Financing New Zealand councils' infrastructure investment

Te tuku pūtea ki te haumitanga hanganga kaunihera o Aotearoa

Annual report

30 June 2020

LGFA NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY

TE PŪTEA KĀWANATANGA Ā-ROHE

Mā te huruhuru ka rere te manu is a traditional saying literally meaning ‘birds need feathers to fly’.

Its wider meaning is that ‘investment is needed for success’.

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Message from the Chair and Chief Executive

He karere mai i te Toihau me te Tumuaki

For the year ended 30 June 2020

"LGFA's robust business model was built by stakeholders who had experienced the severe funding challenges of the Global Financial Crisis. That prescience was rewarded by the performance of LGFA during the funding challenges resulting from COVID-19"

Craig Stobo, Board Chair

Mark Butcher, Chief Executive

We are pleased to record another period of strong financial and non-financial performance to 30 June 2020 and to highlight the following developments over the past year.

Strong Financial and Operational Performance

LGFA total interest income for the financial year of $370.2 million was a 2.5% increase over the 2018-19 financial year result of $361.1 million while net operating profit of $10.6 million for the financial year was a 5.2% decrease on the 2018-19 financial year result of $11.2 million.

While net interest income and net operating profit were lower than the previous year's result, they did exceed the Statement of Intent (SOI) forecasts due to the larger than expected growth in council loans. Lower profitability compared to the prior year was due to the lower level of interest rates reducing income on the Liquid Assets Portfolio and the refinancing by councils of their previous higher margin loans as they matured with lower margin loans.

Expenses have been managed under the SOI budget over the financial year. Lower fees from a reduced utilisation of the standby facility and lower Approved Issuer Levy (AIL) payments due to lower offshore investor holdings relative to forecast were positive. These savings were partially offset by higher legal and NZX costs associated with the record amount of LGFA bond issuance.

The financial strength of LGFA was affirmed by credit rating agencies S&P Global Ratings and Fitch Ratings who both maintained our credit rating at 'AA+' which, very importantly, is the same as the New Zealand Government. In January 2020, Fitch Ratings placed our long-term foreign currency rating on positive outlook while S&P Global Ratings retained the positive outlook on both our local and foreign currency ratings.

Borrowing activity

LGFA issued a record $3.31 billion of bonds over the financial year (including a net increase of $400 million of treasury stock) and outstandings now total $11.66 billion (including $800 million of treasury stock) across nine maturities from 2021 to 2033. The amount issued during the year was significantly more than the average historical issuance amount of $1.60 billion per financial year.

LGFA is the largest issuer of New Zealand dollar securities after the New Zealand Government and our bonds are amongst the largest and most liquid New Zealand dollar debt instruments available for investors. It is pleasing to note increased activity in the secondary market in our bonds.

The performance of LGFA bonds over the past year was also pleasing with LGFA bond spreads to NZGB tighter on all LGFA bond maturities. While LGFA bond spreads to swap were narrower in the 2020 to 2025 maturities, spreads were wider on the longer-dated LGFA bonds. Outright yields declined between 109 bps (1.09%) on the 2033 maturity and 120 bps (1.20%) on the 2024 maturity over the year.

Lending to the sector

LGFA was established in December 2011 to provide long-dated borrowing, certainty of access to markets and to reduce the borrowing costs for the local government sector. The original 31 shareholders, including the Crown, remain as shareholders. Over the past year, we added three new members with Taranaki Regional, Kaikoura District and Carterton District Councils joining. Total membership is now 67 councils, and this is expected to rise in the coming year.

Long-dated lending to councils over the 2019-20 year was $2.33 billion as councils refinanced their April 2020 loans and increased their borrowing to fund infrastructure projects. This was slightly less than the record amount of $2.45 billion in the prior year but our estimated market share of 85.7% remained high. The average tenor of long-dated borrowing by councils of 5.4 years over the 12-month period was shorter than the prior year's 6.0 years.

Short-dated lending for terms less than 12 months continues to be supported by councils and as at 30 June 2020, LGFA had $316 million of short-term loans outstanding to twenty-seven councils.

The changing world and sector outlook

The success of LGFA over the past eight years has been in part due to its ability to evolve and adapt to meet the needs of the local government sector. This has been apparent with the introduction of new products and the introduction of long-dated bond maturities allowing councils to undertake long-dated borrowing.

The sector is now considering its part in the COVID-19 economic recovery as well as responding to the Central Government proposal for the restructure of the three waters (drinking, waste and storm waters). These may have a medium-term impact on the sector but LGFA remains comfortable in its ability to assist the sector in meeting any changes as a result of these initiatives.

The impact from COVID-19 on the sector and LGFA

The local government sector has felt the impact from COVID-19. The move to level 4 lockdown in March resulted in the closure of community facilities and a corresponding loss of revenue from fees and charges. In addition, some councils experienced reduced income from their investments. A further impact will be felt in the 2020/21 financial year as some councils reduce planned rate increases in recognition of a growing level of hardship in their communities. Councils have responded by reducing non-essential operational expenditure while still maintaining core council services. Most councils have looked to retain their planned capital expenditure budgets over the 2020/21 financial year on the basis that this expenditure will play a part in their local economic recovery.

Additional support for the local authority sector has been provided by the Government through grant funding for both shovel-ready projects and the first stage of the three-waters reform. On-going grant funding from the Provincial Growth Fund will also assist a number of councils. This additional grant revenue from the government will be significant in helping councils in the delivery of their long term capital expenditure programmes as well as providing economic stimulus to local economies over the coming year.

The consequences of Covid-19 presented LGFA with challenges and opportunities. The overriding challenge was the announcements by the New Zealand Government on 17 March and 1 April that the bond programme for the 2019-20 financial year would rise from $10 billion to $13 billion and then to $29 billion respectively. This enormous shift had the effect of potentially 'crowding out' borrowers in NZ dollar debt markets including LGFA. Crucial price making by our banking intermediaries became erratic and market liquidity evaporated.

This meant our investors could not manage their portfolios; and LGFA faced the real prospect of being unable to issue bonds around the time of its April 2020 bond maturity. At the same time our council clients' demand for funding increased substantially as they faced revenue shortfall uncertainties. These pincered pressures meant LGFA faced the prospect of drawing down its Liquid Assets Portfolio to provide funding to Councils.

At a strategy day on 18 March, the Board approved the following actions to strengthen both the Company's capital and investor confidence:

- to increase the percentage of borrower notes that a council subscribes for when undertaking long term borrowing from LGFA from 1.6% to 2.5% of their borrowing
- to increase the on-lending margin to councils from 10 bps to 20bps
- to accelerate discussions with the Crown to extend and increase LGFA's $1 billion liquidity facility beyond its December 2021 expiry; and
- to commence discussions with the RBNZ to add LGFA bonds to its Large-Scale Asset Purchase (LSAP) programme.

LGFA successfully achieved all these objectives. Market liquidity returned, we syndicated a record $1.10 billion of a 2026 bond in mid-April following on from numerous investor conference calls to explain the COVID-19 impact on the sector and the response by LGFA. Councils received their required funding during this period and our Liquid Assets Portfolio increased to over $1 billion in size.

In addition, and throughout the year, LGFA sought to enhance secondary market liquidity through doubling the amount of treasury stock held by LGFA (available for stock lending) and increasing the soft cap on each on individual LGFA bond maturity to $1.75 billion.

We have also received stakeholder approval to undertake two significant changes in the past year. We have increased the Net Debt / Total Revenue covenant for councils with a long-term credit rating of 'A' equivalent or higher. This will assist councils with greater financial flexibility through the COVID-19 economic recovery phase as well as reflecting the strong financial position of the sector. We have also progressed work on LGFA being able to lend directly to a Council-Controlled Organisation (CCO) and we expect to undertake our first loan to a CCO by the end of the 2020 calendar year.

Global Reporting Initiative

Finally, this year's annual report is our first report prepared to meet the requirements of the Global Reporting Initiative (GRI) Standards (core option). The GRI Standards are the world's most widely used sustainability reporting standard.

Reporting on our material issues under the GRI framework expands environmental, social and governance (ESG) performance reporting with the aim of meeting the wider sustainability reporting expectations of stakeholders and will provide an opportunity for us to evolve our business strategy over time to create greater value for our stakeholders and society.

Acknowledgments

The Company's work cannot be implemented without the support of our staff, fellow directors, Shareholders Council, New Zealand Debt Management (NZDM) and the Reserve Bank of New Zealand, all whose efforts should be acknowledged. We believe the Company's future remains positive and look forward to working with all stakeholders in the year ahead.

Craig Stobo
Chair, LGFA Board

Chief Executive

LGFA Staff, from left: Mark Butcher, Ariadne Clarke, Neil Bain, Jane Phelan, Sumitha Kaluarachi, Andrew Michl, Koshick Ranchhod

LGFA Board of Directors, from left: John Avery, Linda Robertson, Craig Stobo, Anthony Quirk, Philip Cory-Wright, Mike Timmer

Performance highlights
Ko ngā tino hua

Bonds issued over the financial year (excluding treasury stock)

$2,905 million

Lending to councils over the financial year

$2,328 million

Total interest income

$370.2 million

▲ **2.5%** increase over the 2018-19 financial year

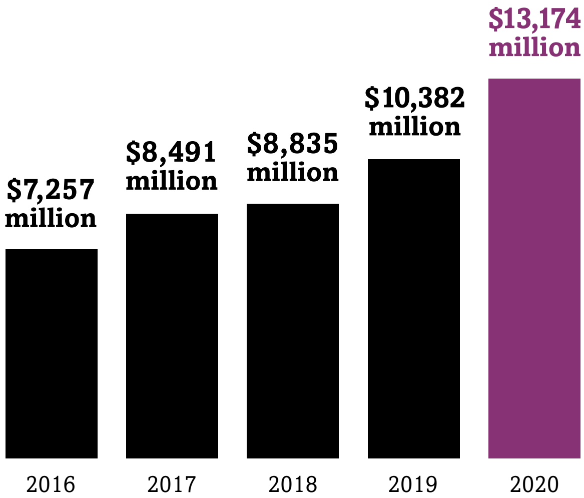
Net operating profit

$10.6 million

▼ **5.2%** decrease over the 2018-19 financial year

Total assets
30 June 2020

$13,174 million



Liquidity
30 June 2020

$166 million Cash

$589 million Marketable securities

$500 million Bank and term deposits

$800 million Treasury Stock for repo

$700 million Government committed liquidity facility
$1 billion total limit available

Shareholder funds
30 June 2020

$83.6 million

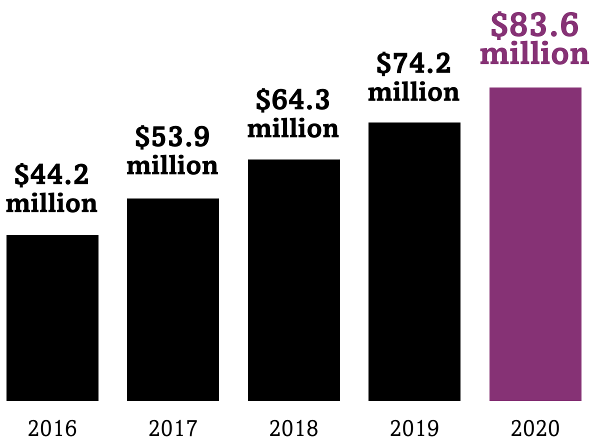
Fully paid shares
$25 million

Retained earnings
$58.6 million

Borrower notes
$182 million

Borrower notes are subordinated convertible debt instruments subscribed for by borrowing councils.

Shareholder equity



Performance against objectives

Ko ngā whakatutukinga ki ngā whāinga

The statement of service performance details LGFA's performance against the objectives and targets set out in the LGFA Statement of Intent 2019-20 (SOI)

2019-20 performance objectives.

The SOI set out two primary performance objectives and eight additional objectives for LGFA for the year ended 30 June 2020:

Primary Objectives

LGFA will operate with the primary objective of optimising the debt funding terms and conditions for Participating Local Authorities. Among other things this includes:

- Providing savings in annual interest costs for all Participating Local Authorities on a relative basis to other sources of financing;
- Offering short and long-term borrowings with flexible lending terms;
- Enhancing the certainty of access to debt markets for Participating Local Authorities, subject always to operating in accordance with sound business practice; and
- Being the debt funder of choice for New Zealand local government.

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:

- LGFA will review each Participating Local Authority's financial position, its financial headroom under LGFA policies and endeavour to visit each Participating Local Authority on an annual basis;
- Implement the changes to the Foundation Policies that were approved at the November 2018 AGM to allow for lending to CCOs. Changes to operational policies and practices need to ensure that no additional risk is borne by lenders, guarantors or the Crown; and
- LGFA will analyse finances at the Council group level where appropriate and report to shareholders as to which Participating Local Authorities are measured on a group basis.

LGFA will take a proactive role to enhance the financial strength and depth of the local government debt market and work with key central government and local government stakeholders on sector and individual council issues.

Additional objectives

LGFA has several additional objectives which complement the primary objectives. These objectives will be measurable and achievable and the performance of the company in achieving its objectives will be reported annually. These additional objectives are to:

- Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy;
- Provide at least 75% of aggregate long-term debt funding to the Local Government sector;
- Achieve the financial forecasts (excluding the impact of AIL) set out in section 4 of the SOI;
- 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 SOI;
- Take appropriate steps to ensure compliance with the Health and Safety at Work Act 2015;
- Maintain LGFA's credit rating equal to the New Zealand Government sovereign rating where both entities are rated by the same Rating Agency;
- Introduce CCO lending by December 2019 and report quarterly, the volume of lending to CCOs; and
- Comply with its Treasury Policy, as approved by the Board.

Performance against primary objectives

This section sets out LGFA's performance for the year ended 30 June 2020 against the two primary objectives set out in the 2019-20 SOI.

LGFA will operate with the primary objective of optimizing the debt funding terms and conditions for Participating Local Authorities. Among other things this includes:

1. **Providing savings in annual interest costs for all Participating Local Authorities on a relative basis to other sources of financing;**

LGFA lending base margins are 20 basis points (bps) for all borrowing terms between May 2021 and April 2033 following an increase of 10 bps in March. We had previously reduced margins in June 2018 but in March the LGFA Board increased these following its biennial Capital Structure Review. The base margin charge covers our operating costs and provides for our capital to grow in line with the growth in our balance sheet to maintain a satisfactory capital buffer. There is an additional credit margin added to the base margin depending upon whether a council has a credit rating or is a guarantor or not a guarantor.

Our estimated annual savings to councils are between -4 bps and 10 bps depending upon the term of borrowing. These estimates are based upon the secondary market levels at 30 June 2020 of LGFA bonds compared to bonds issued by Auckland and Dunedin councils. A cautious approach needs to be taken in drawing conclusions from the data as it is based upon an implied level in the secondary market and not on actual issuance costs. LGFA is a constant issuer of debt and the size of debt tranches are also an important factor eg. the Dunedin 2021 bond has $70 million on issue compared to $1.55 billion of the comparable LGFA bond. Borrowing margins of all issuers have narrowed over the past quarter but LGFA borrowing margins have moved less than other borrowers due to our large volume of issuance.

	Savings to AA rated councils (bps)			
As at 30 June 2020	Dunedin 2021	Auckland 2022	Auckland 2025	Dunedin 2026
AA rated councils margin to swap (bps)	36	33	56	75
Less LGFA margin to swap (bps)	(8)	(18)	(40)	(45)
LGFA gross funding margin advantage (bps)	28	15	16	30
Less LGFA base margin (bps)	(20)	(20)	(20)	(20)
Total savings (bps)	8	(5)	(4)	10

LGFA continues to borrow at very competitive spreads compared to the AAA rated sovereign/supranational/agency (SSA) issuers (who borrow in the New Zealand debt capital markets) and to the domestic banks.

As at 30 June 2020	Comparison to other borrowers – Secondary Market Spread to Swap (bps)									
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2033
LGFA (AA+)	9	18	25	32	40	45	48	-	57	57
Asian Development Bank (AAA)	15	-	29	37	42	47	-	-	-	-
Inter American Development Bank (AAA)	20	-	30	39	42	-	-	65	-	-
International Finance Corp (AAA)	15	-	31	39	-	-	49	-	-	-
KBN (AAA)	19	-	35	39	51	-	-	-	-	69
Rentenbank (AAA)	17	25	29	39	47	-	-	-	-	-
World Bank (AAA)	11	24	29	38	42	-	-	-	-	-
Nordic Investment Bank (AAA)	11	-	30	-	43	-	-	-	-	-
ANZ (AA-)	-	-	55	63	-	-	-	-	-	-
BNZ (AA-)	-	-	51	-	73	-	-	-	-	-
Westpac Bank (AA-)	-	44	53	66	72	-	-	-	-	-

2. Offering short and long-term borrowings with flexible lending terms

Councils can access flexible lending conditions by using LGFA's short-term lending and term lending products. Short-term lending is for loans between 30 days and 364 days while term lending is where councils can borrow for any term between one year and the longest-dated LGFA bond maturity on any drawdown date. Therefore, council members can borrow for terms ranging from 30 days to almost 13 years at any time they wish to draw down.

Over the 12-months ended 30 June 2020:

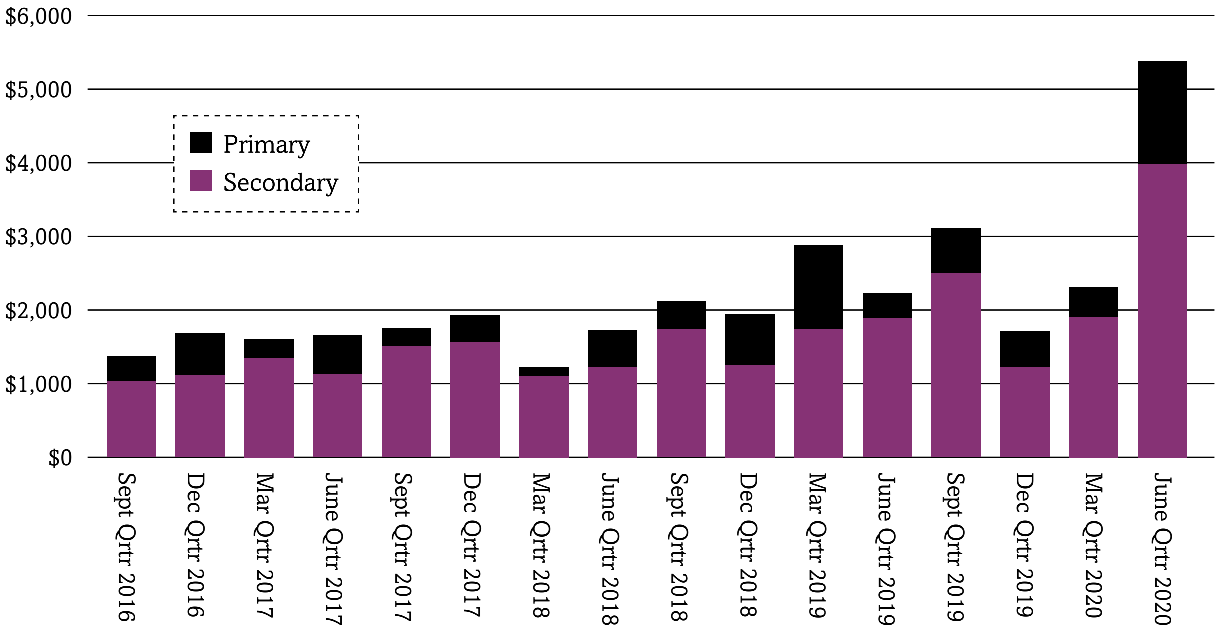
- 53 councils borrowed a total of $2.33 billion over 205 individual loans (excluding short-dated borrowing).
- The average borrowing term for the year was 5.4 years, compared with 6.0 for the previous 2018-19 year.
- 78% of term loans were issued on a floating rate basis, with the remaining 22% issued on a fixed rate basis.
- Short-term borrowing by councils has been well received with loan terms of between one and 12-months. As at 30 June 2020, there were $315.5 million of short-term loans outstanding to 27 councils.

3. Enhancing the certainty of access to debt markets for Participating Local Authorities, subject always to operating in accordance with sound business practice

LGFA issued a record $2.90 billion bonds over the 12-months to June 2020, with eight tenders and two syndications.

