

Report 14.353
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Committee Risk and Assurance
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Local Government Funding Agency (LGFA) Statement of Intent & June Quarter update

1. Purpose

To present the final LGFA Statement of Intent for 2013/14 and the LGFA's Quarterly Report for the period ending 30 June 2014.

2. Background

The LGFA was established on 6 December 2011 and being a Council Controlled Trading Organisation (CCTO), it is required to prepare a Statement of Intent to its shareholders.

Greater Wellington Regional Council (GWRC) has been a promoter of this organisation and initially held \$2 million of the \$25 million share capital, being one of the initial 18 non-central government founding shareholders.

In December 2012 the Council sold down part of its shareholding (from \$2m down to \$1.866m) to allow 12 other councils to join the LGFA. This brought the total number of participating councils to 30.

GWRC has a representative (Vice Chairman) on the Shareholders' Council. The Shareholders' Council is a group consisting of the nine Councils which originally promoted the LGFA.

The principal role of the Shareholder Council is to monitor the LGFA and to provide a focal point for LGFA communication. The Council has formal meetings and meets around five times a year.

The Shareholders' Council has developed its own charter, provided assistance with debt settlements, developed a monitoring framework to monitor the LGFA, monitors the LGFA performance, and provides a Letter of Expectation to the LGFA in relation to its SOI and business operation.

3. Statement of Intent

The final Statement of Intent (refer **Attachment 1**) was received on 30 June 2014.

Looking at the three year plan, the following highlights are notable:

- A profit forecast of \$7.3 million in the 2014/15 year, it dips to \$6.38 million in 2015/16 and then increases to \$7.13 million in 2016/17.
- The dip in profitability in 2015/16 stems from costs relating to the new treasury system (depreciation, maintenance, non-capex implementation costs) and increased staff cost. The increased staff costs are slightly more than the saving from the outsourced treasury cost previously incurred by the New Zealand Debt Management Office (DMO). Other increases include a greater allowance for marketing targeted at offshore investors, and higher Approved Issuer Levy (AIL), being tax levied on overseas holders of New Zealand securities.
- A steady dividend is forecast of \$1.75 million for the 3 years with equity growing from \$34 million in 2014/15 to \$44.5 million by June 2017.
- Total assets (mostly lending to Council) increase from \$4,550 million in 2014/15 to \$6,560 million in 2016/17.
- The performance targets have the LGFA's average cost of funds set at 0.50% above NZ Government Stock for all years. This remains un-adjusted from last year and has yet to be achieved.
- The forecasted margins charged to councils by the LGFA reduce from 0.15% to 0.10% in both 2016 and 2017 for the next three years respectively. This reflects the impact of the larger asset base and economies of scale, however there is room for further reduction and a discussion needs to be had as to the desired level of equity the LGFA should have.

A major focus for the LGFA over the coming year will be the implementation of a new treasury system which is scheduled for completion in June 2015. This will enable the LGFA to move from the DMO who are presently providing the treasury systems.

The new Chief Executive has signalled a number of changes which are consistent with the recommendations from the Shareholders Council. The major one will be the move to providing a greater range of maturities to the sector. This will see the LGFA becoming more of a bank instead of a back to back lender as it is presently.

4. Shareholders' Council Quarterly report – 30 June 2014

The LGFA Quarterly Report and the Shareholders Councils monitoring report in relation to the LGFA report are appended (refer to **Attachment 2 and Attachment 3**).

Highlights from the June Quarter are noted below:

- Total bonds on issues were \$3,697 million for the 2013/14 year, an increase of \$1.3 billion over the year.
- While three of the five key performance indicators were not achieved during the quarter, the seriousness of this non achievement is either beyond the control of the LGFA or minor in nature.
- The average cost of funds to relative New Zealand Government Stock is a market determined and does not provide a direct comparison with the actual bonds issued. This could be considered an aspirational target. Over time with the NZ Government reducing its debt on issue, this margin will reduce. It will also reduce if the LGFA issues shorter dated bonds. It's important for the LGFA to measure itself against Government Bond rate, rather than against the swap rate which compares the LGFA to a bank.
- The estimated interest cost savings for the sector (0.23% v 0.30%) have not been achieved. There is a general feeling that this measurement is inaccurate. The LGFA has had a significant effect on reducing sector margins. The measurement of this is fraught with difficulty. The measure compares the LGFA to Auckland Council, and Dunedin City Council. The point is, the presence of the LGFA has reduced Local Government sector margins.

The LGFA has a new Chief executive Mr Mark Butcher who was previously Treasurer for the Auckland Council. This appointment has enabled a reduction in Directors and requisite costs as Mark was previously on the LGFA Board.

5. The decision-making process and significance

The matter requiring decision in the report has been considered by officers against the requirements of Part 6 of the Local Government Act 2002 (the Act).

Officers have considered the significance of the matter, taking the Council's significance policy and decision-making guidelines into account. Officers recommend that the matter be considered to have low significance.

Officers do not consider that a formal record outlining consideration of the decision-making process is required in this instance.

6. Recommendations

That the Council:

- 1. Notes the contents of this report*
- 2. Notes the Statement of Intent from the Local Government Funding Agency for 2014/15 and the next two years.*
- 3. Notes the Local Government Funding Agency Quarterly Report for the period ended 30 June 2014*

4. Notes the Shareholders' Council Quarterly Monitoring Report for the period ended 30 June 2014

Report prepared by:

Mike Timmer

Treasurer/Acting Chief Financial Officer

Report approved by:

David Benham

Chief Executive Officer

Attachment 1: LGFA Ltd Final Statement of Intent 2014/14

Attachment 2: LGFA Quarterly Monitoring Report for the period ended 30 June 2014

Attachment 3: Shareholders' Council Quarterly Monitoring Report – Q4 30 June 2014