Compiled Date	24/11/2023
File Number	23.24.59

LGOIMA

When releasing responses to previous LGOIMA requests, names and contact details of individual requestors will be withheld to protect their privacy.

Information requested by the media, lobby groups, public sector organisations and MPs will always be published, while information specific to an individual or their property will not generally be published.

Request from:	Private Individual
Information requested:	LGFA agreement with WDC
Response by:	Simon Bastion, Chief Executive

24 November 2023

Via Email:

Dear Private Individual

Official information request for information regarding LGFA agreement with Westland District Council

I refer to your official information request dated 14 November 2023 for information regarding LGFA agreement with Westland District Council.

You have asked for the following information:

1. **Which financial year did Westland District Council (WDC) first enter into any loan/financial agreement with the Local Government Financial Agency (LGFA) and/or LGFA Ltd?**

   2018

2. **When/how did the WDC ratepayers agree, approve, and accept joining/engaging the LGFA? Please provide evidence of any agreement/approval/acceptance.**

   There was a consultation for members of the public to submit to Council regarding joining the Local Government Agency. Enclosed is the consultation proposal and the advertisement that ran.

   No submissions were received therefore Council joined the LGFA.

There is no charge in supplying this information to you.

Council has adopted a Proactive Release Policy and accordingly may publish LGOIMA responses on the Council Website at https://www.westlanddc.govt.nz/lgoima-responses. The collection and use of personal information by the Westland District Council is regulated by the Privacy Act 2020. Westland District Council's Privacy Statement is available on our website here

If you wish to discuss this decision with us, please feel free to contact Mary-anne Bell, Business Analyst at LGOIMA@westlanddc.govt.nz, 03 756 9091.

Sincerely,

Simon Bastion | Chief Executive

SB/MB

CCL 4

25 August 2017

Advertising
Hokitika Guardian

Can you please:

1. Insert the following notice in the **Hokitika Guardian on Monday 28 August 2017.**

2. Quote order number 101378.

3. Ensure that the heading stands out as per our copy and the Council logo is added; double column also.

Diane Maitland
<u>Executive Assistant</u>

WDC 23.24.59 Released under LGOIMA

STATEMENT OF PROPOSAL

Participation in the New Zealand Local Government Funding Agency Limited (LGFA)

Westland District Council has adopted the Statement of Proposal to participate in the New Zealand Local Government Funding Agency Limited.

This means that Council will participate in the LGFA Scheme, but not as a Principal Shareholding Local Authority or as a Guaranteeing Local Authority, but simply as a borrower.

Under Section 82A of the Local Government Act 2002, the proposal is available for inspection and there is an opportunity to make submissions. The proposal is available at the Council's Customer Service Centre, 36 Weld Street, Hokitika, and also on Council's Website www.westlanddc.govt.nz.

Submissions must be in writing and addressed to the Council. Submissions may be sent either:

- by post to *the Group Manager: Corporate Services, Westland District Council, 36 Weld Street, Private Bag 704, Hokitika 7842*; or
- by email to consult@westlanddc.govt.nz.or
- Delivery to the Customer Service Centre, 36 Weld Street, Hokitika.

Submissions must be received no later than **5.00 pm** on **29 September 2017.**

WDC 23.24.59 Released under LGOIMA

STATEMENT OF PROPOSAL

Westland District Council
Participation in New Zealand Local Government Funding Agency Limited

Date: 24 August 2017

WDC 23.24.59 Released under LGOIMA

CONTENTS

Introduction 3
Reasons for Proposal 3
Analysis of Reasonably Practicable Options 4
Investment Policy 5
Liability Management Policy 5
Opportunity to Make Submissions 5
Appendix 1 7
Annex 1 .... **Error! Bookmark not defined.**
Appendix 2 21

WDC 23.24.59 Released under LGOIMA

Introduction

The Westland District Council is considering participating in the New Zealand Local Government Funding Agency Limited (**LGFA**), which is a council-controlled trading organisation (**CCTO**).

Council is proposing it will participate as a borrower but not as a Principal Shareholding Local Authority or as a Guaranteeing Local Authority.

The LGFA is established by the local authority sector and the Crown to enable local authorities to borrow at lower interest margins than would otherwise be available. The LGFA is recognised in legislation.