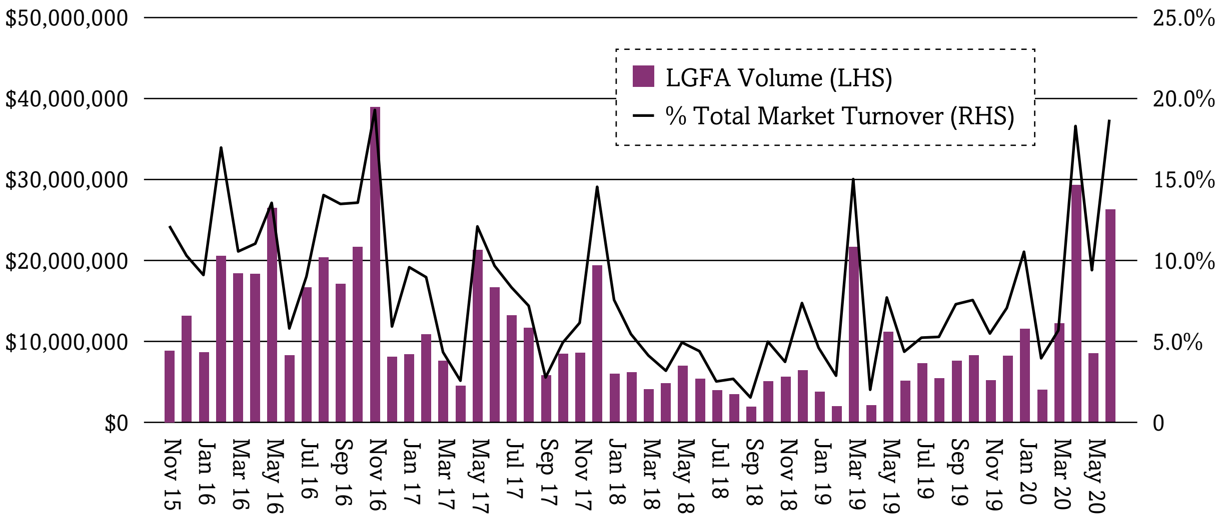
Activity in LGFA bonds in both the primary market (tender or syndicated issuance) and secondary market (between banks and investors) during the during the year totalled $12.54 billion, compared with $8.73 billion for the 2018-19 year. There was $2.91 billion of primary issuance and an estimated $9.63 billion of secondary market activity in LGFA bonds over the 12-months.

LGFA Primary and Secondary Market Activity (NZ$million)



LGFA bonds were listed on the NZX Debt Market in November 2015 and have averaged turnover of $11.1 million per month or 8.3% of the total turnover of the NZX Debt Market since listing. There was light turnover on the NZX over the year as retail investors were more attracted to high term deposit rates and higher-yielding bond issues by lower credit quality borrowers. There was an increase in volume over the second six-month period (averaging $15.3 million per month) due to the lack of retail bond primary issuance by corporate borrowers in NZD during this time period.

LGFA Turnover on NZX (monthly)

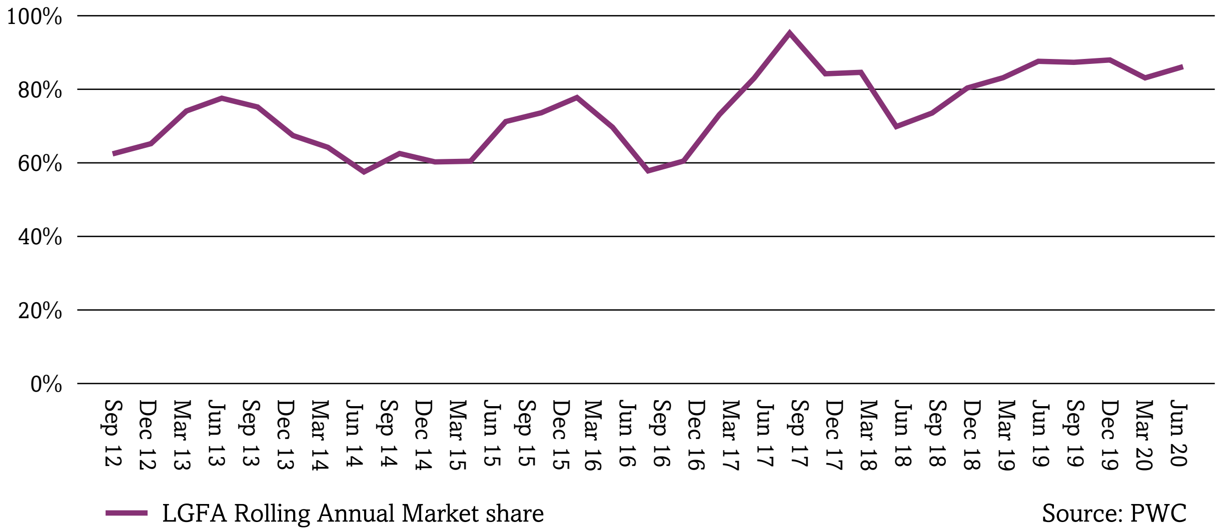


LGFA documented an Australian Medium-Term Notes Programme in November 2017 and refreshed the programme documents in March 2020. There is no immediate intention to use this programme, but it provides flexibility if there is a significant market disrupting event in the future.

4. Being the debt funder of choice for New Zealand local government

Our estimated market share of council borrowing for the rolling twelve-month period to 30 June 2020 was 86%, which compares favourably to the historical average since 2012 of 74%.

LGFA Market Share – rolling one year average



Source: PWC

We survey our council members each year and the latest stakeholder survey result in July 2019 was a 100% positive response to the question "How would you rate LGFA in adding value to your borrowing requirements?" We also received a 99% positive response to the question "How satisfied are you with the pricing that LGFA has provided to your Council?"

5. 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 headroom under LGFA policies and endeavour to visit each Participating Local Authority on an annual basis

Although travel restrictions due to the COVID-19 lockdown restricted our ability to meet with councils during the final quarter of the year, LGFA conducted 38 visits to 31 different councils over the 12-month period to June 2020 to discuss their financial performance and any developments with the underlying council operations.

By 30 November each year, member councils are required to complete an annual compliance certificate in relation to their 30 June financial statements.

Annual compliance certificates were completed by council members in 2019 and all councils were compliant with the financial covenants as at June 2019.

ii. Implement the changes to the Foundation Policies that were approved at the November 2018 AGM to allow for lending to Council Controlled Organisations (CCOs). Changes to operational policies and practices need to ensure that no additional risk is borne by lenders, guarantors or the Crown

Shareholders approved the changes to the Shareholder Agreement, Notes Subscription Agreement (NSA), Multi Issuer Deed (MID) and Guarantee and Indemnity Deed (GID) and Foundation Policies to allow for lending to CCOs and to offer standby facilities. The Borrower Notes percentage will also rise from 1.6% to 2.5% of a council's borrowings from July 2020 to assist with improving LGFA's capital position. It is planned to commence lending to CCOs and offer standby facilities in the 2020-21 year.

iii. LGFA will analyse finances at the Council group level where appropriate and report to the Shareholder Council and shareholders as to which Participating Local Authorities are measured on a group basis.

LGFA reviews council agendas and management reports on an ongoing basis for councils on the LGFA borrower watch-list. No council has yet to request to LGFA that they be measured on a group basis.

LGFA completed work on credit default assessment analysis of its member councils in conjunction with adopting IFRS9 for accounting purposes.

6. LGFA will take a proactive role to enhance the financial strength and depth of local government debt market and work with key central government and local government stakeholders on sector and individual council issues

Over the course of the year, LGFA management met with the Treasury, Reserve Bank of New Zealand, OECD and Department of Internal Affairs to discuss local government sector issues.

LGFA hosted its annual Shareholder Borrower Day in August 2019 and staff attended the LGNZ conference, Infrastructure NZ Building Nations Symposium and SOLGM Annual Summit.

LGFA continues to assist the sector and their advisers in finding ways for the Company to play a supporting role in providing solutions to off balance sheet financing for councils. We are currently providing technical input into the Cameron Partners Ratepayer Financing Scheme (RFS).

LGFA has been a member of the Department of Internal Affairs-led workstream on assessing the impact of COVID-19 on council finances.

A Special General Meeting (SGM) of shareholders on 30 June 2020 passed a resolution to relax the Net Debt / Total Revenue covenant within the Foundation Policies for those councils with a minimum credit rating of 'A'. Effective from 1 July 2020, the change was made to allow councils some additional financial flexibility in dealing with the COVID-19 crisis and to allow councils to co-invest alongside Central Government to pursue an infrastructure-led growth recovery response to the crisis. LGFA assessed the impact on guarantors to be negligible and consulted with stakeholders including investors, banks and credit rating agencies.

Performance against additional objectives

LGFA has eight performance objectives which complement the primary objectives. This section sets out LGFA's performance for the year ended 30 June 2020 against the additional objectives set out in the 2019-20 Statement of Intent.

7. Operate with a view to making a profit sufficient to pay a dividend in accordance with its stated Dividend Policy

LGFA's Net Operating Gain was $10.62 million for the financial year. The average cost of funds for the twelve-month period was 1.51%, which is lower than the 2.78% for the prior 2018-19 financial year due to the lower outright level of interest rates. The LGFA Board has the sole discretion to set the dividend.

8. Provide at least 75% of aggregate long-term debt funding for Participating Local Authorities

As noted earlier, our estimated market share of council borrowing for the rolling twelve-month period to 30 June 2020 was 86%. Our market share remains strong compared to our global peers.

As at 30 June 2020, there were 67 participating local authority members of LGFA, an increase of three from a year ago. We estimate a further five councils will become members in the next twelve months.

9. Achieve the financial forecasts (excluding the impact of AIL) set out in Section 4

For the 12-month period to 30 June 2020, Net Interest Income (NII) was $398k above budget while expenses were $209k below budget. Net Operating Gain of $10.62 million was $606k above budget. Included in the NII is the unrealised mark to market movement in fixed rate swaps that are not designated effective for hedge accounting purposes. We have used these swaps to reduce exposure to fixed rate loans made outside of the normal tender process and to reduce mismatches between time periods in our balance sheet. The unrealised loss increases as interest rates fall and the year-to-date revaluation is a loss of $1.3 million.

10. Ensure its products and services are delivered at a cost that does not exceed the forecast for issuance and operating expenses

Expenses for the 12-month period were $7.67 million which is $209k below budget. This variance is the consequence of:

- Issuance and on-lending costs (excluding AIL) at $2.575 million were $133k above SOI budget. A larger amount of bond issuance and short-term lending increased these costs relative to SOI budget, primarily in relation to higher NZX costs and legal costs. These were offset to some extent from lower fees than budgeted relating to the NZDMO facility.
- Operating costs at $3.685 million were $170k below budget due to lower IT, personnel, travel and general overhead costs, offset by slightly higher legal costs relative to SOI budget.
- Approved Issuer Levy (AIL) payments of $1.396 million were $172k below SOI budget. We pay AIL on behalf of offshore investors at the time of semi-annual coupon payment. During the twelve-month period, offshore investor holdings of LGFA bonds were less than forecast.

11. Take appropriate steps to ensure compliance with the Health and Safety at Work Act 2015

LGFA has a Health and Safety staff Committee which reports on a regular basis to the LGFA Board by the Risk and Compliance Manager. There were no Health and Safety incidents during the year. LGFA staff moved to work from home in late March as the country moved to Level 4 in the COVID-19 response and returned to offices under Level 1.

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

Standard and Poor's (S&P) and Fitch Ratings (Fitch) review LGFA's credit rating on an annual basis and formal review meetings were held in September 2019 with Fitch and in November 2019 with S&P.

On 18 November 2019, Fitch affirmed our long-term local currency credit rating as AA+ and classified LGFA as a corporate mission, government-related entity (GRE) under its GRE rating criteria. Fitch equalises our ratings with those of the New Zealand Government. On 28 January 2020 Fitch placed our foreign currency credit rating of AA on positive outlook. Fitch left the local currency credit rating unchanged at AA+ with a stable outlook.

On 28 February 2020, S&P affirmed LGFA's long-term local currency credit rating as AA+ and our long-term foreign currency credit rating of AA. Both ratings remained on positive outlook. Both credit ratings and outlook are the same as the New Zealand Government.

13. Introduce CCO lending by December 2019 and report quarterly, the volume of lending to CCOs to both the Shareholder Council and shareholders

Council members approved the amendments to the Shareholder Agreement, Notes Subscription Agreement (NSA), Multi Issuer Deed (MID), Guarantee and Indemnity Deed (GID) and Foundation Policies to allow for lending to CCOs on 6 July 2020. The approval process took longer than expected due to the need to have the changes to the documents approved by every council and by the response to COVID-19. We expect to undertake our first loan to a CCO in the 2020-21 fiscal year.

14. Comply with its Treasury Policy as approved by the Board

There were two compliance breaches of the Treasury Policy during the 12-month period ending 30 June 2020.

There was no financial loss to LGFA from either breach and reputational risk was assessed to be minimal.

There was full reporting on both breaches to the LGFA Board and Shareholders Council, and a formal review of both breaches was led by the Chair of the Audit and Risk Committee. LGFA management have reviewed controls that could be put in place to mitigate the risk of further breaches.

Performance targets

2019-20 performance targets	Target	Result for 12-month period to 30 June 2020	Outcome
Net interest income for the period to 30 June 2020	Greater than $17.9 million	$18.2 million	✓
Annual issuance and operating expenses (excluding AIL) for the period to 30 June 2020	Less than $6.30 million	$6.26 million	✓
Total lending to Participating Local Authorities at 30 June 2020	At least $9,792 million	$10,899 million	✓
Conduct an annual survey of councils who borrow from LGFA	Achieve at least an 80% satisfaction score for the value added by LGFA	100%	✓
Meet all lending requests from Participating Local Authorities, where those requests meet LGFA operational and covenant requirements			✓
Achieve 75% market share of all council borrowing in New Zealand		86%	✓
Review each Participating Local Authority's financial position, its headroom under LGFA policies and arrange to meet each Participating Local Authority at least annually			✗ Refer 5i, page 14
No breaches of Treasury Policy, any regulatory or legislative requirements including the Health and Safety at Work Act 2015			✗ Refer 14, page 16
Successfully refinance of existing loans to councils and LGFA bond maturities as they fall due			✓
Maintain a credit rating equal to the New Zealand Government rating where both entities are rated by the same credit rating agency			✓

About us
Mō mātou

Establishment

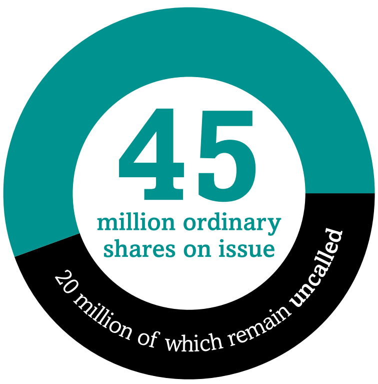
The New Zealand Local Government Funding Agency Ltd (LGFA) specialises in funding the New Zealand local government sector, the primary purpose being to provide more efficient funding costs and diversified funding sources for New Zealand local authorities. LGFA was established to raise debt on behalf of local authorities on terms that are more favourable to them than if they raised the debt directly.

Incorporated on 1 December 2011 under the Companies Act 1993

Enabled by Local Government Borrowing Act 2011

Council-controlled organisation under the Local Government Act 2002

Ownership



20%
New Zealand Government

80%
30 councils

Share ownership is restricted to New Zealand Government or councils.

Governance overview

20%
Shareholding
New Zealand Government

80%
Shareholding
30 councils

31 Shareholders

New Zealand Government shareholding will reduce to 11.1% if a future call is made on the uncalled capital of the 30 council shareholders.

Shareholders' Council
Page 49

The LGFA Shareholders' Council comprises five to ten appointees from the Council Shareholders and the New Zealand Government. The role of the Shareholders' Council is to:

Review and report performance of LGFA and the Board;

Recommend to Shareholders as to the **appointment, removal, replacement and remuneration of directors;**

Recommend to Shareholders as to any **changes to policies**, or the Statement of Intent (SOI), requiring their approval;

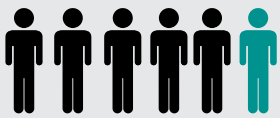
Update Shareholders on LGFA matters and to coordinate Shareholders on governance decisions.

LGFA Board
Page 41-49

The LGFA Board is responsible for the strategic direction and control of LGFA's activities. The Board guides and monitors the business and affairs of LGFA, in accordance with the:

- Local Government Act 2002;
- Local Government Borrowing Act 2011;
- Companies Act 1993;
- LGFA's Constitution;
- LGFA Shareholder Agreement;
- LGFA Annual Statement of Intent.

The Board comprises **five independent** and **one non-independent** directors appointed by shareholders.



Bonds listed on NZX Debt Market

Issue of securities to the public under the Financial Markets Conduct Act and regulated by Financial Markets Authority

Supervised by independent trustee

Guarantee structure

All shareholder councils are guarantors as well as councils with total borrowings over $20 million.

LGFA's securities obligations are guaranteed by council guarantors.

A council's obligations under the guarantee is secured against rates revenue

LGFA is not guaranteed by the New Zealand Government.

Credit rating as at 30 June 2020

Standard & Poor's

Domestic Currency

AA+

(Positive Outlook)

Foreign Currency AA

(Positive Outlook)

Fitch Ratings

Domestic Currency

AA+

(Stable Outlook)

Foreign Currency AA

(Positive Outlook)

These credit ratings are the same as the New Zealand Government ratings.

New Zealand Domestic Bond Deal of the Year

New Zealand Local Government Funding Agency
NZ$1 billion 2.25% April 2024

Joint lead managers: Bank of New Zealand
Westpac Banking Corporation New Zealand Branch

Our history

Dec 2011

- Incorporated December 2011
- Commenced bond issuance February 2012
- April 2015 and December 2017 bonds issued

June 2012

- KangaNews NZ Domestic Issuer of the Year – 2012
- March 2019 bond issued
- INFINZ award for Best Bond issue of 2012
- Inaugural LGFA Borrowers Forum

June 2013

- Inaugural dividend of $1.5m declared
- May 2021 and April 2023 bonds issued

June 2014

- April 2020 and April 2027 bonds issued
- Bespoke lending introduced
- Refinanced April 2015 bond ($240m) and council loans
- New Treasury Management System implemented
- Transitioned front/middle/back office from NZDMO

June 2015

- LGFA Bonds listed on NZX November 2015
- Commenced LGFA Bill issuance
- Commenced short-term lending to councils
- Transitioned to Financial Markets Conduct Act

June 2016

- Bond lending facility established October 2016
- April 2033 bond issued

June 2017

- Refinanced December 2017 bond ($1.015b) bond and council loans
- April 2022 bond issued
- First bond not matched to a New Zealand Government bond maturity

June 2018

- April 2024 bond issued via inaugural syndication ($1.0b)
- Refinanced March 2019 bond ($1.240b) and council loans

June 2019

- KangaNews NZ. NZ Domestic Bond Deal of the Year
- Refinanced April 2020 bond ($980m) and council loans
- April 2026 bond issued via syndication ($1.0b)
- Reserve Bank adds LGFA bonds to its Large Scale Asset Purchase programme. April 2020

June 2020

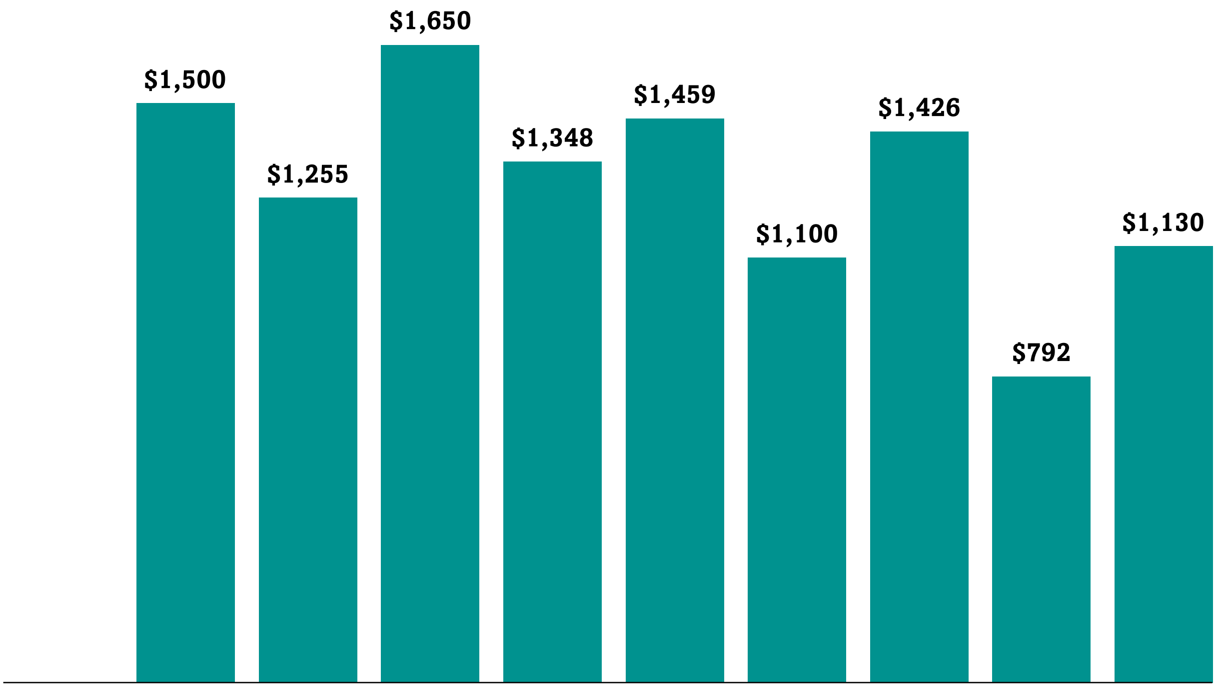
LGFA bonds on issue

Ko ngā pūtea taurewa pūmau kua tukuna e te LGFA

LGFA bonds on issue (NZ$ million, face value)

