greater WELLINGTON
REGIONAL COUNCIL

Report 11.72
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Committee Council
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Investing in the New Zealand Local Government Funding Agency (LGFA)

1. Purpose

To recommend that Council undertakes a special consultative process in conjunction with the annual planning process to seek feedback from the public on the proposal to invest in the New Zealand Local Government Funding Agency Limited (LGFA).

2. Significance of the decision

Before making any decision on investing in a new council controlled organisation the Council is required to follow a special consultative procedure under the Local Government Act 2002.

3. Background

The officers have been working with a steering group, (who together hold over 60% of the local authority debt) to establish an organisation that could raise funds collectively for the sector at margins below where the sector currently borrows.

Councillors have been supportive of this venture and to date Greater Wellington has committed $100,000 to the preliminary cost prior to the establishment of the LGFA. A paper and presentation package was forwarded to Councillors in late February with opportunity to contact the Chief Financial Officer for further information or clarification should that have been needed.

At this juncture then it is expected the Councillors are familiar with the LGFA and the potential benefits it could convey to Greater Wellington.

4. LGFA proposal

The proposal is for this Council to become a shareholder in the Council Controlled Trading Organisation (CCTO) called the LGFA along with initially up to eight other Councils and the Government.

Law firm Simpson Grierson has prepared a draft Statement of Proposal on which any consultation will be based for the participation in shareholding in the LGFA.

A copy of the Statement of Proposal and a detailed Information Memorandum is in **Attachment 1**.

5. Assessment of risks

The setting up of the LGFA is not entirely without risk. There are three risks that the Councillors should be aware of:

The first risk relates to the take up of the LGFA by the sector.

Clearly if a very few local authorities use the LGFA then its viability will be at risk as it needs a critical level of borrowing to cover its fixed costs. This is currently assessed around $1.5 billion and is subject to a number of assumptions.

The mitigating factors here are that the steering group, who (using the sectors 2009/19 LTCCP) were collectively forecasting to have on issued $4.5 billion of debt (at 2010), are expected to place their maturing and new borrowing through the LGFA . With total sector debt currently at around $6.5 billion (at 2010) and projected to increase to around $10 billion in 5 years time there is ample opportunity for the LGFA to capture a big portion of this.

The recent announcement by Moody's Investor Service to downgrade the trading banks bodes well for the LGFA as the cost of funds of some of its main competitors will be marginally more expensive.

The second risk relates to the joint and several guarantee, whereby each local authority borrowing in excess of $20 million is obliged to guarantee the obligations of the LGFA.

The mitigating factors here are many, firstly that no local authority has ever defaulted on its debt obligations.

Secondly if a local authority did default the LGFA is structured in such a manner that it would have adequate liquidity to call upon and sustain itself till the defaulting local authority could go to its constituents and raise funds via a special rate.

Thirdly the LGFA is not guaranteed by Government, however due to its close involvement it is difficult to see the LGFA not being supported by the Government.

This is because the Government has been closely involvement with the LGFA set up and has provided $5 million of capital. The recent precedent of the Government providing a guarantee to the banks to protect local investors and its past assistance with the Bank of New Zealand, it is difficult to see the Government not supporting the LGFA given its large potential New Zealand investor base.

Fourthly, the joint and several guarantee, while not finalised, is to be structured between the Councils on a per ratepayer basis and is expected to be adjusted for Regional Councils given their larger rating base but low dollar value from each ratepayer.

The last risk is around the operation of the LGFA. This is considered to be very low due to its conservative borrowing and lending policies. Its operational functions will be undertaken by the Debt Management Office of the New Zealand Treasury. The Treasury is a well established institution with a number of years of experience and of course owned by the Government.

5.1 Change to the Councils security structure

The Council currently borrows funds from the market place and does not grant specific security to its lenders. Instead it has a “Negative Pledge Deed” under which the Council undertakes to each borrower not to grant security to any other borrower. On joining the LGFA the Council is required to provide security in the form of a charge over its rates and rates revenue. This type of security arrangement is widely granted by New Zealand local authorities to secure their general borrowing obligations and related incidental arrangements. Thus a receiver would have the power to exercise this charge and recoup the funds from the ratepayers.

As part of the proposal to joint the LGFA we are seeking Council approval to enter into this type of security arrangement.

5.2 Amendment to the Policies Document – 10 year plan 2009-19

As part of the process of investing in a CCTO the wording of our Treasury Risk Management Policy needs to be amended. This amendment is to record investment in the LGFA, the granting of the guarantee, provision of a charge over rates and rates revenue and other ancillary comments enabling the investment and future proposed borrowing via the LFGA.

5.3 Consultation and decision process

The Local Government Act 2002 requires that a special consultative procedure be undertaken on the proposal to invest in a new CCTO. Subject to the approval of the Council, this can be undertaken concurrently with the Draft Annual Plan 2011/12.

Depending on the number of submissions, submitters could be heard by the Council at its meeting on 26 May.

6. Communication

Subject to approval by the Council, the proposal will be fully consulted on concurrently with the Proposed Annual Plan 2011/12. The proposal will be published in the Proposed Annual Plan 2011/12 documents and an updated LTCCP Policies Document prepared and available for inspection.

7. Recommendations

That the Council:

1. ***Receives** the report.*
2. ***Notes** the content of the report.*
3. ***Approves** the Statement of Proposal as set out in Attachment 1.*

Report prepared by:	Report approved by:
Mike Timmer Treasurer	Bruce Simpson Chief Financial Officer

Attachment 1: Draft Statement of Proposal & Information Memorandum