All member local authorities are able to borrow from the LGFA, but different benefits apply depending on the level of participation. Most local authorities borrowing from LGFA will have some shareholding and/or enter into guarantees in favour of the LGFA and other local authorities. This is certainly the case for Principal Shareholding and Guaranteeing Local Authorities. Local authorities which borrow from the LGFA without entering into the guarantee will only be able to borrow a limited amount, and will be required to pay higher funding costs.

Principal Shareholding Local Authorities are required to invest capital in the LGFA, but expected to receive a return on that capital.

Any local authority that borrows from the LGFA will be required to provide LGFA with subordinated debt (borrower notes, to the value of a percentage of the amount borrowed). These borrower notes will be held by the local authority while the borrowing is outstanding and may be certain situations convert to redeemable preference shares in LGFA.

An Information Memorandum, describing the arrangements in detail, is attached as Appendix 1, and forms part of this proposal. A number of terms which are used in this proposal are defined in that Information Memorandum.

Summary of Proposal

Given the short nature of this entire Statement of Proposal, Council is not producing a separate summary.

Statutory Considerations

Section 56 of the Local Government Act 2002 (**LGA 2002**) provides that a proposal to establish a council-controlled organisation (**CCO**) (which includes a CCTO) must be adopted following consultation in accordance with section 82 before a local authority may establish or become a shareholder in the CCO. At any level of participation (including as a borrower), the Council either will become a shareholder, or will enter into commitments that could result in it becoming a shareholder in LGFA. The purpose of this consultation is to enable the Council to enter into these commitments.

Reasons for Proposal

The Council is proposing participating in the LGFA Scheme because it believes it provides an opportunity that will enable it to borrow at lower interest margins, and that this benefit outweighs any costs and risks associated with the LGFA Scheme. A discussion of these costs and benefits is included as Part C of the Information Memorandum.

The Council is proposing to participate solely as a potential borrower and not as a Principal Shareholding Local Authority or a Guaranteeing Local Authority for two reasons:

WDC 23.24.59 Released under LGOIMA

(a) Council's view is that for the Westland District Council the risks associated with being a Principal Shareholding Local Authority or a Guaranteeing Local Authority outweighs the rewards.
(b) Westland District Council is not in a position to commit the required capital to be a Principal Shareholding Local Authority.

The Council is consulting on this proposal for the reasons set out above under "Statutory Considerations".

Analysis of Reasonably Practicable Options

The reasonably practicable options are as follows:

1. **Participate in the LGFA Scheme as a Principal Shareholding Local Authority.**

2. **Participate in the LGFA Scheme as a Guaranteeing Local Authority, but not a Principal Shareholding Local Authority.**

3. **Participate in the LGFA Scheme, but not as a Principal Shareholding Local Authority or as a Guaranteeing Local Authority, but simply as a borrower.**

4. **Not participate in the LGFA Scheme.**

Part C of the Information Memorandum sets out an analysis of the costs and benefits of participating in the LGFA Scheme. That analysis is supplemented by some consideration of the Council's specific circumstances below.

Q. Should the Council participate in the LGFA Scheme as a Principal Shareholding Local Authority or as a Guaranteeing Local Authority?

Investing in the LGFA Scheme as a Principal Shareholding Local Authority would provide the lowest cost option for borrowing by:

(a) As discussed in the Information Memorandum (in Part C), a return will be paid on the capital investment made by Principal Shareholding Local Authorities.

(b) If the Council participates as a Principal Shareholding Local Authority, that increases the chance that the LGFA Scheme will be viable, and that the Council will be able to gain the benefits of participating in it.

However, there is an associated shared risk through:

- Westland District Council is not in a position to commit the required capital to be a Principal Shareholding Local Authority

- Principle Shareholding Local Authorities will be required to subscribe for uncalled capital which is equal in amount to its paid up equity contribution. LGFA would only call uncalled capital if there is a risk of imminent default. However, such a call is likely to be made before the guarantee or additional equity commitments are utilized.

- Guaranteeing Local Authorities being required to guarantee the obligations of all other Guaranteeing Local Authorities and the obligations of the LGFA.

WDC 23.24.59 Released under LGOIMA

- Guaranteeing Local Authorities commit to contributing additional equity to the LGFA if there an imminent risk that the LGFA will default.

(Refer to the *Summary of transactions a Council will enter into if it joins the LGFA Scheme* in Appendix 1 (Information Memorandum) for detail on what commitments will be made if participating as a Principal Shareholding Local Authority or as a Guaranteeing Local Authority.)