As 30 June 2020 : NZ$11,660 million

Includes NZ$800 million treasury stock



Maturity	May 2021	Apr 2022	Apr 2023	Apr 2024	Apr 2025	Apr 2026	Apr 2027	Apr 2029	Apr 2033
Coupon	6.00%	2.75%	5.50%	2.25%	2.75%	1.50%	4.50%	1.50%	3.50%
NZX Code	LGF040	LGF090	LGF050	LGF100	LGF070	LGF120	LGF060	LGF110	LGF080

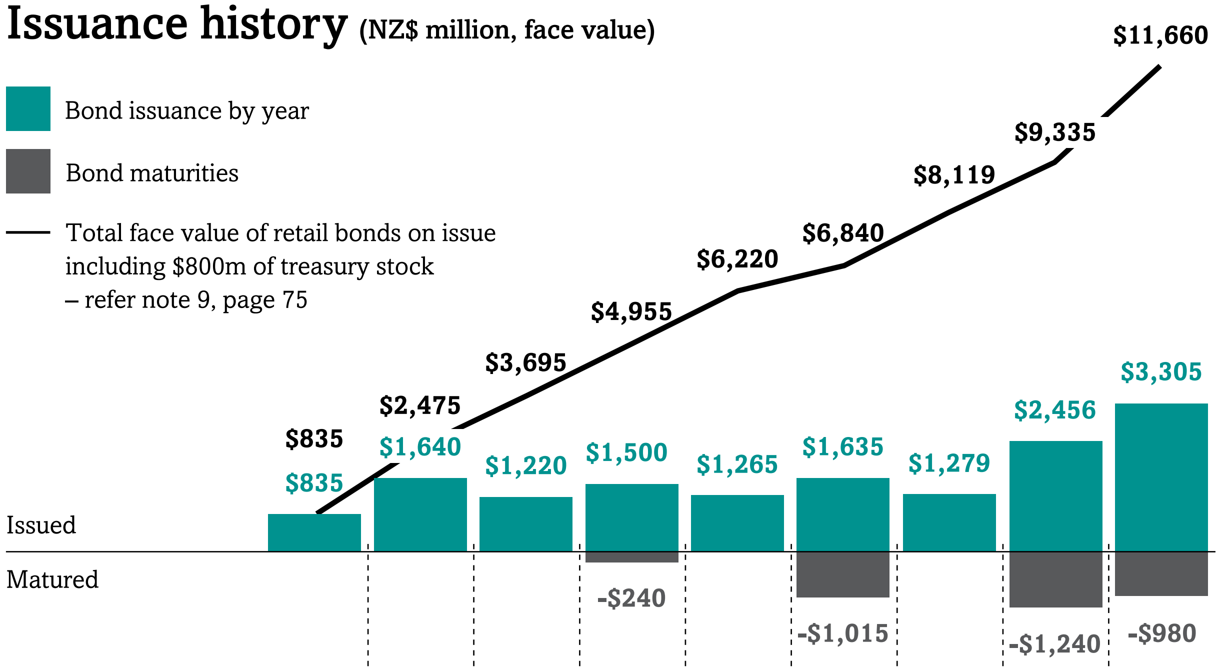
In addition to the retail bonds listed on the NZDX, LGFA have $130 million of Wholesale Floating Rate Notes on issue.

LGFA bond issuance

LGFA typically issues a new bond maturity via an initial syndication and then through ongoing regular scheduled tenders.

- Preferred bond tender sizes are between NZ$150 million to NZ$200 million with at least three maturities offered at each tender.
- LGFA bonds match NZ Government Bond maturities where possible for maturity and coupon and Approved Issuer Levy is paid on behalf of offshore holders.
- Target issuance of NZ$1 billion plus per series over time with a soft cap of $1.75 billion per series to support market liquidity.
- All bonds New Zealand dollar (NZD) to date, but have capability to issue non-NZD bonds if required.
- All LGFA bonds listed on NZX.

Issuance history (NZ$ million, face value)



Financial year	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**
Average tender size (NZ$ million)	209	182	153	188	141	143	137	188	182
Average issuance term (years)	5.3	6.6	7.0	7.9	8.1	8.3	6.1	6.6	6.9

LGFA typically issues a new bond maturity each year

LGFA is the largest domestic issuer of NZD domestic bonds (excluding New Zealand Government)

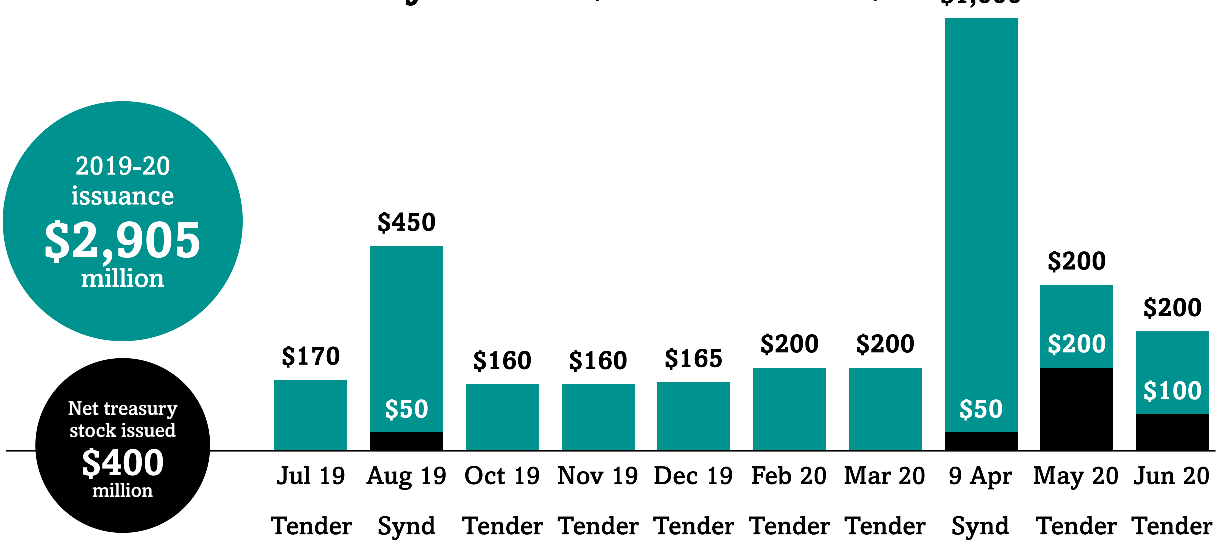
LGFA is the largest issuer of debt listed on the NZDX

2019-20 issuance by maturity (NZ$ million, face value)

LGFA bond issuance by bond maturity over the 12-month period to 30 June 2020

	May 21	Apr 22	Apr 23	Apr 24	Apr 25	Apr 26	Apr 27	Apr 29	Apr 33	Total
Tenders										
17 Jul 2019	-	60	-	60	-	-	-	-	50	170
2 Oct 2019	-	50	-	35	-	-	-	-	75	160
6 Nov 2019	-	40	-	40	30	-	-	-	50	160
11 Dec 2019	-	40	-	30	-	-	-	60	35	165
5 Feb 2020	-	75	-	50	-	-	-	75	-	200
11 Mar 2020	-	80	50	23	-	-	-	47	-	200
6 May 2020	-	50	50	-	-	-	50	-	50	200
3 Jun 2020	-	50	-	60	-	-	-	60	30	200
Total tender issuance	**-**	**445**	**100**	**298**	**30**	**-**	**50**	**242**	**290**	**1,455**
Syndication	**-**	**-**	**-**	**-**	**-**	**1,000**	**-**	**450**	**-**	**1,450**
Total 2019-20 issuance	**-**	**445**	**100**	**298**	**30**	**1,000**	**50**	**692**	**290**	**2,905**
Prior issuance	1,450	710	1,450	950	1,379	-	1,276	-	740	7,955
	1,450	**1,155**	**1,550**	**1,248**	**1,409**	**1,000**	**1,326**	**692**	**1,030**	**10,860**
Treasury stock	50	100	100	100	50	100	100	100	100	800
Total bonds on issue	**1,500**	**1,255**	**1,650**	**1,348**	**1,459**	**1,100**	**1,426**	**792**	**1,130**	**11,660**

2019-20 issuance by month (NZ$ million, face value)



	Jul 19	Aug 19	Oct 19	Nov 19	Dec 19	Feb 20	Mar 20	9 Apr	May 20	Jun 20
Tender coverage ratio	2.6x	n/a	2.3x	1.6x	1.8x	1.7x	1.3x	n/a	3.5x	1.5x
Weighted average yield	1.99	1.77	1.73	1.74	1.78	1.76	1.71	1.61	1.56	1.51

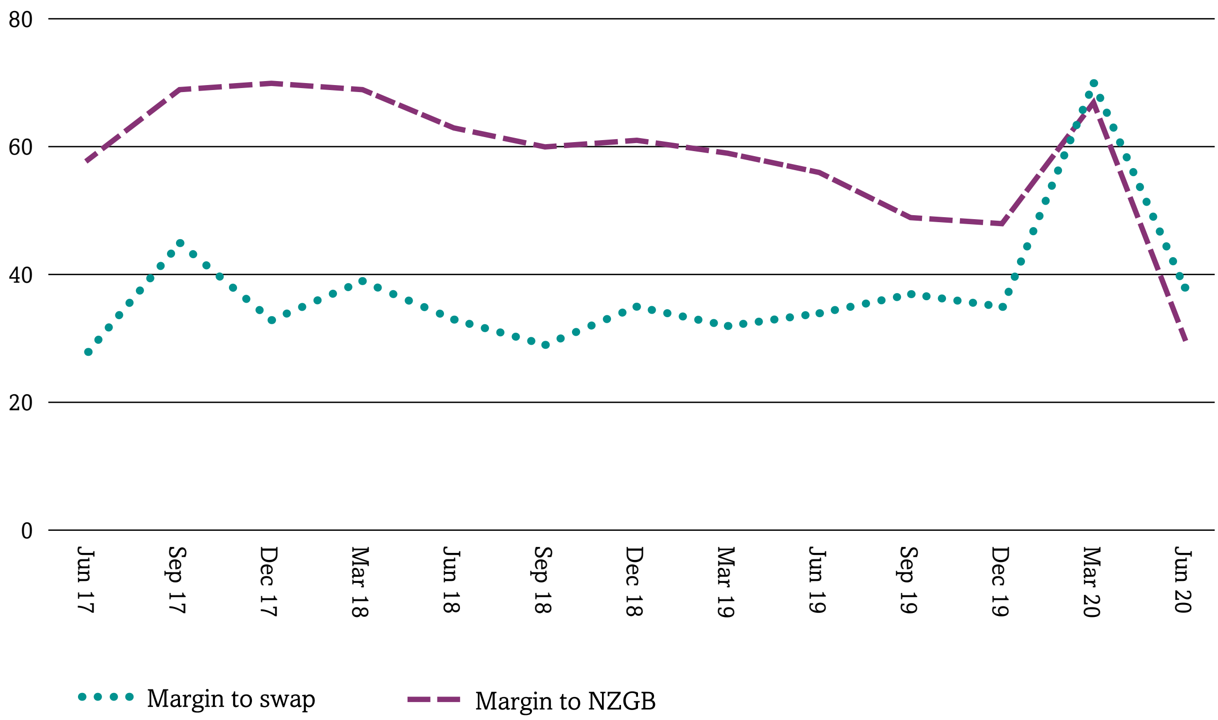
LGFA bond margins (basis points)

LGFA bond margins against swap and NZ government bonds (NZGB) as at 30 June 2020

Margin to swap	May 21	Apr 22	Apr 23	Apr 24	Apr 25	Apr 26	Apr 27	Apr 29	Apr 33
30 June 2019	15	22	30	37	41	n/a	46	n/a	67
30 June 2020	9	18	25	32	40	45	48	57	69
Annual change	6	4	5	5	1	n/a	(2)	n/a	(2)

Margin to NZGB	May 21	Apr 22	Apr 23	Apr 24	Apr 25	Apr 26	Apr 27	Apr 29	Apr 33
30 June 2019	35	36	42	59	65	n/a	70	n/a	92
30 June 2020	14	13	18	22	31	34	36	44	58
Annual change	21	23	24	37	34	n/a	34	n/a	34

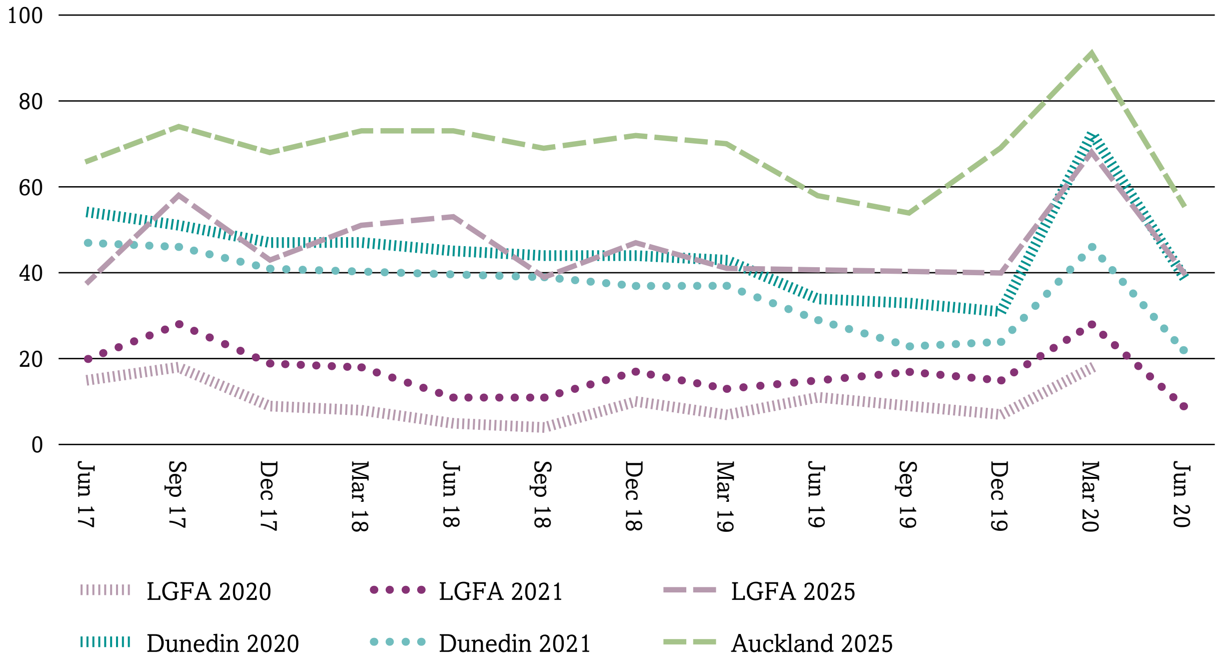
LGFA bond margins to swap over NZGB over the 36 months to 30 June 2020 (basis points)



Average of all LGFA bonds outstanding: Secondary market levels as at end of each month taken from end of month closing rate sheets published by NZ banks.

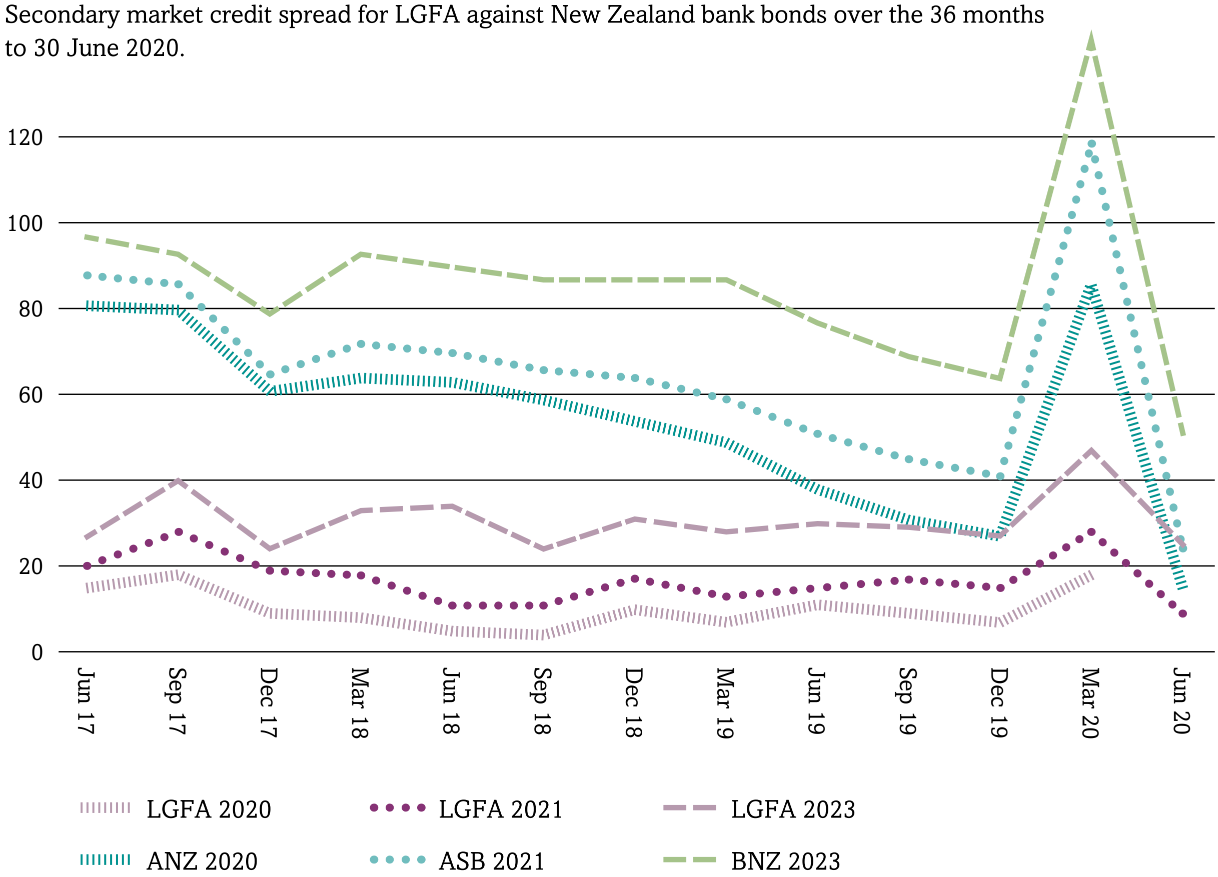
Secondary market credit spread to swap for LGFA and council bonds (basis points)

Secondary market credit spread for LGFA against Auckland Council and Dunedin City Council over the 36 months to 30 June 2020.

