA Staff. From left. Koshick Ranchhod, Louise Mckenzie, Andrew Michl, Jane Phelan, Mark Butcher (Chief Executive), Neil Bain.

Directory

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Street address

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Website

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Follow us twitter.com/nzlgfa

Right: Ashley Bridge (Cones Road, Rangiora) – midway through construction. December 2014. Waimakiriri District Council. Photo: Aaron Campbell.

Back cover: Walter Nash Centre – opened October 2015. The centre comprises five indoor courts, meeting rooms, the Taita Library and a fitness suite. Hutt City Council.

LGFA

NEW ZEALAND
LOCAL GOVERNMENT
FUNDING AGENCY