The risk is assessed as low. Nonetheless it is a risk that the Council is proposing not to take.

Consequently, the Council is proposing that option (1) and option (2) NOT be adopted.

Q. Should the Council participate in the LGFA Scheme as a borrower (and not as a Principal Shareholding Local Authority or a Guaranteeing Local Authority)?

It is assumed that membership would be as a non-guaranteeing borrower so current LGFA pricing has been used for maturity terms 2021, 2022 and 2023. An amount of $15m has been assumed to be refinanced through issuing LGFA bonds of $5m for each maturity date. Upon repaying the bank debt, the equivalent of $15m of bank facilities would be cancelled. The Council estimates that the annual borrowing cost saving based on prevailing LGFA pricing is around $80,000 per annum.

Consequently, the Council proposes that Option (3) is adopted.

Investment Policy

The Council's Investment Policy includes a statement to make clear that the Council's investment activity includes the LGFA.

The primary objective for Council's interest in LGFA is to lower the Council's cost of borrowing.

Liability Management Policy

The Council's Liability Management Policy makes it clear that the Council may participate in the LGFA Scheme, including borrowing from the LGFA and entering into the transactions relating to that borrowing described in paragraph 63 of the Information Memorandum.

The primary objective of these changes is to allow borrowing by the Council at lower interest margins than it currently faces.

Opportunity to Make Submissions

This proposal will be distributed, and available for inspection and copying, as required by section 82A of the Local Government Act 2002.

This statement of proposal is available for inspection at Council's main office (36 Weld Street, Hokitika) and any other place the Council considers appropriate to ensure all interested persons have a reasonable opportunity to view the proposal eg on Council's website; www.westlanddc.govt.nz. Visitor information centre, Library.

WDC 23.24.59 Released under LGOIMA

Submissions on this proposal must be in writing and addressed to the Council. Submissions may be sent either:

- by post to *the Group Manager, Corporate Services, Westland District Council,36 Weld Street, Private bag 704, Hokitika 7842*; or
- by email to consult@westlanddc.govt.nz.or
- Delivery to the Customer Service Centre, 36 Weld Street, Hokitika.

Submissions must be received no later than **5.00 pm** on **29 September 2017.**

Any person or organisation who makes a submission has a right to be heard by the Council. Submitters who wish to be heard must request this in their submission.

Every submission will be:

- acknowledged by the Council in accordance with the LGA 2002,
- copied and made available to the public.

The LGA 2002 requires the Council to make all written submissions on this consultation available to the public. This requirement is subject to the provisions of the Local Government Official Information and Meetings Act 1987. If you consider there to be compelling reasons why your contact details and/or submission should be kept confidential, you should advise within your submission.

The consultation process dates are as follows:

24 August 2017	adopts statement of proposal and summary of proposal
28 August 2017	public notice of proposal and consultation process in Local newspapers, Council website, electronic newsletter and local radio stations.
29 September 2017	submissions close at 5.00 pm
October 2017	If a hearing is necessary

WDC 23.24.59 Released under LGOIMA

LOCAL GOVERNMENT FUNDING AGENCY SCHEME

INFORMATION MEMORANDUM

PART A – INTRODUCTION AND PURPOSE

Purpose of Information Memorandum

1. This Information Memorandum provides a description of the structure for local authorities (**LGFA Scheme**), which is designed to enable participating local authorities (**Participating Local Authorities**) to borrow at lower interest margins than they would otherwise pay.

2. The purpose of this Information Memorandum is to provide information to supplement any consultation materials prepared by local authorities consulting on whether to participate in the LGFA Scheme.

3. This Information Memorandum is divided into three parts:

(a) This Part A (Introduction and Purpose), which sets out the purpose of the Information Memorandum and provides some background on the purpose of, and rationale for, the LGFA Scheme.

(b) Part B (How the LGFA Scheme Works), which sets out the characteristics of the LGFA Scheme, and the transactions that Participating Local Authorities enter into as part of their participation in the LGFA Scheme.

(c) Part C (Local Authority Costs and Benefits), which sets out the costs and benefits to individual local authorities of participating in the LGFA Scheme.