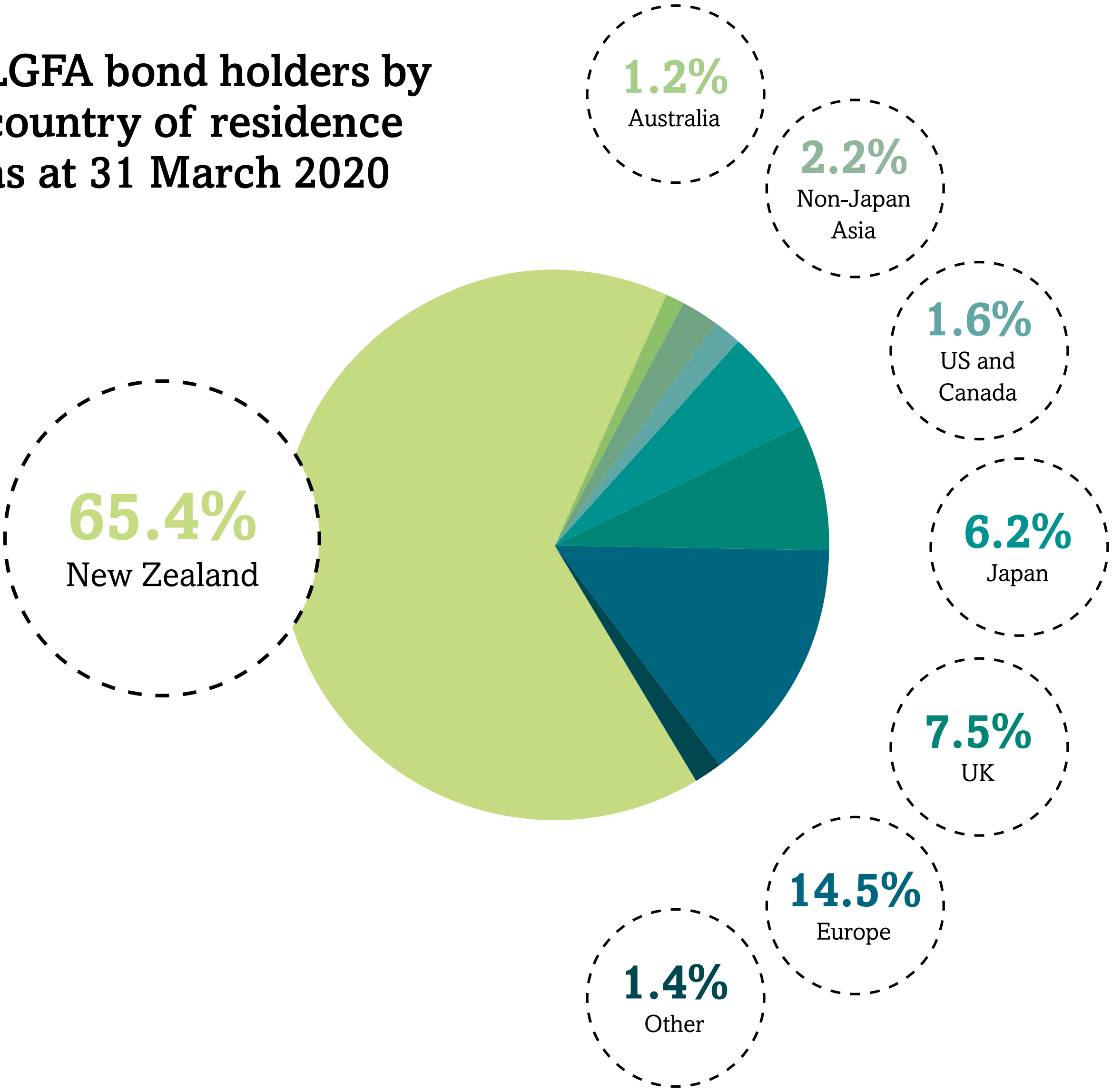


Secondary market credit spread to swap for LGFA and bank bonds (basis points)

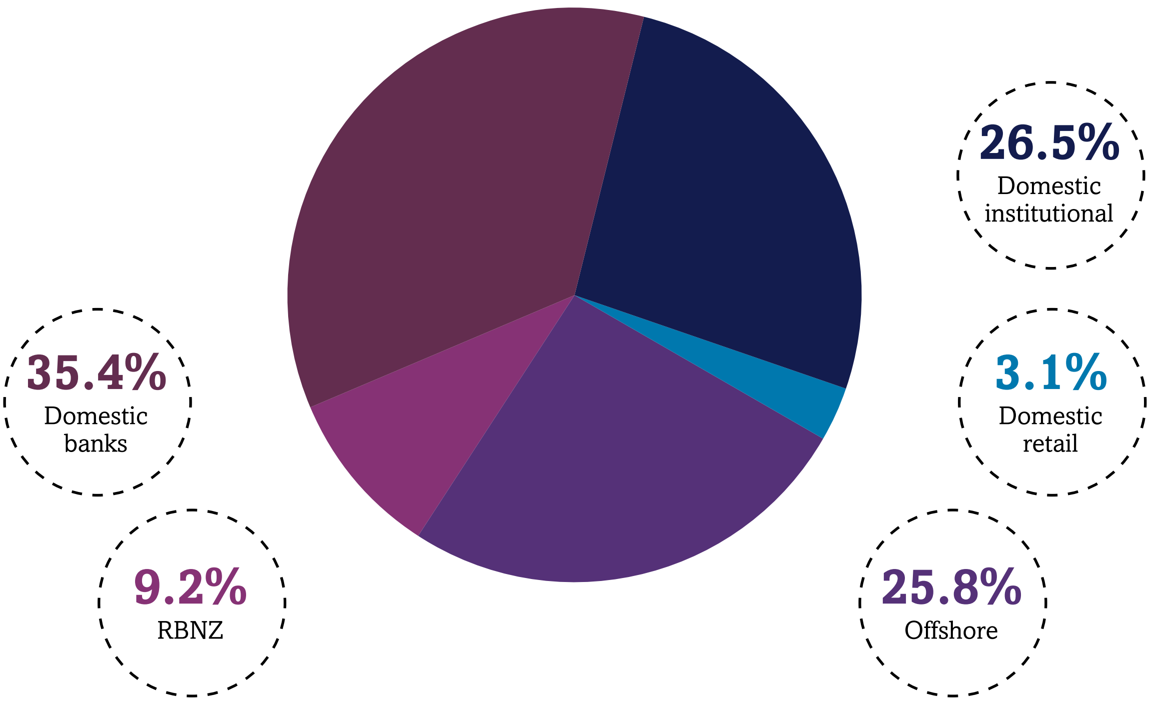
Secondary market credit spread for LGFA against New Zealand bank bonds over the 36 months to 30 June 2020.



LGFA bond holders by country of residence as at 31 March 2020



LGFA bond holders by investor group as at 30 June 2020



Member councils
Ko ngā kaunihera e noho mema ana

LGFA operates with the primary objective of optimising the debt funding terms and conditions for its member councils.

Among other things this includes:

- Providing savings in annual interest costs
- Offering short and long-term borrowings with flexible lending terms
- Enhancing the certainty of debt markets
- Being the funder of choice for New Zealand local government

To become a member council of LGFA, a council is required to complete a formal application. Following an application for membership, LGFA management completes a formal review of the council's financial position and its ability to comply with LGFA's financial covenants, which is considered by the LGFA Board who approve all council memberships. All member councils are required to complete a compliance certificate each year which certifies that the council has complied with LGFA's financial covenants. In addition, LGFA monitor all member councils' annual reports, annual plans and long term plans on an ongoing basis to ensure that the financial forecasts are consistent with the LGFA financial covenants.

As at 30 June 2020

30
member councils are shareholders

67
member councils were eligble to borrow from LGFA

54
member councils were guarantors of LGFA's securities obligations

Total member council borrowings at 30 June 2020

(NZ$ million)

Member type	Number of councils	Amount borrowed	% of total borrowings
Guarantors	54	10,736	98.8%
Non guarantors	13	133	1.2%
Total	**67**	**10,869**	**100%**

86%
LGFA's estimated market share of local government debt

Member	Amount borrowed	% of total borrowings
Auckland Council	2,757	25.4%
Christchurch City Council	1,924	17.7%
Wellington City Council	635	5.8%
Tauranga City Council	525	4.8%
Hamilton City Council	480	4.4%
Wellington Regional Council	425	3.9%
Rotorua District Council	217	2.0%
Hutt City Council	216	2.0%
Kapiti Coast District Council	210	1.9%
Tasman District Council	208	1.9%
57 other member councils	3,272	30.2%
Total face value	**10,869**	**100%**

Loans to Auckland Council are limited to a maximum of **40%** of total loans

Over the 12 months to 30 June 2020

53 member councils borrowed a total of **$2,328 million**

Comprising **205** individual term loans

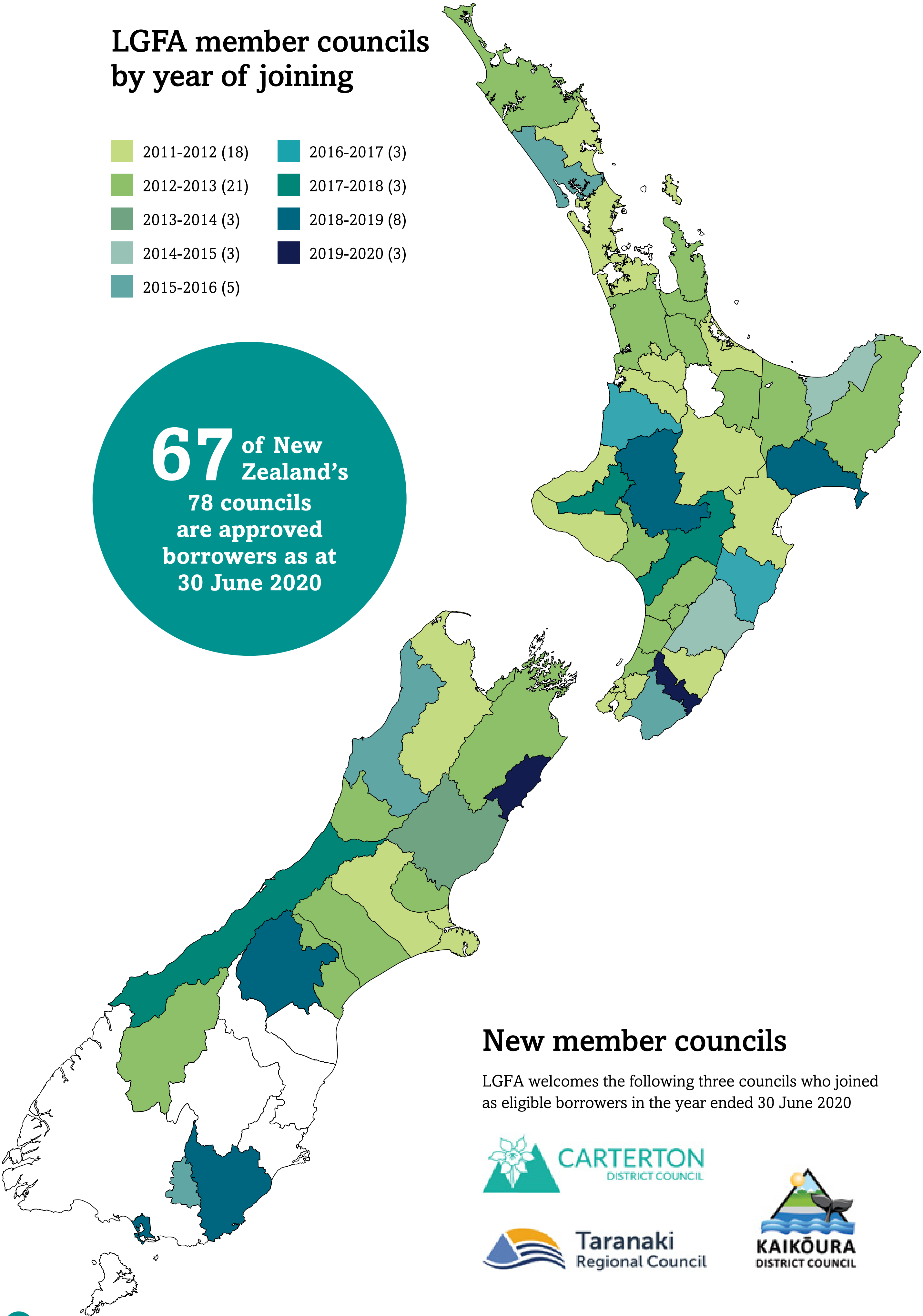
With an average term of **5.4** borrowing years

At 30 June 2020

$316 million of short term loans were outstanding to **27** member councils

Member councils are required to comply with LGFA financial covenants at all times

LGFA member councils by year of joining



67 of New Zealand's 78 councils are approved borrowers as at 30 June 2020

New member councils

LGFA welcomes the following three councils who joined as eligible borrowers in the year ended 30 June 2020

CARTERTON DISTRICT COUNCIL

Taranaki Regional Council

KAIKŌURA DISTRICT COUNCIL

Member councils by year of joining

North Island

2011-12	Auckland Council	Shareholder
2011-12	Bay of Plenty Regional Council	Shareholder
2011-12	Greater Wellington Regional Council	Shareholder
2011-12	Hamilton City Council	Shareholder
2011-12	Hastings District Council	Shareholder
2011-12	Masterton District Council	Shareholder
2011-12	New Plymouth District Council	Shareholder
2011-12	South Taranaki District Council	Shareholder
2011-12	Taupo District Council	Shareholder
2011-12	Tauranga City Council	Shareholder
2011-12	Waipa District Council	Shareholder
2011-12	Wellington City Council	Shareholder
2011-12	Western Bay of Plenty District Council	Shareholder
2011-12	Whangarei District Council	Shareholder
2012-13	Far North District Council	Borrower and Guarantor
2012-13	Gisborne District Council	Shareholder
2012-13	Hauraki District Council	Shareholder
2012-13	Horowhenua District Council	Shareholder
2012-13	Hutt City Council	Shareholder
2012-13	Kapiti Coast District Council	Shareholder
2012-13	Manawatu District Council	Shareholder
2012-13	Matamata-Piako District Council	Borrower and Guarantor
2012-13	Palmerston North City Council	Shareholder
2012-13	Rotorua District Council	Borrower and Guarantor
2012-13	Thames-Coromandel District Council	Shareholder
2012-13	Waikato District Council	Borrower and Guarantor
2012-13	Whakatane District Council	Shareholder
2012-13	Whanganui District Council	Shareholder
2013-14	Horizons District Council	Borrower and Guarantor
2013-14	Upper Hutt City Council	Borrower and Guarantor
2014-15	Opotiki District Council	Borrower
2014-15	Porirua City Council	Borrower and Guarantor
2014-15	Tararua District Council	Borrower
2015-16	Kaipara District Council	Borrower and Guarantor
2015-16	South Wairarapa District Council	Borrower and Guarantor
2016-17	Central Hawkes Bay District Council	Borrower
2016-17	Northland Regional Council	Borrower
2016-17	Waitomo District Council	Borrower and Guarantor
2017-18	Rangitikei District Council	Borrower
2017-18	Stratford District Council	Borrower
2018-19	Hawkes Bay Regional Council	Borrower and Guarantor
2018-19	Ruapehu District Council	Borrower and Guarantor
2018-19	Waikato Regional Council	Borrower and Guarantor
2018-19	Wairoa District Council	Borrower
2019-20	Taranaki Regional Council	Borrower and Guarantor
2019-20	Carterton District Council	Borrower

South Island

2011-12	Christchurch City Council	Shareholder
2011-12	Otorohanga District Council	Shareholder
2011-12	Selwyn District Council	Shareholder
2011-12	Tasman District Council	Shareholder
2012-13	Ashburton District Council	Borrower and Guarantor
2012-13	Grey District Council	Borrower
2012-13	Marlborough District Council	Shareholder
2012-13	Nelson City Council	Borrower and Guarantor
2012-13	Queenstown Lakes District Council	Borrower and Guarantor
2012-13	Timaru District Council	Borrower and Guarantor
2012-13	Waimakariri District Council	Shareholder
2013-14	Hurunui District Council	Borrower and Guarantor
2015-16	Buller District Council	Borrower
2015-16	Canterbury Regional Council	Borrower and Guarantor
2015-16	Gore District Council	Borrower
2017-18	Westland District Council	Borrower
2018-19	Clutha District Council	Borrower
2018-19	Invercargill City Council	Borrower and Guarantor
2018-19	Mackenzie District Council	Borrower
2018-19	West Coast Regional Council	Borrower
2019-20	Kaikoura District Council	Borrower

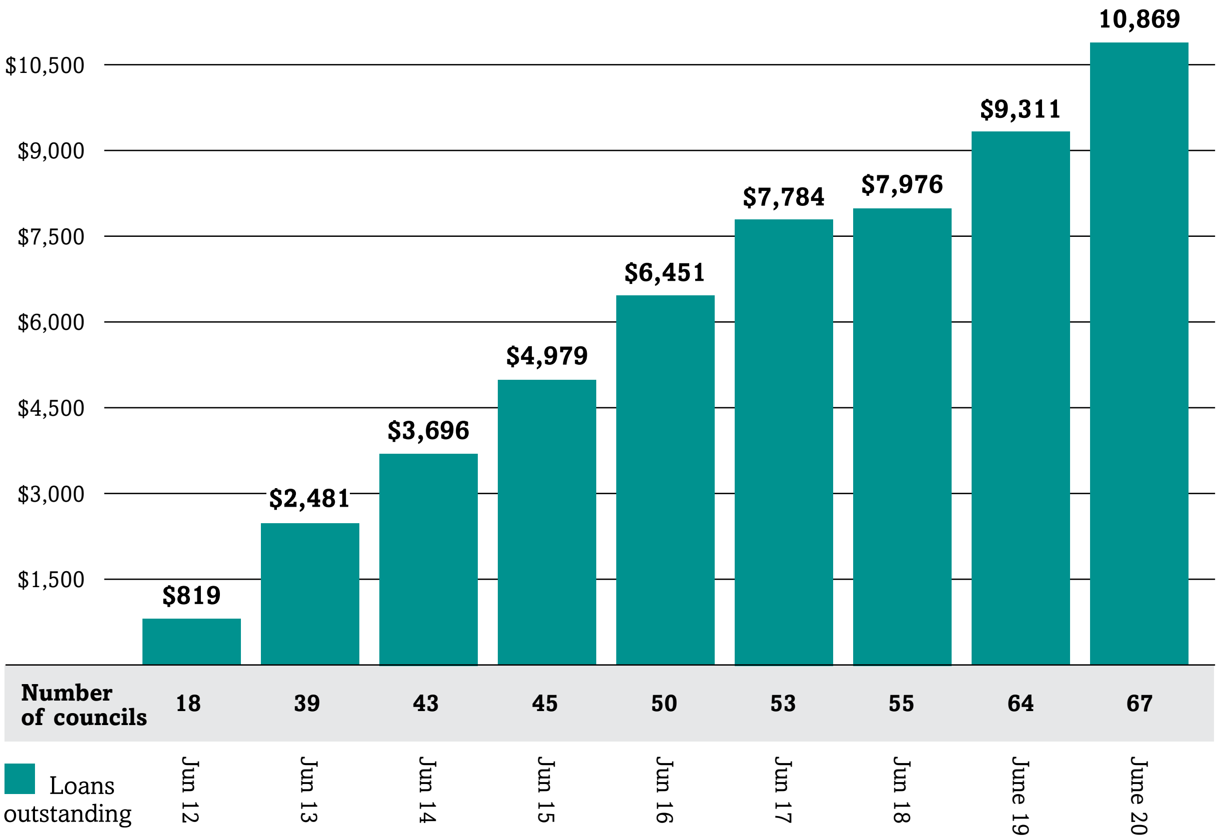
88%
of LGFA loans are to councils with credit ratings of
AA-
or better as at 30 June 2020

30
member councils have credit ratings (A+ to AA+ range)

LGFA assign internal credit ratings for all councils, including all councils without extrernal credit ratings.

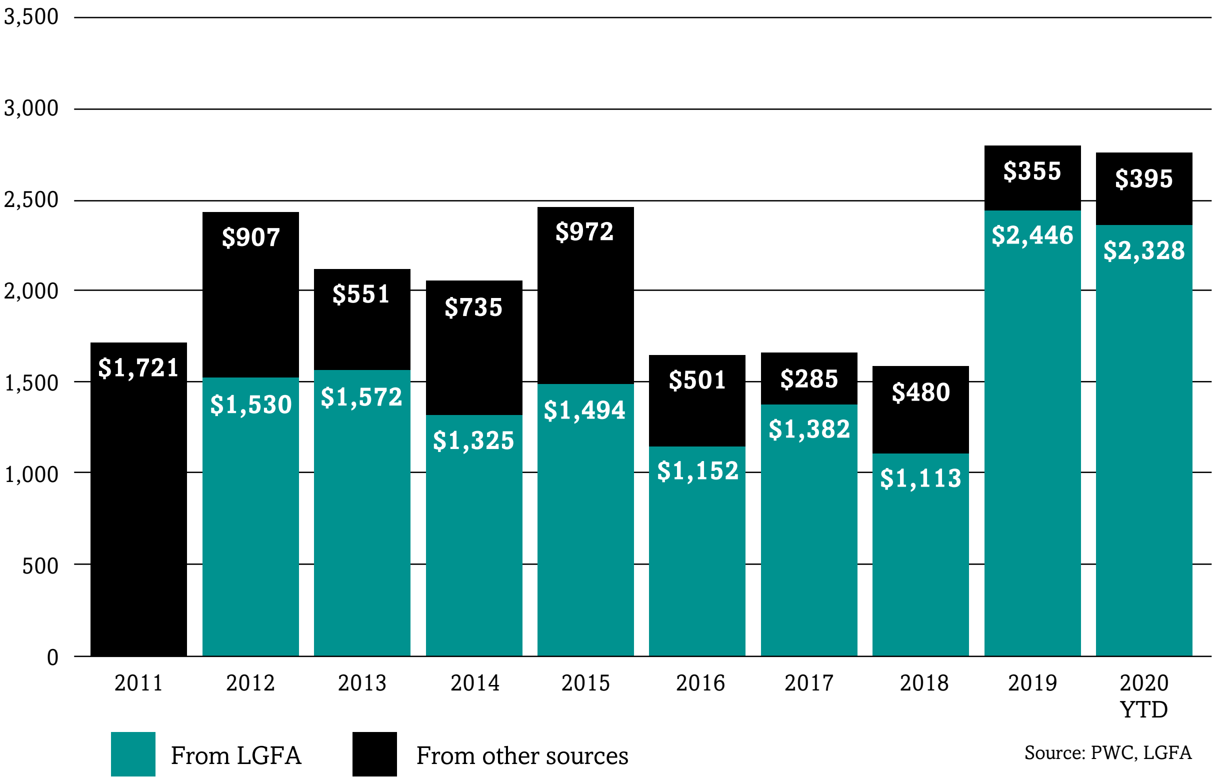
LGFA council members and nominal loans outstanding

(NZ$ million)



Councils' borrowing

All councils (NZ$ million) calendar year



Source: PWC, LGFA

Upgrading the Great Lake Pathway, Taupo

Taupo District Council

Sustainability at LGFA
Toitūtanga ki te LGFA

LGFA was established with the primary objective of optimising the debt funding terms and conditions for our member councils. Key to achieving this objective is that we conduct our affairs in accordance with sound business practice, while having regard to the interests of the community and by exhibiting a sense of social and environmental responsibility, as well as being a good employer.

This year's annual report is our first to have been prepared to under the Global Reporting Initiative (GRI) sustainability reporting standards which are the most widely adopted global standards for sustainability reporting. This report has been prepared in accordance with the GRI Standards: Core option.

In 2019, LGFA engaged Proxima, an independent sustainability consultancy, to work with staff and directors to undertake an analysis of material sustainability issues relevant to our business and key stakeholders. Following a series of internal workshops, including discussions with key stakeholders, we determined our material topics. Material topics are those issues that reflect our significant economic, environmental, and social impacts or that substantively influence the assessments and decisions of our stakeholders.

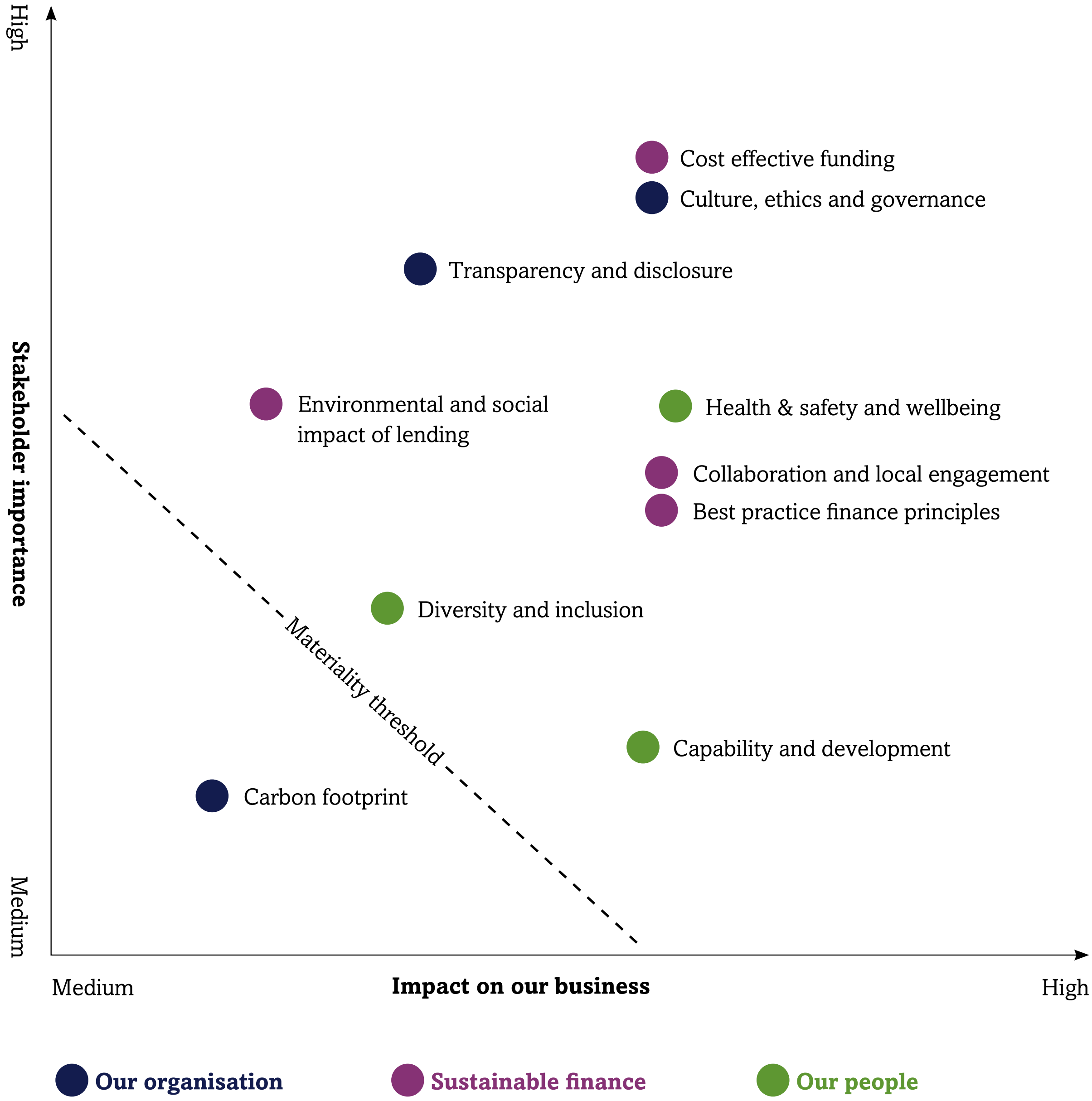
LGFA's ten material topics are grouped under three overarching principles.

Our organisation	Sustainable finance	Our people
Culture, ethics and governance	Cost effective funding	Health & safety and wellbeing
Transparency and disclosure	Environmental and social impact of lending	Diversity and inclusion
Carbon footprint	Collaboration and local engagement	Capability and development
	Best practice finance principles	

LGFA's materiality matrix

LGFA's materiality matrix depicts the outcome of our materiality analysis and is prioritised by stakeholder importance and the estimated impact on our business or on society. The prioritisation of these material topics will assist us to review our management approach and assess where we can improve over time.

Our approach and performance on each material topic can be found in this Annual Report and are referenced in the GRI Index on page 85.



KAURI 2000

In 2020, LGFA made a donation to **Kauri 2000** to offset carbon for air travel kilometres by staff. **Kauri 2000** was established in 1999 as a project to celebrate the start of the new millennium by planting 2000 kauri on the Coromandel Peninsula. To date the Trust has planted over 50,000 trees and continues to plant kauri throughout the Coromandel.

LGFA's material topics

In order of priority

Our organisation **Sustainable finance** **Our people**

Cost effective funding

- Delivery of lower cost funding
- Access to longer term funding
- Ongoing contribution to NZ Capital Markets
- NZX listing

Transparency and disclosure

Transparency and disclosure are essential for shareholder, rating agencies and investor confidence and codified through:

- Shareholders' agreement
- NZX listing rules
- Financial accounting standards
- Regulatory compliance

Health & safety and wellbeing

- Compliance with Health and Safety at Work Act 2015
- Health and safety committee and regular reporting to Board
- Flexible workplace

Best practice finance principles

- Knowledge sharing
- Audit and risk independence
- Best practice risk management framework
- Credit metrics
- External rating / lower margin borrowing
- Operational excellence
- Product and process improvement
    - CCO lending
    - Bills
    - Flexible maturities
    - Standby facilities

Carbon footprint

- Air travel kilometres travelled offset by donation to Kauri 2000.
- Paperless office – use electronic where possible for transaction recording.
- Physical offices – minimal impact given small size
- Video links reduce need for physical travel
- Compliance with Climate Change Response (Zero Carbon) Amendment Act 2019

Culture, ethics and governance

High ethical standards required and codified through:

- NZX Corporate Governance Code
- Code of Ethics
- Code of Conduct
- Board Charter
- ARC Charter

Environmental and social impact of lending

- Development of green financing option for councils
- Lower cost financing promotes greater ability for councils to fund green/social impact projects

Collaboration and local engagement

- Industry sponsor – Kanganews and SOLGM
- Infrastructure funding development liaison with Crown and industry
- Productivity Commission
- LGNZ
- Regular engagement with council employees and elected officials

Diversity and inclusion

- Diversity policy and reporting
- Equal opportunity
- Māori language plan
- Flexible working

Capability and development

- Regular attendance for staff and directors at industry training and conference events

Construction underway on the new $27 million Whau Valley Treatment Plant
Whangarei District Council

Green, social and sustainability lending

Ko te tuku pūtea taurewa mā te taiao, mā te hapori, mā te toitūtanga

A commitment to assist councils finance projects that promote environmental and social wellbeing in New Zealand.

LGFA recognises the risks inherent in climate change at the national and regional level and wishes to support New Zealand's shift to a low-carbon economy. LGFA also recognises it has a role to play in New Zealand's contribution to meeting the United Nations Sustainable Development Goals (SDGs) and helping its council members to build a stronger and more resilient society.

One of the principal objectives of LGFA, being a Council Controlled Organisation, under the Local Government Act 2002, is to exhibit a sense of social and environmental responsibility and LGFA acknowledges the future importance of assisting its council members by financing projects that promote environmental and social wellbeing in New Zealand and progress the SDGs.

LGFA has commenced consulting with member councils on the feasibility of establishing a future loan program that will enable councils to undertake green, social and sustainability projects that will help drive forward ambitious climate, environmental and social projects in the New Zealand local government sector. The loans will be Green, Social or Sustainable (GSS Loans).

Green, social and sustainability loans

Any future GSS lending program would be underpinned by a framework that encompasses evaluation and eligibility criteria, transparency of disclosures and reporting and ongoing independent external review.

The criteria for GSS lending would include projects that are able to provide a proven reduction in energy consumption and/or greenhouse gas emissions, that strengthen the level of local adaptation to challenges posed by climate change, or that have an identified social objective. These projects would target requirements higher than the minimum requirements in the relevant legislation and have explicit climate, environmental, social or sustainable ambitions.

Pipe replacement on Queens Drive, Invercargill.
Invercargill City Council

GSS lending would support councils with financing across a wide range of projects that promote achievement across the following green and social project categories:

Green Categories
Renewable Energy
Energy Efficiency
Pollution Prevention and Control
Environmentally Sustainable Management of Living Natural Resources and Land Use
Terrestrial and Aquatic Biodiversity Conservation
Clean Transport
Sustainable Water and Wastewater Management
Climate Change Adaptation
Eco-efficient and/or Circular Economy Adapted Products, Production Technologies and Processes
Green Buildings

Social Categories
Affordable Basic Infrastructure
Access to Essential Services
Affordable Housing
Employment Generation Including through the Potential Effect of SME Financing and Microfinance
Food Security
Socioeconomic Advancement and Empowerment

As at the date of this report, work is progressing on consulting councils on the development of a framework. This project is scheduled to be completed in the coming year, the outcome of which will form part of our 2021 Annual Report.

Corporate governance
Ārahitanga ā-rangatōpū

NZX Corporate Governance Best Practice Code

The LGFA Board is committed to ensuring LGFA demonstrates ongoing commitment to strong and sound corporate governance.

LGFA is a listed issuer on the NZX Debt Market and this section sets out LGFA's compliance with the eight core principles underpinning the NZX Corporate Governance Best Practice Code 2020.

LGFA considers that its governance practices have not materially differed from the NZX Code for the year ended 30 June 2020. Areas where LGFA has implemented alternative measures to the Code are as follows:

An Issuer should establish a nomination committee to recommend director appointments to the Board.	The process for the nomination and remuneration of directors is documented in the Constitution of New Zealand Local Government Funding Agency Limited and outlined below.
An Issuer should have a remuneration committee which operates under a written charter.	

The following governance documents referred to in this section are available on the LGFA website: lgfa.co.nz/about-lgfa/governance:

- LGFA Constitution
- Shareholders' Agreement
- Code of Ethics
- Board Charter
- Audit and Risk Committee Charter
- Internal Audit Charter
- Diversity Policy
- Remuneration Policy

Principle 1
Code of ethical behaviour

Directors should set high standards of ethical behaviour, model this behaviour and hold management accountable for these standards being followed throughout the organisation.

Code of Ethics

LGFA has adopted a formal Code of Ethics, incorporating its Conflicts of Interest Policy and Code of Conduct Policy, which sets out the standards that both directors and employees of LGFA are expected to follow to reflect the values of LGFA.

LGFA recognises impartiality and transparency in governance and administration are essential to maintaining the integrity of LGFA. Accordingly, the Conflicts of Interest Policy formally provides guidance to employees and directors of LGFA in relation to conflicts of interest and potential conflicts of interest, including specific guidance 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.

The Code of Conduct Policy requires employees and directors to carry out their roles while maintaining high standards of integrity and conduct by clearly setting out standards for expected behaviour. In addition, the policy sets out LGFA's commitment to behave in a fair and reasonable manner to employees, while providing a fair and safe working environment.

Protected Disclosures and Whistle Blowing

LGFA has adopted a Protected Disclosures and Whistle Blowing Policy which provides procedure, support and protection to persons who disclose information which they reasonably believe to be about serious wrong-doing in or by LGFA.

Financial Products Trading Policy

LGFA has formally adopted a Financial Products Trading Policy, which applies to all directors, employees and contractors, and details LGFA's policy on, and rules for dealing in, listed debt securities issued by LGFA and any other quoted financial products of LGFA.

Principle 2
Board composition and performance

To ensure an effective Board, there should be a balance of independence, skills, knowledge, experience and perspectives.

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 LGFA achieves the its goals. Having regard to its role the Board will direct, and supervise the management of the business and affairs of LGFA, including:

- ensuring that LGFA's 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 LGFA's performance;
- ensuring strategies are in place for meeting expectations set out in the current Statement of Intent and monitoring performance against those expectations, in particular LGFA'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;
- deciding on whatever steps are necessary to protect LGFA'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 LGFA's financial statements are true and fair and otherwise conform with law;
- ensuring that LGFA adheres to high standards of ethics and corporate behaviour; and
- ensuring that LGFA has appropriate risk management/regulatory compliance policies in place.

In the normal course of events, day-to-day management of LGFA will be in the hands of management. The Board will satisfy itself that LGFA is achieving its goals, and engaging and communicating with Shareholders' Council.

Board composition

The LGFA Board comprises five independent Directors and one non-independent Director. An independent director is a director who, within five years prior to appointment, was not an employee of any shareholder, employee of a Council-Controlled Organisation owned by a shareholder, or a councillor of any local authority which is a shareholder.

The directors of LGFA as at 30 June 2020:

Craig Stobo
Independent Chair

BA (Hons) Economics. First Class, Otago
C.F.Inst.D
Associate Member CFA Society New Zealand

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 the listed companies Precinct Properties New Zealand Limited and AIG Insurance (NZ Board). He has directorship and private equity interests in financial services and other businesses.

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, several start-up businesses, a number of CCOs, an industry cooperative 'ITM', Regional Facilities Auckland Limited and Spider Tracks Limited. He is currently an independent director of Strategic Pay Limited and a Trustee of the Royal New Zealand Ballet.

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 30 years. He is currently a director of Powerco, Matariki Forests, South Port New Zealand and Papa Rererangi I Puketapu (New Plymouth Airport). Philip is also a 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.

Linda Robertson

Independent Director

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

Linda Robertson is a professional company director with over 20 years of governance experience and more than 30 years' experience in executive finance roles having worked in the banking and energy sector in New Zealand. Linda is currently chair of Central Lakes Trust and Crown Irrigation Investments, and a director of Dunedin City Holdings Limited, Dunedin City Treasury Limited and Dunedin Stadium Properties Limited. She is chair of the Audit and Risk Committee for the Central Otago District Council, a member of the Board of AWS Legal, a member of the Risk and Audit Committee for The Treasury and a member of the Capital Markets Advisory Committee for The Treasury.

Mike Timmer

Non-Independent Director

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

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, Independent member Whanganui District Council Audit and Risk Committee and past Deputy Chair of the LGFA Shareholders' Council.

Anthony Quirk

Independent Director

BCA Hons (First Class), INFINZ (Fellow), AFA, M.Inst.D

Anthony is an experienced financial services sector professional with over thirty years executive experience in the sector, including nine years as Managing Director of Milford Asset Management. He has a varied portfolio of governance interests with an emphasis on areas that improve or contribute to communities. He is a Fellow of the Institute of Finance Professionals New Zealand (INFINZ) and is a former Chairman of that organisation. He was previously Chair of the Asset Management Advisory Board of the New Zealand Exchange, Deputy Chair and Board member of the New Zealand Society of Investment Analysts and a previous member of the Financial Reporting Standards Board of the New Zealand Society of Accountants.

Directors and staff interests as at 30 June 2020

Craig Stobo (Chair)

Director

Precinct Properties New Zealand Limited (Chair and shareholder)

Elevation Capital Management Limited (Chair and shareholder)

Saturn Portfolio Management Limited (Chair and shareholder)

Stobo Group Limited (Managing Director and shareholder)

AIG Insurance NZ Limited (Chair)

SouthWest Trustees Limited (Shareholder)

Appello Services Limited

Biomarine Group Limited (Chair and shareholder)

Legend Terrace Limited (Chair and shareholder)

John Avery

Director

Strategic Pay Limited

General disclosure

Royal New Zealand Ballet (Trustee)

Philip Cory-Wright

Director

South Port New Zealand Limited

Matariki Forest Group Limited

Powerco Limited

Papa Rererangi i Puketapu (New Plymouth Airport) (Chairman)

Anthony Quirk

Director

Milford Asset Management Limited (and associated subsidiaries) (Non-Executive Director and shareholder)

Compass Housing NZ (Deputy Chair)

Humanitix, New Zealand (Chair)

Linda Robertson

Director

Dunedin City Holdings Limited

Dunedin City Treasury Limited

Dunedin Stadium Property Limited

Central Lakes Trust (Chair) and associated subsidiaries.

Crown Irrigation Investments Limited (Chair)

General disclosure

Capital Markets Advisory Committee, The Treasury (Member)

Risk & Audit Committee, The Treasury (Member)

Audit & Risk Committee, Central Otago District Council (Chair)

Board, AWS Legal (Member)

Mike Timmer

General disclosure

Greater Wellington Regional Council (Officer)

Finance Committee, Physiotherapy New Zealand (Chairman)

Whanganui District Council Risk & Audit Committee (Member)

Mark Butcher – Chief Executive

New Plymouth PIF Guardians Limited (Chair)

Waikato-Tainui Group Investment Committee (Chair)

Nominating Committee for Guardians of New Zealand Superannuation (Member)

Neil Bain – Chief Financial Officer

Audit & Risk Committee, Central Hawkes Bay District Council (Chair)

Nomination of Directors

Director nominations can only be made by a shareholder by written notice to LGFA 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 LGFA 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, 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

As at 30 June 2020

Director	Originally appointed	Last reappointed/ elected	Tenure	Next reappointment
Craig Stobo (Chair)	1 December 2011	21 November 2017	8 years, 7 months	November 2021
John Avery	1 December 2011	21 November 2018	8 years, 7 months	November 2022
Philip Cory-Wright	1 December 2011	24 November 2016	8 years, 7 months	November 2020
Anthony Quirk	21 November 2017	21 November 2017	2 years, 7 months	November 2021
Linda Robertson	24 November 2015	21 November 2019	4 years, 7 months	November 2023
Mike Timmer	24 November 2015	21 November 2019	4 years, 7 months	November 2020

Board performance review

The Board has established an annual formal self-assessment procedure to assess director, board and committee performance. In addition, Board performance is reviewed by external consultants on a periodic basis.

Director and staff capability

As part of LGFA's commitment to ongoing education for directors and staff, LGFA regularly invites directors and staff to attend relevant industry conferences and training events, as well as organising for industry experts to attend and present to directors at Board meetings.

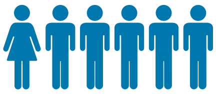
Diversity

The LGFA is committed to promoting a culture that supports both workplace diversity and inclusion within the organisation.

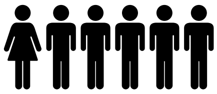
LGFA has formally adopted a Diversity Policy which applies to both LGFA employees and directors. Diversity and inclusiveness at LGFA involves recognising the value of individual differences and managing them in the workplace. Diversity in this context covers gender, age, ethnicity, cultural background, sexual orientation, religious belief, disability, education and family responsibilities.

Appointments to the LGFA Board are made in accordance with LGFA's Constitution and the Shareholders Agreement.

Gender diversity of directors

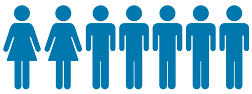


2020
Female 1, Male 5

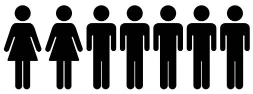


2019
Female 1, Male 5

Gender diversity of employees



2020
Female 2, Male 5



2019
Female 2, Male 5

Indemnities and insurance

Under LGFA'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 LGFA. Cover is for damages, judgements, fines, penalties, legal costs awarded and defence costs arising from wrongful acts committed while acting for LGFA. The types of acts that are not covered are dishonest, fraudulent, malicious acts, or omissions, wilful breach of statute or regulation, or duty to LGFA, improper use of information to the detriment of LGFA, or breach of professional duty.

Principle 3
Board committees

The Board should use committees where this will enhance its effectiveness in key areas, while still retaining board responsibility.

Audit and Risk Committee

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

The Audit and Risk Committee is governed by an Audit and Risk Committee Charter, which states that the purpose of the Audit and Risk Committee 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 LGFA. It assists the Board to fulfil its duties by considering, reviewing and monitoring:

- Risk management framework and processes;
- Internal control environment and mechanisms;
- The operations and effectiveness of the internal audit function;
- Processes relating to the preparation and audit of financial statements of 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.

Audit and Risk Committee members are appointed by the Board. Membership comprises at least three directors, the majority of whom must be independent. The members of the Audit and Risk Committee as at the date of this Annual Report are:

- Linda Robertson (Chair)
- Philip Cory-Wright
- Anthony Quirk
- Mike Timmer

Principle 4
Reporting and disclosure

The Board should demand integrity in financial and non-financial reporting and in the timeliness and balance of corporate disclosures.

The Board is committed to ensuring the highest standards are maintained in financial reporting and disclosure of all relevant information.

The Audit and Risk Committee has responsibility to provide assurance to the Board that due process has been followed in the preparation and audit of the financial statements of LGFA and to ensure there are appropriate processes and activities to ensure compliance with relevant regulatory and statutory requirements.

LGFA has adopted a formal Continuous Disclosure Policy, the requirements of which ensure that LGFA meets the continuous disclosure requirements of the NZX Listing Rules including the disclosure for material environmental, social and governance (ESG) factors.

The GRI sustainability reporting standards are the most widely adopted global standards for sustainability reporting and this year's annual report is our first to have been prepared to meet the requirements of the Global Reporting Initiative (GRI) Standards (core option).

Principle 5
Remuneration

The remuneration of directors and the executives should be transparent, fair and reasonable.

The remuneration of the Board reflects LGFA's size and complexity and the responsibilities, skills, performance and experience of the directors. A specialist independent adviser may be used to ensure the remuneration is appropriate.

Board remuneration is determined by an Ordinary Resolution of shareholders. The current board remuneration was approved by shareholder resolution at the Annual General Meeting on 21 November 2019.

Director annual fee breakdown

Position. Fees per annum	2020	2019
Board Chair	$102,000	$97,000
Audit and Risk Committee Chair	$63,000	$60,000
Director / ARC Member	$59,000	$55,000
Director	$57,000	$55,000

Director remuneration

Director	2020
Craig Stobo	$102,000
John Avery	$57,000
Philip Cory-Wright	$59,000
Anthony Quirk	$59,000
Linda Robertson	$63,000
Mike Timmer	$59,000
Total	**399,000**

The remuneration of the CEO is determined by the Board and is reviewed on an annual basis taking into consideration the scope and complexity of the position with reference to the remuneration of CEOs of similar organisations. A specialist independent adviser may be used to ensure the remuneration is appropriate.

The CEO remuneration package comprises a fixed cash component of $530,000 per annum as at 30 June 2020 ($530,000, 2019) and an at-risk short-term incentive of the fixed cash component. The short-term incentive payment is made annually at the Board's discretion subject to the CEO and LGFA meeting a range of specific performance objectives for the respective financial year.

Chief Executive remuneration

Position. Fees per annum	2020	2019
Salary	530,000	530,000
Taxable benefits	-	-
Subtotal	530,000	530,000
Pay for Performance STI	79,500	71,500
Kiwisaver Employer Contribution	24,000	24,000
Total remuneration	609,500	601,550

Staff remuneration

Total remuneration	2020
$140,000 to $149,999	1
$170,000 to $179,999	1
$180,000 to $189,999	1
$260,000 to $269,999	1
$300,000 to $309,999	1
$600,000 to $609,999	1
Total staff receiving $100,000 or more	6

Principle 6
Risk management

Directors should have a sound understanding of the material risks faced by the issuer and how to manage them. The Board should regularly verify that the issuer has appropriate processes that identify and manage potential and material risks.

LGFA continually reviews its core business risks. This review process includes the identification and assessment of core business risks which are ranked using predetermined criteria for both the likelihood and potential impact of each risk. LGFA maintains a company-wide risk register which records all identified risks, potential impacts and the controls and mitigation strategies used to manage the risks.

The Audit and Risk Committee assists the Board by considering, reviewing and monitoring LGFA's risk management framework and processes, and the internal control environment and mechanisms.

A detailed description of LGFA's risk management processes, including managing treasury exposures, is detailed in the Managing Risk section of this report.

Internal audit

LGFA has an internal audit function to provide assurance that LGFA's risk management, governance and internal controls are operating effectively.

The Audit and Risk Committee has responsibility for oversight of the internal audit function, including:

- Reviewing the Internal Audit Charter, the operations of the internal audit and organisational structure of the internal audit function;
- Reviewing and approving the annual audit plan;
- Reviewing the effectiveness of the internal audit function; and
- Meeting separately with the internal auditor to discuss any matters that the Audit and Risk Committee or Internal Audit believes should be discussed privately.

Health and safety

LGFA is committed to a safe and healthy work environment and has formally adopted a Health and Safety Policy that clearly sets out the duty of directors and staff under the Health and Safety at Work Act 2015. A staff health and safety committee has been established with responsibility to continuously review health and safety issues and ongoing compliance with the Act, with reporting to the Board on health and safety issues at each Board meeting.

Principle 7
Auditors

The Board should ensure the quality and independence of the external audit process.

External audit

The external audit of LGFA is conducted in accordance with Section 14 of the Public Audit Act 2001, including the appointment of the external auditors of LGFA by the Auditor-General.

The Audit and Risk Committee has responsibility for all processes relating to the audit of financial statements, including the setting of audit fees and ensuring the independence and objectivity of the auditors.

The external audit of LGFA is conducted in accordance with a formal external audit plan which is reviewed and approved by the Audit and Risk Committee on an annual basis. The external auditor attends LGFA's Annual General Meeting.

Principle 8
Shareholder rights and relations

The Board should respect the rights of shareholders and foster relationships with shareholders that encourage them to engage with the issuer.

LGFA has 31 shareholders, comprising the New Zealand Government (20%) and the following 30 councils

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.

Foundation documents

The LGFA Constitution and the Shareholders' Agreement are foundation documents.

The LGFA Constitution defines the rights and the exercise of powers of shareholders, the acquisition and redemption of company shares, proceedings of shareholder meetings, voting at meetings and the right to demand polls, shareholder proposals and review of management.

The Shareholders' Agreement is an agreement between LGFA and its shareholders which clearly defines LGFA's business, its objectives, the role of the Board, the establishment of the shareholders' Council and the approval rights of the shareholders.

LGFA Shareholders' Council

The LGFA Shareholders' Council comprises five to ten appointees from the Council Shareholders and the New Zealand Government. 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.

Members of the Shareholders' Council as at 30 June 2020

- Alan Adcock, Whangarei District Council, Chair
- John Bishop, Auckland Council, Deputy Chair
- Mohan de Mel, Tauranga City Council
- David Bryant, Hamilton City Council
- Kumaren Perumal, Western Bay of Plenty District Council
- Mat Taylor, Bay of Plenty Regional Council
- Martin Read, Wellington City Council
- Mike Drummond, Tasman District Council
- Carol Bellette, Christchurch City Council
- Richard Hardie/Oliver Martin, New Zealand Government

Managing risk
Ko te whakahaere tūraru

An effective risk management framework is a critical component of LGFA's business structure as the company is exposed to business and treasury related risks as a result of its normal business activities in relation to raising and on-lending funds to local councils.

The objective of LGFA's risk management function is to ensure that effective controls and frameworks are implemented to ensure that risks are managed effectively and in compliance with LGFA's governance and legislative requirements. The risk management function ensures that LGFA can achieve its objectives, as set out in the Statement of Intent, in a manner that is consistent with the risk appetite of the company's shareholders and Board.

The objective of LGFA's risk management framework is to ensure that the organisation operates within shareholder and Board-approved risk limits. LGFA's approach to risk management is based on the following core elements:

- The LGFA Board oversees the risk appetite of the organisation and ensures that it is consistent with the constitution and shareholders' agreement.
- The risk appetite is reflected in policies that are approved by the LGFA Board and Audit and Risk Committee, as defined by the LGFA register of policies.
- LGFA management ensures that policies and controls are implemented and maintained to ensure that all relevant risks are identified, monitored, measured and managed.
- The Internal Audit (IA) and risk and compliance function provide assurance to both the Board and the Audit and Risk Committee on the performance of internal controls and risk management systems that are in place.

The LGFA adopts the three lines of defence model to ensure that essential risk management functions are completed using a systematic approach that reflects industry best practice. The three lines of defence model can be summarised as:

- The 1st line of defence establishes risk ownership within the business and is represented by the operational risk and control processes within the business. Business managers are responsible for identifying controls, maintaining effective controls and mitigating risks.
- The 2nd line of defence establishes risk control within the organisation by ensuring that risks are actively and appropriately managed by processes such as the regular review of risk reports and compliance monitoring against the risk management framework.
- The 3rd line of defence establishes independent assurance on the risk governance framework provided by both the internal and external audit functions which review and highlight control weaknesses and inefficiencies to management and the Board.

LGFA risk register

The LGFA risk register is a key component of the company's risk management framework.

The key objective of the LGFA risk register is to ensure that the company assesses the inherent risks faced by the business on an ongoing basis.

The risk register:

- Identifies the inherent risks that LGFA is exposed to when conducting its core business activities;
- Provides an assessment of the likelihood and potential impact of the inherent risks on the business;
- Describes the internal control framework and management processes that are in place to manage and mitigate the identified inherent risks;
- Provides commentary on internal audit coverage of the identified inherent risks; and
- Assesses the likelihood and impact of the residual risks.

The LGFA risk register is reviewed quarterly by management and at each meeting of the Audit and Risk Committee.

Treasury risk management

LGFA funds itself through domestic and international wholesale and retail debt capital markets, with the funds raised on-lent to participating New Zealand Local Authority borrowers. LGFA activities are governed by the Local Government Borrowing Act 2011, the Local Government Act 2002, and the Companies Act 1993. In addition, the company is required to comply with `Foundation Policies' outlined in the Shareholders Agreement. Any change to the Foundation Policies require shareholders' consent.

The LGFA risk management framework uses an approved risk identification and assessment framework to actively monitor and manage all treasury and financial risks using best practice risk management principles, processes and practices.

LGFA has treasury exposures arising from its normal business activities that principally relate to the raising and on-lending of funds. LGFA manages treasury exposures under a Board-approved Treasury Policy. The objectives for the Treasury Policy are to:

- Effectively manage treasury risks within approved compliance limits to protect LGFA's capital position and Net Interest Margin over time.
- Fund participating local authorities in the most cost-effective manner and in accordance with the operating principles, values and objectives of the LGFA.
- Protect LGFA's assets and prevent unauthorised transactions.
- Promote professional expertise of financial and management control to all external parties.
- Minimise operational risk by maintaining adequate internal controls, systems and staffing competencies.
- Provide timely reporting to the LGFA Board with meaningful and accurate reporting of interest rate exposures, liquidity, asset and liability maturity, funding, counterparty credit, performance and Policy compliance.

Specific treasury exposures relate to liquidity, interest rate/market risk, foreign exchange, counterparty credit, operational and lending risks.

Liquidity risk

Liquidity risk refers to the potential inability of LGFA to meet its financial obligations when they become due, under normal or abnormal/stressed operating conditions.

Liquidity risk is managed using a forecasted cashflow approach measured over 30-day, 90-day and one-year periods. LGFA is required to maintain sufficient liquidity (comprising a government standby facility and holdings of cash and liquid investments) to support 12 months operating and funding commitments.

Interest rate risk / market risk

Interest rate risk is the risk that financial assets may re-price/ mature at a different time and/ or by a different amount than financial liabilities.

Interest rate / market risk is managed using Value at Risk (VaR) and Partial Differential Hedge (PDH) limits to mitigate the potential change in value of the balance sheet due to changes in interest rates.

- **Value at Risk** calculates the potential amount LGFA's portfolio could be expected to lose 5% of the time over a given time period. It is calculated using historical changes in underlying risk variables and applying those changes to the current portfolio.

LGFA measures VaR over a daily time horizon with a 95% confidence interval. A daily 95% VaR exposure of $1 million means that there is a 5% chance that the portfolio could potentially lose more than $1 million over the next business day.

- **Partial Differential Hedge** measures the sensitivity of a portfolio to a one basis point change in underlying interest rates. For example, a PDH of NZD$100,000 means that the portfolio value will increase by NZD$100,000 for a one basis point fall in interest rates.

In addition, LGFA also undertakes scenario analysis to model the potential effect of changing market environments on the balance sheet.

Counterparty credit risk

Counterparty credit risk is the risk of financial loss to LGFA arising from a counterparty defaulting on an investment, security and/or financial instrument where LGFA is a holder or party.

Counterparty credit risk is managed through counterparty limits for investments. These are determined as a function of the term of investment, liquidity and credit quality of the counterparty (as measured by credit rating).

Counterparty risk on derivative contracts is mitigated by transacting all derivative trades through the Treasury (New Zealand Debt Management) as the counterparty.

Investment is restricted to approved financial instruments listed in the Treasury Policy.

Foreign currency risk

Foreign currency risk is the risk of an adverse change in the fair value of a financial instrument due to a change in foreign exchange rates.

Exposure to foreign currency risk could exist if LGFA accesses foreign capital markets for funding purposes. To date, all funding has been sourced through New Zealand domestic currency.

Foreign exchange risk is managed through a requirement for LGFA to fully hedge back to floating rate NZD the full amount and term of all foreign currency funding and cash flows.

Operational risk

Operational risk, with respect to treasury management, is the risk of financial and/or reputation loss because of human error, fraud, negligent behaviour, system failures and inadequate procedures and controls.

Operational risk is managed using internal controls and procedures across LGFA's operational functions. Segregation of duties between staff members who have the authority to enter transactions with external counterparties and the staff who control, check and confirm such transactions is a cornerstone internal control principle.

Financial instruments are not entered into if the systems, operations and internal controls do not satisfactorily support the measurement, management and reporting of the risks.

Lending risk

As at 30 June 2020, LGFA provides debt funding solely to New Zealand Local Government councils. The Local Government borrowing counterparty will be the Council itself and will not be any Council-Controlled Organisation, Council-Controlled Trading Organisation, Council joint venture or partially owned entity.

The LGFA Board have ultimate discretion on approving term funding to councils.

All Local Authorities that borrow from LGFA:

- Provide debenture security in relation to their borrowing from LGFA and related obligations, and (if relevant), equity commitment liabilities to LGFA and (if relevant) guarantee liabilities to a security trustee approved for LGFA's creditors.
- If the principal amount of a Local Authority's borrowings is at any time equal to, or greater than, NZD 20 million, then it is required to become a party to a deed of guarantee and an equity commitment deed.
- Issue securities (bonds/floating rate notes/commercial paper) to LGFA (ie. not enter into facility arrangements).
- Comply with their own internal borrowing policies.

- Comply with the financial covenants outlined in the table below, provided that:
  - Unrated Local Authorities or Local Authorities with a long-term credit rating lower than 'A' equivalent can have bespoke financial covenants that exceed the:
    - Lending policy covenants outlined in the following table only with the approval of the Board;
    - Foundation policy covenants outlined in the following table only with the approval of an Ordinary Resolution of shareholders.
- Local Authorities with a long-term credit rating of 'A' equivalent or higher can have bespoke financial covenants that exceed the foundation policy covenants only with the approval of an Ordinary Resolution of shareholders.
- Any Board or Ordinary Resolution approval of bespoke financial covenants will only be provided after a robust credit analysis and any approval must also include bespoke reporting and monitoring arrangements.
- Non-compliance with the financial covenants will either preclude a council from borrowing from the LGFA or in the case of existing council borrowers trigger an event of review. An event of default will occur when (among other things) a council fails to meet an interest or principal payment (subject to grace periods). An event of default will enable the LGFA to accelerate a council's repayment of loans.
- Total revenue is defined as cash earnings from rates, government grants and subsidies, user charges, interest, dividends, financial and other revenue and excludes non-government capital contributions, eg. developer contributions and vested assets.
- Net debt is defined as total consolidated debt less liquid financial assets and investments.
- Liquidity is defined as external debt plus committed loan facilities plus liquid investments divided by external debt.
- Net interest is defined as the amount equal to all interest and financing costs less interest income for the relevant period.
- Annual rates income is defined as the amount equal to the total revenue from any funding mechanism authorised by the Local Government (Rating) Act 2002 together with any revenue received from other local governments for services provided and for which the other local governments rate.

Financial covenants are measured on a parent council only basis, not consolidated group, unless requested by a parent council and approved by the LGFA board.

To minimise concentration risk the LGFA will require that no more than the greater of NZD 100 million or 33% of a council's borrowings from the LGFA will mature in any 12-month period.

Auckland Council will be limited to a maximum of 40% of the LGFA's total Local Government assets.

Financial covenant	Lending policy covenants Unrated councils	Foundation policy covenants Rated councils
Net debt/ total revenue	<175%	<250%
Net interest / total revenue	<20%	<20%
Net interest/ annual rates income	<25%	<30%
Liquidity	>110%	>110%

On 30 June 2020 a Special General Meeting of Shareholders approved a change to the Net Debt/Total Revenue covenant contained within the Foundation Policy Covenants. For the financial year ending June 2020 a covenant limit of 250% applies. This increases to 300% for the June 2021 and June 2022 years and then reduces by 5% for each of the subsequent years until 280% applies from the June 2026 year.

Financial statements
Nga taukī pūtea

In the opinion of the directors of the New Zealand Local Government Funding Agency Limited, the financial statements and notes on pages 55 to 77:

- Comply with New Zealand generally accepted accounting practice (GAAP), New Zealand equivalents to International Financial Reporting Standards (NZIFRS) as appropriate for profit-oriented entities and give a true and fair view of the financial position of the Company as at 30 June 2020, and
- Have been prepared using appropriate accounting policies, which have been consistently applied and supported by reasonable judgements and estimates.
- The directors believe that proper accounting records have been kept which enables, with reasonable accuracy, the determination of the financial position of the Company and facilitates the compliance of the financial statements with the Financial Markets Conduct Act 2013 and the Financial Reporting Act 2013.

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

Craig Stobo
Chair, LGFA Board
28 August 2020

Linda Robertson
Chair, Audit and Risk Committee
28 August 2020

Statement of comprehensive income

For the year ended ended 30 June 2020 in $000s

	Note	Year ended 2020	Year ended 2019
Interest income			
Cash and cash equivalents		394	490
Marketable securities		4,462	4,118
Deposits		6,341	3,887
Derivatives		152,621	104,568
Loans		206,402	248,015
Fair value hedge ineffectiveness	2c	-	-
Total interest income		**370,220**	**361,078**
Interest expense			
Bills		6,632	9,519
Bond repurchase transactions		590	358
Lease liability		22	-
Bonds		341,783	328,907
Borrower notes		2,914	3,535
Total interest expense		**351,941**	**342,319**
Net interest income		**18,279**	**18,759**
Operating expenses			
Issuance and on-lending expenses	3	3,971	4,287
Operating expenses	4	3,685	3,271
Total expenses		**7,657**	**7,558**
Net operating profit		**10,623**	**11,201**
Total comprehensive income		**10,623**	**11,201**

Statement of changes in equity

For the year ended 30 June 2020 in $000s

	Note	Share capital	Retained earnings	Total equity
Equity as at 30 June 2018		**25,000**	**39,290**	**64,290**
Adjustment on adoption of NZ IFRS 9			(57)	(57)
Net operating profit			11,201	11,201
Total comprehensive income for the year			11,201	11,201
Transactions with owners			-	-
Dividend paid on 7 September 2018			(1,285)	(1,285)
Equity as at 30 June 2019		**25,000**	**49,149**	**74,149**
Net operating profit			10,623	10,623
Total comprehensive income for the year			10,623	10,623
Transactions with owners			-	-
Dividend paid on 6 September 2019			(1,155)	(1,155)
Equity as at 30 June 2020	**11**	**25,000**	**58,616**	**83,616**

Statement of financial position

As at 30 June 2020 in $000s

	Note	2020	2019
Assets			
Financial assets			
Cash and bank balances		165,826	56,198
Marketable securities		589,124	255,715
Deposits		499,824	136,216
Derivatives in gain	2d	1,018,775	622,559
Loans	5	10,899,756	9,310,617
Non-financial assets			
Prepayments		642	570
Other assets	12	419	457
Total assets		**13,174,365**	**10,382,332**
Equity			
Share capital	11	25,000	25,000
Retained earnings		58,616	49,149
Total equity		**83,616**	**74,149**
Liabilities			
Financial liabilities			
Payables and provisions		705	563
Bills	6	647,021	503,225
Bond repurchases	9	202,755	24,625
Derivatives in loss	2d	19,075	12,926
Bonds	7	12,038,468	9,612,394
Borrower notes	8	182,272	154,168
Non-financial liabilities			
Other liabilities		453	282
Total liabilities		**13,090,748**	**10,308,183**
Total equity and liabilities		**13,174,365**	**10,382,332**

Statement of cash flows

For the year ended 30 June 2020 in $000s

	Note	Year Ended 2020	Year Ended 2019
Cash Flow from Operating Activities			
Cash applied to loans		(1,556,491)	(1,330,360)
Interest paid on bonds issued		(381,666)	(385,850)
Interest paid on bills issued		(6,609)	(9,516)
Interest paid on borrower notes		(745)	(2,874)
Interest paid on bond repurchases		(333)	(341)
Interest received from loans		223,829	244,079
Interest received from cash & cash equivalents		372	490
Interest received from marketable securities		6,729	3,742
Interest received from deposits		5,713	4,786
Net interest on derivatives		171,367	160,664
Payments to suppliers and employees		(7,452)	(7,420)
Net cash flow from operating activities	10	**(1,545,287)**	**(1,322,601)**
Cashflow from Investing Activities			
Purchase of marketable securities		(335,676)	(24,513)
Purchase of deposits		(362,980)	64,000
Net Cashflow from Investing Activities		**(698,656)**	**39,487**
Cashflow from Financing Activities			
Cash proceeds from bonds issued		2,146,925	1,255,337
Cash proceeds from bills issued		143,773	29,802
Cash proceeds from bond repurchases		177,874	18,425
Cash proceeds from borrower notes		(24,066)	18,400
Dividends paid		(1,155)	(1,285)
Cash applied to derivatives		(89,782)	(31,647)
Net Cashflow from Financing Activities		**2,353,570**	**1,289,032**
Net (Decrease) / Increase in Cash		**109,627**	**5,918**
Cash, Cash Equivalents and Bank overdraft at beginning of year		56,198	50,281
Cash, Cash Equivalents and Bank overdraft at end of year		**165,826**	**56,198**

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 2020.

These financial statements were authorised for issue by the Directors on 28 August 2020.

b. Statement of compliance

LGFA is an FMC reporting entity under the Financial Markets Conduct Act 2013 (FMCA). These financial statements have been prepared in accordance with that Act and the Financial Reporting Act 2013. LGFA's bonds are quoted on the NZX Debt Market.

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) and 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

NZ IFRS 16 Leases

NZ IFRS 16 became effective from 1 July 2019 and did not have a material impact on the financial statements.

On adoption of NZ IFRS 16, LGFA recognised right-of-use assets and lease liabilities in relation to its property leases which had previously been classified as operating leases under NZ IAS 17 Leases.

In adopting NZ IFRS 16, LGFA elected to use the simplified retrospective approach which does not require restatement of comparative information. The lease liability is recognised at the present value of the remaining lease payments, discounted using LGFA's incremental borrowing rate, with the corresponding right-of-use asset recognised as an equal amount.

The following items in the balance sheet were impacted by the change of accounting on 1 July 2019: Other assets and Other liabilities both increased by $0.157 million.

Lease payments previously included in other operating expense are now classified to financing and depreciation costs under NZ IFRS 16.

There have been no other changes to accounting policies.

Early adoption standards and interpretations

LGFA has not early adopted any standards.

New standards adopted

NZ IFRS 16 Leases became effective from 1 July 2019.

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.

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 and 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 expected credit loss assessment is performed for all financial assets and is calculated as either:

- Credit losses that may arise from default events that are possible within the next 12 months, where no significant increase in credit risk has arisen since acquisition of the asset, or
- Credit losses that may arise from default events that are possible over the expected life of the financial asset, where a significant increase in credit risk has arisen since acquisition of the asset.

Impairment losses on financial assets will ordinarily be recognised on initial recognition as a 12-month expected loss allowance and move to a lifetime expected loss allowance if there is a significant deterioration in credit risk since acquisition.

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 (three to seven 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. Segment reporting

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

i. Judgements and estimations

The preparation of these financial statements requires judgements, estimates and assumptions that affect the application of policies and reported amounts. For example, the fair value of financial instruments depends critically on judgements regarding future cash flows, including inflation assumptions and the risk-free discount rate. Refer note 2a.

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 and these estimates and underlying assumptions are reviewed on an ongoing basis. Where these judgements significantly affect the amounts recognised in the financial statements they are described in the following notes.

The financial statements at 30 June 2020 include estimates and judgements of the potential impact of COVID-19 on LGFA's financial position and performance. Whilst there has been no material impact on the estimates and judgements at the date these financial statements are authorised, it is noted that there is significant uncertainty with regards to the medium and long-term effects of COVID-19 on the local government sector.

2 Analysis of financial assets and financial liabilities

a. Categories of financial instruments

Derivative financial instruments are the only instruments recognised in the statement of financial position at fair value.

Derivative financial instruments are valued under level 2 of 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 and other receivables, trade and other payables

The carrying value of cash and bank, trade and other receivables, trade and 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

The fair value of loans 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 following table shows the fair value of financial assets and financial liabilities, together with the carrying amounts shown in the statement of financial position.

As at 30 June 2020 in $000s	Financial liabilities at amortised cost	Financial assets at amortised cost	Financial assets measured at fair value in accordance with NZ IFRS 9	Fair value
Financial assets				
Cash and bank balances	-	165,826	-	165,826
Trade and other receivables	-	-	-	-
Marketable securities	-	589,124	-	591,617
Deposits	-	499,824	-	501,625
Derivatives	-	-	1,018,775	1,018,775
Loans	-	10,899,756	-	12,713,917
	-	**12,154,529**	**1,018,775**	**14,991,758**
Financial liabilities				
Payables and provisions	705	-	-	705
Bills	647,021	-	-	647,235
Bond repurchases	202,755	-	-	202,879
Derivatives	-	-	19,075	19,075
Bonds	12,038,468	-	-	12,196,826
Borrower notes	182,272	-	-	186,725
	13,071,221	**-**	**19,075**	**13,253,445**

As at 30 June 2019 in $000s	Financial liabilities at amortised cost	Financial assets at amortised cost	Financial assets measured at fair value in accordance with NZ IFRS 9	Fair value
Financial assets				
Cash and bank balances	-	56,198	-	56,198
Trade and other receivables	-	-	-	-
Marketable securities	-	255,715	-	257,124
Deposits	-	136,216	-	137,355
Derivatives	-	-	622,559	622,559
Loans	-	9,310,617	-	9,640,053
	-	**9,758,746**	**622,559**	**10,713,289**
Financial liabilities				
Payables and provisions	563	-	-	563
Bills	503,225	-	-	503,451
Bond repurchases	24,625	-	-	24,625
Derivatives	-	-	12,926	12,926
Bonds	9,612,394	-	-	9,727,610
Borrower notes	154,168	-	-	155,935
	10,294,975	**-**	**12,926**	**10,425,110**

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 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 using Value at Risk (VaR) and Partial Differential Hedge (PDH) limits to mitigate the potential change in value of the balance sheet due to changes in interest rates. PDH risk measures the sensitivity of a portfolio to a one basis point change in underlying interest rates, whereas VaR measures the expected loss for a given period with a given confidence.

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

As at 30 June 2020 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	165,826	165,826	-	-	-	-
Marketable securities	576,298	335,758	112,903	18,214	109,423	-
Deposits	497,980	397,980	100,000	-	-	-
Loans	10,868,876	9,118,964	529,990	153,300	532,200	534,423
Financial liabilities						
Bills	(647,500)	(647,500)	-	-	-	-
Bond repurchases	(202,478)	(202,478)	-	-	-	-
Derivatives	-	(9,347,750)	1,014,500	1,065,000	3,735,250	3,533,000
Bonds	(10,990,000)	(130,000)	(1,450,000)	(1,155,000)	(4,207,000)	(4,048,000)
Borrower notes	(168,845)	(141,197)	(8,130)	(2,453)	(8,515)	(8,551)
Total	**100,157**	**(450,397)**	**299,263**	**79,061**	**161,358**	**10,872**

As at 30 June 2019 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	56,198	56,198	-	-	-	-
Marketable securities	253,972	203,850	40,122	10,000	-	-
Deposits	135,000	55,000	80,000	-	-	-
Loans	9,262,858	8,030,980	16,520	452,700	284,700	477,958
Financial liabilities						
Bills	(505,000)	(480,000)	(25,000)	-	-	-
Bond repurchases	(24,604)	(24,604)	-	-	-	-
Derivatives	-	(7,715,000)	938,750	1,027,500	2,828,750	2,920,000
Bonds	(8,935,000)	-	(980,000)	(1,450,000)	(3,110,000)	(3,395,000)
Borrower notes	(142,027)	(122,333)	(248)	(7,243)	(4,555)	(7,647)
Total	**101,398**	**4,091**	**70,144**	**32,957**	**(1,105)**	**(4,689)**

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 in $000s	2020		2019	
	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	484,492	(493,186)	(369,387)	376,054
Derivative financial instruments	(483,279)	491,932	369,387	(376,054)
	1,213	**(1,254)**	**-**	**-**
Cash flow sensitivity analysis				
Variable rate assets	89,636	(89,636)	76,708	(76,708)
Variable rate liabilities	(2,712)	2,712	(1,227)	1,227
Derivative financial instruments	(93,608)	93,608	(79,320)	79,320
	(6,684)	**6,684**	**(3,839)**	**3,839**

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 single counterparty.

Exposure to credit risk

LGFA monitors the concentration of credit risk by the type of counterparty. The following table shows 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.

As at 30 June 2020 in $000s	NZ government agencies	NZ local authorities	NZ registered banks	Other counter-parties	Total carrying value
Financial assets					
Cash and bank balances	165,070	-	756	-	165,825
Trade and other receivables	-	-	-	-	-
Marketable securities	123,615	52,181	89,868	323,460	589,124
Deposits	-	-	459,783	40,041	499,824
Derivatives	999,700	-	-	-	999,700
Loans	-	10,899,756	-	-	10,899,756
	1,288,385	**10,951,937**	**550,406**	**363,501**	**13,154,229**

As at 30 June 2019 in $000s	NZ government agencies	NZ local authorities	NZ registered banks	Other counter-parties	Total carrying value
Financial assets					
Cash and bank balances	55,679	-	520	-	56,198
Trade and other receivables	-	-	-	-	-
Marketable securities	40,962	48,668	135,597	30,488	255,715
Deposits	-	-	136,216	-	136,216
Derivatives	609,632	-	-	-	609,632
Loans	-	9,310,617	-	-	9,310,617
	706,273	**9,359,285**	**272,333**	**30,488**	**10,368,378**

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 nor 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. LGFA is required by policy to maintain sufficient liquidity (comprising a committed liquidity facility and holdings of cash and liquid investments) to meet all operating and funding commitments over a rolling 12-month period.

The Treasury (New Zealand Debt Management) provides a committed liquidity facility that LGFA can draw upon to meet any exceptional and temporary liquidity shortfall. As at 30 June 2020, the undrawn committed liquidity facility was $700 million (2019: $700 million). The facility is due to expire in December 2021.

Contractual cash flows of financial instruments.

The following table shows the contractual cash flows associated with financial assets and liabilities.

As at 30 June 2020 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	165,826	-	-	-	-	165,826	165,826
Trade and other receivables	-	-	-	-	-	-	-
Marketable securities	-	194,160	222,916	175,954	-	593,029	589,124
Deposits	-	289,288	212,759	-	-	502,048	499,824
Loans	-	224,293	1,902,829	6,047,790	3,355,153	11,530,065	10,899,756
Financial liabilities							
Payables and provisions	(705)	-	-	-	-	-	(705)
Bills	-	(530,500)	(117,000)	-	-	(647,500)	(647,021)
Bond repurchases	-	(102,752)	(100,276)	-	-	(203,028)	(202,755)
Bonds	-	(483)	(1,843,131)	(6,420,275)	(4,512,260)	(12,776,150)	(12,038,468)
Borrower notes	-	(438)	(31,198)	(99,957)	(59,551)	(191,144)	(182,272)
Derivatives	-	(21,309)	266,054	554,255	265,760	1,064,760	999,700
	165,121	**52,258**	**512,953**	**257,766**	**(950,898)**	**37,904**	**83,008**

As at 30 June 2019 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	56,198	-	-	-	-	56,198	56,198
Trade and other receivables							
Marketable securities	-	127,363	52,615	80,815	-	260,793	255,715
Deposits	-	-	138,543	-	-	138,543	136,216
Loans	-	279,328	936,604	5,556,479	3,583,112	10,355,524	9,310,617
Financial liabilities							
Payables and provisions	(563)	-	-	-	-	(563)	(563)
Bills	-	(330,000)	(175,000)	-	-	(505,000)	(503,225)
Bond repurchases	-	(24,628)	-	-	-	(24,628)	(24,625)
Bonds	-	-	(1,338,293)	(5,495,770)	(3,838,283)	(10,672,345)	(9,612,394)
Borrower notes	-	(332)	(10,820)	(92,580)	(65,981)	(169,713)	(154,168)
Derivatives	-	(42,732)	183,130	358,542	154,427	653,366	609,632
	55,635	**8,998**	**(213,220)**	**407,487**	**(166,724)**	**92,176**	**73,403**

c. Hedge accounting

LGFA is exposed to interest rate risk from fixed rate borrowing and variable rate lending to councils. LGFA uses interest rate swaps to manage this interest rate risk. For hedge accounting purposes, LGFA has designated these swaps in fair value relationships to its fixed rate borrowings and loans.

The following table shows the gain or loss on the hedging instrument and the hedged item attributable to the hedged risk for fair value hedge relationships.

For the year ended ended 30 June in $000s	2020 Gain/(loss)	2019 Gain/(loss)
Hedging instruments – interest rate swaps	319,032	312,996
Hedged items attributable to the hedged risk – fixed rate bonds	(319,032)	(312,996)
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 or loans) 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 the 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 2020 in $000s	Derivative assets	Derivative liabilities
Gross amounts	1,018,775	19,075
Amounts offset	-	-
Carrying amounts	1,018,775	19,075
Amounts that don't qualify for offsetting	-	-
Financial assets & liabilities	(19,075)	(19,075)
Collateral	-	-
Net amount	**999,700**	**-**

As at 30 June 2019 in $000s	Derivative assets	Derivative liabilities
Gross amounts	622,559	12,926
Amounts offset	-	-
Carrying amounts	622,559	12,926
Amounts that don't qualify for offsetting	-	-
Financial assets & liabilities	(12,926)	(12,926)
Collateral	-	-
Net amount	**609,633**	**-**

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 in $000s	2020	2019
NZDM facility fee	650	644
NZX	559	455
Rating agency fees	609	596
Legal fees for issuance	499	493
Regulatory, registry, other fees	157	147
Trustee fees	100	100
Approved issuer levy[1]	1,396	1,708
Information services[2]	-	144
	3,971	**4,287**

1. The amount of Approved Issuer Levy is a function of the number of the offshore holders of certain LGFA bond maturities.
2. From 1 July 2019, information services costs are reported under Information Technology in Operating Expenses (Note 4)

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 in $000s	2020	2019
Information technology[1]	689	-
Consultants	127	205
Directors fees	399	377
Insurance	78	65
Legal fees	139	84
Other expenses	354	796
Auditors' remuneration		
Statutory audit	103	96
Advisory services	-	-
Personnel	1,798	1,648
	3,685	**3,271**

1. Information technology aggregates all LGFA information technology-related expenses under a single category. Previously, these expenses were recorded across information services, consultants and other expenses.

5 Loans

As at 30 June in $000s	2020 Short-term loans	2020 Loans	2019 Short-term loans	2019 Loans
Ashburton District Council	10,001	32,279	10,025	27,465
Auckland Council	-	2,766,155	-	2,422,898
Bay of Plenty Regional Council	-	192,077	90,974	50,631
Buller District Council	-	20,005	-	20,013
Canterbury Regional Council	6,002	48,129	6,006	32,108
Central Hawkes Bay District Council	-	20,107	-	2,027
Christchurch City Council	25,094	1,904,271	27,110	1,721,759
Clutha District Council	2,003	7,030	-	5,020
Far North District Council	10,001	46,686	-	40,149
Gisborne District Council	-	58,754	5,982	42,819
Gore District Council	6,004	16,538	6,011	13,059
Greater Wellington Regional Council	-	425,877	-	401,676
Grey District Council	3,967	15,196	4,978	15,305
Hamilton City Council	-	481,064	-	356,737
Hastings District Council	-	150,335	-	105,985
Hauraki District Council	-	44,102	-	38,192
Hawkes Bay Regional Council	-	2,507	-	2,509
Horizons Regional Council	6,987	37,199	-	35,182
Horowhenua District Council	16,003	90,618	11,006	85,780
Hurunui District Council	8,005	30,065	-	32,140
Hutt City Council	-	216,523	-	179,746
Invercargill City Council	25,013	65,165	25,093	30,095
Kaikoura District Council	4,007	3,008	-	-
Kaipara District Council	-	44,089	999	44,189
Kapiti Coast District Council	-	210,353	-	210,804
Manawatu District Council	11,519	65,669	-	68,229
Marlborough District Council	27,224	73,157	26,545	73,252
Masterton District Council	-	51,215	-	50,248
Matamata-Piako District Council	-	26,561	2,546	21,597
Nelson City Council	-	75,118	-	65,264
New Plymouth District Council	-	139,939	-	99,535
Northland Regional Council	-	9,729	-	9,728
Opotiki District Council	-	8,620	-	5,125
Otorohanga District Council	-	3,035	-	3,048

5 Loans (cont)

As at 30 June in $000s	2020 Short-term loans	2020 Loans	2019 Short-term loans	2019 Loans
Palmerston North City Council	-	137,267	10,024	104,439
Porirua City Council	-	131,787	-	86,894
Queenstown Lakes District Council	20,027	95,525	20,076	85,644
Rangitikei District Council	-	3,020	-	3,013
Rotorua District Council	22,855	195,105	2,817	180,186
Ruapehu District Council	8,005	17,061	3,027	13,070
Selwyn District Council	-	35,092	5,097	10,053
South Taranaki District Council	-	101,232	-	80,383
South Wairarapa District Council	-	22,018	-	20,023
Stratford District Council	-	15,571	1,003	13,570
Taranaki Regional Council	3,992	-	-	-
Tararua District Council	2,006	33,080	4,020	21,104
Tasman District Council	31,143	177,039	25,380	127,172
Taupo District Council	-	115,177	-	115,452
Tauranga City Council	-	526,768	9,963	432,609
Thames-Coromandel District Council	-	61,147	-	51,244
Timaru District Council	22,577	67,203	17,568	67,313
Upper Hutt City Council	2,993	46,108	4,975	38,174
Waikato District Council	-	95,222	-	80,400
Waikato Regional Council	-	32,085	-	22,120
Waimakariri District Council	-	160,550	10,010	135,872
Waipa District Council	13,503	40,053	-	15,013
Wairoa District Council	-	9,045	1,514	3,519
Waitomo District Council	7,022	30,044	10,055	30,093
Wellington City Council	-	635,684	-	533,151
West Coast Regional Council	2,001	6,610	1,985	5,608
Western Bay of Plenty District Council	-	90,212	-	90,478
Westland District Council	-	19,652	-	18,688
Whakatane District Council	-	67,178	5,008	57,298
Whanganui District Council	7,510	94,290	-	73,408
Whangarei District Council	9,992	142,301	9,976	122,543
	315,456	**10,584,299**	**359,771**	**8,950,846**

As at 30 June 2020, $1,960 million of loans are due to mature within 12 months. This comprises all short-term loans and $1,645 million of loans.

6 Bills on issue

As at 30 June 2020 in $000's	Face value	Unamortised premium	Accrued interest	Total
8 July 2020	110,000	-	(21)	109,979
17 July 2020	58,500	-	(31)	58,469
22 July 2020	12,000	-	(9)	11,991
6 August 2020	225,000	-	(102)	224,898
12 August 2020	75,000	-	(79)	74,921
9 September 2020	50,000	-	(59)	49,941
7 October 2020	17,000	-	(36)	16,964
11 November 2020	50,000	-	(63)	49,937
9 December 2020	25,000	-	(37)	24,963
15 December 2020	25,000	-	(43)	24,957
	647,500	**-**	**(479)**	**647,021**

As at 30 June 2019 in $000's	Face value	Unamortised premium	Accrued interest	Total
4 July 2019	25,000	-	(4)	24,996
10 July 2019	85,000	-	(41)	84,959
17 July 2019	25,000	-	(23)	24,977
29 July 2019	25,000	-	(35)	24,965
5 August 2019	25,000	-	(48)	24,952
14 August 2019	50,000	-	(109)	49,891
23 August 2019	45,000	-	(117)	44,883
11 September 2019	50,000	-	(174)	49,826
4 October 2019	25,000	-	(124)	24,876
9 October 2019	25,000	-	(125)	24,875
7 November 2019	25,000	-	(168)	24,832
13 November 2019	25,000	-	(159)	24,841
4 December 2019	25,000	-	(203)	24,797
11 December 2019	25,000	-	(180)	24,820
22 January 2020	25,000	-	(266)	24,734
	505,000	**-**	**(1,775)**	**503,225**

7 Bonds on issue

Bonds on issue do not include $800 million face value of issued LGFA bonds subscribed by LGFA and held as treasury stock. Refer Note 9: Treasury stock and bond repurchase transactions.

As at 30 June 2020 in $000's	Face Value	Unamortised premium	Accrued interest	Fair value hedge adjustment	Total
Fixed interest bonds					
15 May 2021	1,450,000	19,259	11,111		
14 April 2022	1,155,000	16,630	6,769		
15 April 2023	1,550,000	55,449	17,935		
15 April 2024	1,248,000	6,717	5,908		
15 April 2025	1,409,000	(31,014)	8,152		
15 April 2026	1,000,000	763	3,156		
15 April 2027	1,326,000	56,918	12,554		
20 April 2029	692,000	(14,904)	2,042		
14 April 2033	1,030,000	8,706	7,683		
Total fixed interest	**10,860,000**	**118,524**	**75,309**	**854,268**	**11,908,100**
Floating rate notes					
14 October 2022	130,000	(58)	426	-	130,368
Total	**10,990,000**	**118,465**	**75,735**	**854,268**	**12,038,468**

As at 30 June 2019 in $000's	Face Value	Unamortised premium	Accrued interest	Fair value hedge adjustment	Total
15 April 2020	980,000	(2,674)	6,185		
15 May 2021	1,450,000	40,569	11,111		
14 April 2022	710,000	5,876	4,161		
15 April 2023	1,450,000	56,972	16,778		
15 April 2024	950,000	(3,895)	4,497		
15 April 2025	1,379,000	(38,648)	7,978		
15 April 2027	1,276,000	51,179	12,080		
14 April 2033	740,000	(35,533)	5,520		
Total	**8,935,000**	**73,848**	**68,311**	**535,236**	**9,612,394**

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.

9 Treasury stock and bond repurchase transactions

Periodically, LGFA subscribes for LGFA bonds as part of its tender process and holds these bonds as treasury stock. LGFA bonds held by LGFA as treasury stock are derecognised at the time of issue and no liability is recognised in the statement of financial position. As at 30 June 2020, $800 million of LFGA bonds had been subscribed as treasury stock.

LGFA makes these treasury stock bonds available to banks authorised as its tender counterparties to borrow under short-term repurchase transactions. The objective of the bond lending facility is to assist with improving secondary market liquidity in LGFA bonds. Bonds lent to counterparties are disclosed as a separate stock lending liability on the face of the statement of financial position.

As at 30 June 2020, bond repurchase transactions comprised:

in $000s	30 June 2020	30 June 2019
15 May 2021	25,970	-
14 April 2022	25,196	15,535
15 April 2023	27,670	-
15 April 2024	25,139	-
15 April 2025	22,135	-
15 April 2026	-	-
15 April 2027	31,145	5,837
20 April 2029	22,899	-
14 April 2033	22,600	3,252
	202,755	**24,624**

10 Reconciliation of net profit to net cash flow from operating activities

For the year ended 30 June in $000s	2020	2019
Net profit/(loss) for the period	10,603	11,201
Cash applied to loans	(1,556,491)	(1,330,360)
Non-cash adjustments		
Amortisation and depreciation	528	(3,428)
Working capital movements		
Net change in trade debtors and receivables	87	62
Net change in prepayments	(72)	(9)
Net change in accruals	58	(66)
Net Cash From Operating Activities	**(1,545,287)**	**(1,322,601)**

11 Share Capital

As at 30 June 2020, 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 2020	2020		2019	
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	3,731,958	8.3%	3,731,958	8.3%
Greater Wellington Regional Council	3,731,958	8.3%	3,731,958	8.3%
Tasman District Council	3,731,958	8.3%	3,731,958	8.3%
Tauranga City Council	3,731,958	8.3%	3,731,958	8.3%
Wellington City Council	3,731,958	8.3%	3,731,958	8.3%
Western Bay of Plenty District Council	3,731,958	8.3%	3,731,958	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 District 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

LGFA paid a dividend of $1,155,000 on 6 September 2019, being $0.0462 per paid up share (2019: $1,285,000 on 7 September 2018, being $0.0514 per paid up share).

12 Other assets

As at 30 June in $000s	2020	2019
Intangible assets[1]	306	457
Right-of-use lease asset	113	-
Total other assets	**419**	**457**

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

13 Capital commitments

As at 30 June 2020, there are no capital commitments.

14 Contingencies

There are no contingent liabilities at balance date.

15 Related parties

Identity of related parties

LGFA is related to the local authorities set out in the Shareholder Information in note 11.

LGFA operates under an annual Statement of Intent with the respective local authorities that sets out the intentions and expectations for LGFA's operations and lending to participating local authorities.

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. Refer note 8.

The Treasury (New Zealand Debt Management) provides LGFA with a committed credit facility and is LGFA's derivatives counterparty.

Transactions with key management personnel:

Salaries $951,900 (2019: $904,300)

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

16 Subsequent events

On 6 July 2020 the group of Participating Local Authorities approved changes to the Multi Issuer Deed, Guarantee and Indemnity Deed and Notes Subscription Agreement. This allowed LGFA to lend to CCOs and CCTO's, and permitted an increase in the Borrower Notes Percentage from 1.6% to 2.5% of a member council's borrowings.

On 11 August 2020, the Minister of Finance and LGFA signed an amendment to the Crown Liquidity Facility that extends the term of the facility to 31 December 2031 (from 31 December 2021) and increases the size of the facility to $1.5 billion (from $1 billion).

On 28 August 2020, the Directors of LGFA declared a dividend of $878,500 ($0.03514 per paid up share).

Subsequent to balance date, LGFA has issued $1.2 billion in bonds (including $100 million of treasury stock).

INDEPENDENT AUDITOR'S REPORT

TO THE READERS OF NEW ZEALAND LOCAL GOVERNMENT FUNDING AGENCY LIMITED'S FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION FOR THE YEAR ENDED 30 JUNE 2020

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

Opinion

We have audited:

- the financial statements of the company on pages 55 to 77, that comprise the statement of financial position as at 30 June 2020, 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 10 to 17.

In our opinion:

- the financial statements of the company on pages 55 to 77:
  - present fairly, in all material respects:
    - its financial position as at 30 June 2020; 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 Accepted Accounting Practice (NZ GAAP) and they comply with New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS); and
- the performance information of the company on pages 10 to 17 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 2020.

Our audit was completed on 28 August 2020. This is the date at which our opinion is expressed.

The basis for our opinion is explained below. In addition, we outline the responsibilities of the Board of Directors and our responsibilities relating to the financial statements and the performance information, we comment on other information, and we explain our independence.

Basis for our opinion

We carried out our audit in accordance with the Auditor-General's Auditing Standards, which incorporate the Professional and Ethical Standards and the International Standards on Auditing (New Zealand) issued by the New Zealand Auditing and Assurance Standards Board. Our responsibilities under those standards are further described in the Responsibilities of the auditor section of our report.

We have fulfilled our responsibilities in accordance with the Auditor-General's Auditing Standards.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Materiality

The scope of our audit was influenced by our application of materiality. Materiality helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole. The materiality for the financial statements as a whole was set at $85 million determined with reference to a benchmark of company Total Assets. We chose the benchmark because, in our view, this is a key measure of the company's performance. In addition, we also assess whether other matters that come to our attention during the audit would in our judgement change or influence the decisions of a reasonably knowledgeable person ('qualitative' materiality).

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements in the current period. We summarise below those matters and our key audit procedures to address those matters in order that the readers as a body may better understand the process by which we arrived at our audit opinion. Our procedures were undertaken in the context of and solely for the purpose of our statutory audit opinion on the financial statements as a whole and we do not express discrete opinions on separate elements of the financial statements.

The key audit matter	How the matter was addressed in our audit
Existence and impairment of loans	
Refer to Note 5 to the Financial Statements. The loans LGFA has provided to local government make up over 83% of total assets. The loans are recognised at amortised cost and the nature of the counterparties is such that we do not consider these loans to be at high risk of significant misstatement. However, based on their materiality, and the judgement involved in assessing the credit worthiness of counterparties they are considered to be the area which had the greatest effect on our overall audit strategy and allocation of resources in planning and completing our audit. In addition, the Covid-19 pandemic has created significant additional risks across a number of areas of the business, particularly the assessment of the provision for credit impairments. All forward looking assumptions are inherently more uncertain during these unprecedented times. While this key audit matter is unchanged from last year, the underlying audit risk has increased which impacted the extent and nature of audit evidence that we had to gather.	Our audit procedures included: - understanding the processes in place to assess borrowers and to record loan transactions. This included evaluating the control environment in place at LGFA. - agreeing the 30 June 2020 loan balances to external confirmations received from NZ Clear. - assessing the borrowers' compliance with financial covenants. We did not identify any material differences in relation to the existence or impairment of loans.
Application of hedge accounting	
Refer to Note 2 of the Financial Statements. LGFA enters into derivatives (interest rate swaps) to manage interest rate risk related to issuing fixed rate bonds. Fair value hedge accounting is applied where specific requirements are met around documentation of the hedge relationship and the relationship is demonstrated as being an effective hedge. Hedge accounting is complex, particularly in the area of whether the requirements (both initial and ongoing) for its application are met. Should the requirements for hedge accounting not be met, LGFA could experience significant volatility in the Statement of Comprehensive Income from changes in the fair value of the derivatives. Due to the size of the derivative positions and the complexity of hedge accounting we consider this to be a key audit matter.	Our audit procedures included: - reviewing LGFA's accounting policies related to financial instruments. - agreeing the terms of the derivatives to the confirmation provided by the derivative counterparty. - using our treasury valuation specialists we independently recalculated the fair value of all of the derivatives recorded by LGFA. - ensuring the hedge documentation supporting the application of hedge accounting was in accordance with NZ IFRS 9 and the disclosures made in the financial statements were appropriate. - determining that management's hedge effectiveness calculations were correctly performed using appropriate source information. We did not identify any material differences in relation to the application of hedge accounting.

Responsibilities of the Board of Directors for the financial statements and the performance information

The Board of Directors is responsible on behalf of the company for preparing financial statements that are fairly presented and that comply with generally accepted accounting practice in New Zealand in accordance with NZ IFRS and IFRS. The Board of Directors is also responsible for preparing the performance information for the company.

The Board of Directors is responsible for such internal control as it determines is necessary to enable it to prepare financial statements and performance information that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements and the performance information, the Board of Directors is responsible on behalf of the company for assessing the company's ability to continue as a going concern. The Board of Directors is also responsible for disclosing, as applicable, matters related to going concern and using the going concern basis of accounting, unless the Board of Directors intends to liquidate the company or to cease operations, or has no realistic alternative but to do so.

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

Responsibilities of the auditor for the audit of the financial statements and the performance information

Our objectives are to obtain reasonable assurance about whether the financial statements and the performance information, as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit carried out in accordance with the Auditor-General's Auditing Standards will always detect a material misstatement when it exists. Misstatements are differences or omissions of amounts or disclosures, and can arise from fraud or error. Misstatements are considered material if, individually or in the aggregate, they could reasonably be expected to influence the decisions of readers, taken on the basis of these financial statements and the performance information.

For the budget information reported in the financial statements and the performance information, our procedures were limited to checking that the information agreed to the company's statement of intent.

We did not evaluate the security and controls over the electronic publication of the financial statements and the performance information.

As part of an audit in accordance with the Auditor-General's Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. Also:

- We identify and assess the risks of material misstatement of the financial statements and the performance information, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- We obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control.
- We evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors.
- We evaluate the appropriateness of the reported performance information within the company's framework for reporting its performance.
- We conclude on the appropriateness of the use of the going concern basis of accounting by the Board of Directors and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the company's ability to continue as a going concern. If we conclude that a material uncertainty exists we are required to draw attention in our

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auditor's report to the related disclosures in the financial statements and the performance information or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the company to cease to continue as a going concern.

- We evaluate the overall presentation, structure and content of the financial statements and the performance information, including the disclosures, and whether the financial statements and the performance information represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Board of Directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Our responsibilities arise from the Public Audit Act 2001.

Other Information

The Board of Directors is responsible for the other information. The other information comprises the information included on pages 4 to 9, 18 to 54 and 82 to 86, but does not include the financial statements and the performance information, and our auditor's report thereon.

Our opinion on the financial statements and the performance information does not cover the other information and we do not express any form of audit opinion or assurance conclusion thereon.

In connection with our audit of the financial statements and the performance information, our responsibility is to read the other information. In doing so, we consider whether the other information is materially inconsistent with the financial statements and the performance information or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on our work, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Independence

We are independent of the company in accordance with the independence requirements of the Auditor-General's Auditing Standards, which incorporate the independence requirements of Professional and Ethical Standard 1(Revised): Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board.

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

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

Motuoapa Reservoir.
Taupo District Council

Other disclosures
He whākitanga anō

Donations

A donation of $3000 was made to Kauri 2000 for the year ended 30 June 2020.

Net Tangible Assets

Net tangible assets per $1,000 of listed bonds as at 30 June 2020 is $7.09 (2019: $7.95).

Earnings per security

Earnings per $1,000 of bonds on issue as at 30 June 2020 is $0.90 (2019: $1.20).

Amount per security of final dividends

Not applicable

Spread of Quoted Security holders

Holding Range	Holder Count	Holder Count %	Holding Quantity	Holding Quantity %
10,000 to 49,999	355	39.1	$9,098,000	0.08
50,000 to 99,999	194	21.4	$13,712,000	0.12
100,000 to 499,999	238	26.2	$47,730,000	0.41
500,000 to 999,999	38	4.2	$25,566,000	0.22
1,000,000 to 9,999,999,999,999	83	9.1	$11,563,894,000	99.17
Total	**908**	**100.0**	**$11,660,000,000**	**100.00**

Newly built Waverley Water Treatment Plant at a cost of $2.1m.
South Taranaki District Council

GRI Index
Tāpiritanga GRI

The GRI Standards are the world's most widely used sustainability reporting standard.

This is the first year LGFA has prepared its annual report in compliance with the GRI Standards. The following index is based on the GRI core option.

Disclosure title	Reference/Disclosure
102-1. Name of the organisation	Page 18
102-2. Activities, brands, products and services	Pages 18-27
102-3. Location of headquarters	Page 87
102-4. Location of operations	Page 87
102-5. Ownership and legal form	Pages 18, 59
102-6. Markets served	Pages 4-6, 10-17, 18-27, New Zealand
102-7. Scale of the organisation	Pages 4-6, 18-32, 57
102-8. Information on employees and other workers	Pages 45, 47, 77
102-9. Supply chain	Pages 18-27
102-10. Significant changes to the organization and its supply chain	None.
102-11. Precautionary Principle or approach	Page 38
102-12. External initiatives	Page 40
102-13. Membership of Associations	Financial Service Providers Register
102-14. Statement from senior decision-maker	Pages 4-6
102-16. Values, principles, standards, and norms of behaviour	Pages 40-49
102-18. Overview of Governance Structure	Page 19
102-40. List of stakeholder groups	Pages 4-7, 10-16, 28-33, 49
102-41. Collective bargaining agreements	None.
102-42. Identifying and selecting stakeholders	Page 34
102-43. Approach to stakeholder engagement	Pages 4-6, 15, 34
102-44. Key topics and concerns raised	Page 34
102-45. Entities included in the consolidated financial statements	Page 59
102-46. Defining report content and topic Boundaries	Page 34
102-47. List of material topics	Pages 34-36
102-48. Restatements of information	None
102-49. Changes in reporting	None

102-50. Reporting period	1 July 2019 to 30 June 2020
102-51. Date of most recent report	2019 Annual Report
102-52. Reporting cycle	Annual
102-53. Contact point for questions regarding the report	lgfa@lgfa.co.nz
102-54. Claims of reporting in accordance with the GRI Standards	The report has been prepared in accordance with the GRI Standards: Core option
102-55. GRI content index	Page 85
102-56. External assurance	None
Cost effective funding	Pages 4-6, 10-17, 28
Culture, ethics and governance	Pages 34-36, 40-49
Transparency and disclosure	Pages 4-6, 34-36, 40-49, 50-53
Environmental and social impact of lending	Pages 4-6, 34-36, 38-39
Health & safety and wellbeing	Pages 11, 16-17, 34-36, 48
Collaboration and local engagement	Pages 4-6, 15, 34-36
Financial markets best practice and influence	Pages 4-6, 10-17, 40-53
Diversity and inclusion	Pages 4-6, 45
Capability and development	Pages 4-6, 45
Carbon footprint	Pages 34-36
Health and Safety and Wellbeing	
403-1 Occupational health and safety management system	Page 48
403-9 Work-related injuries	Page 16
403-10 Work-related ill health	Page 16
Diversity and Inclusion	
405-1 Diversity of governance bodies and employees	Page 45
405-2 Ratio of basic salary and remuneration of women to men	Page 47
Capability and Development	
404-2 Programs for upgrading employee skills and transition assistance programs	Page 45

Directory
Rārangi tauwaea

Postal address

PO Box 5704
Lambton Quay
Wellington 6145

Office hours

Monday through Friday
09.00-17.30 hrs

Except Public Holidays

Phone

+64 4 974 6530

Personnel e-mail addresses

firstname.lastname@lgfa.co.nz

Website

www.lgfa.co.nz

General enquiries

lgfa@lgfa.co.nz

Street address

WELLINGTON
Registered Office

Level 8
City Chambers
142 Featherston Street
Wellington 6011

AUCKLAND

Level 5
Walker Wayland Centre
53 Fort Street
Auckland 1010

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