Origin of the LGFA Scheme

4. The LGFA Scheme was developed by a group of New Zealand local authorities and central government. That development involved:

(a) undertaking a detailed review and analysis of:

(i) the borrowing environment in which New Zealand local authorities borrow; and

(ii) centralised local authority debt vehicle structures that have been developed offshore to successfully lower the cost of local authority borrowing;

(b) using this review and analysis to develop a funding structure (the LGFA Scheme), which is anticipated to deliver significant benefits to New Zealand local authorities;

(c) confirming with rating agencies that the proposed LGFA Scheme can achieve a high enough credit rating to deliver the anticipated benefits;

WDC 23.24.59 Released under LGOIMA

(d) obtaining formal central government support to facilitate establishment of the LGFA Scheme.

Rationale for LGFA Scheme

New Zealand Local Authority debt market

5. New Zealand local authorities face a number of debt related issues.

6. First, local authorities have significant existing and forecast debt requirements. Current long-term council community plans indicate that local authority debt will reach $20,036 million over the next 5 years.

7. Secondly, pricing, length of funding term and other terms and conditions vary considerably across the sector and are less than optimal. This is due to:

(a) Limited debt sources – Local authorities' debt funding options are limited to the banks, private placements and wholesale bonds (issuance to wholesale investors), and, to a lesser extent, retail bonds. Increasing local authority sector funding requirements and domestic funding capacity constraints are likely to further negatively impact pricing, terms and conditions and flexibility of local authority sector debt.

(b) Fragmented sector – There are 78 local authorities. Individually, a significant proportion of these local authorities lack scale - the 10 largest account for ~70%

(c) Regulatory restrictions - Offshore (foreign currency) capital markets are closed to local authorities and the process for local authority retail bond issuance is burdensome.

Addressing the local authority debt issues

8. Each of these issues needs to be addressed to rectify this situation. The LGFA Scheme rectified the situation by the following reasons:

(a) Individually, local authorities were not able to attain significant scale (except organically in the long-term).

(b) At a sector level it may be possible to address the issue regarding regulation, but regulators are likely to remain reluctant to significantly ease restrictions on financial management across the sector without gaining significant comfort as to the sophistication of the financial management of all local authorities. Even if this issue were addressed by regulators, this change alone would be insufficient to provide a major step change.

9. The LGFA Scheme was developed because of the homogenous nature of local authorities; the large sector borrowing requirements and the high credit quality / strong security position (i.e. charge over rates) of local authorities, created the opportunity for a centralised local authority debt vehicle to generate significant benefits.

WDC 23 24.59 Released under LGOIMA

10. There are numerous precedents globally of successful vehicles which pool local authority debt and fund themselves through issuing their own financial instruments to investors. Such vehicles achieve success through:

(a) "Credit rating arbitrage" – Attaining a credit rating higher than that of the individual underlying assets (local authority borrowers) and therefore being able to borrow at lower margins.

(b) "Economies of scale" – By pooling debt the vehicles can access a wider range of debt sources and spread fixed operating costs, thereby reducing the $ cost per $ of debt raised.

(c) "Regulatory arbitrage" – The vehicles can receive different regulatory treatment than the underlying local authorities, improving their ability to efficiently raise debt eg through access to offshore foreign currency debt markets.

11. The offshore precedents are typically owned by the local authorities in the relevant jurisdiction (often with central government involvement), and that is similar to the LGFA Scheme.

PART B – HOW THE LGFA SCHEME WORKS

Basic structure of the LGFA Scheme

12. The basic structure of the LGFA Scheme is that a company is established which will borrow funds and lend them on to local authorities at lower interest margins than those local authorities would pay to other lenders.

New Zealand Local Government Funding Agency Limited

13. LGFA was incorporated as a limited liability company under the Companies Act 1993 on 1 December 2011, and is subject to the requirements of the Local Government Act 2002. Its shares are held entirely by central government and by local authorities.

14. There are currently 31 shareholders comprising New Zealand Government at 20% and 30 Councils at 80%. As a result the LGFA is a council-controlled organisation.

15. The LGFA was established solely for the purposes of the LGFA Scheme, and its activities will be limited to performing its function under the LGFA Scheme.

16. A number of local authorities (**Principal Shareholding Local Authorities**) hold all, of those shares that are not held by central government. The Principal Shareholding Local Authorities have contributed capital and, as compensation for their capital contribution, will receive a pre-determined return on this capital. However, the over-arching objective is that the benefits of the LGFA Scheme are passed to local authorities as lower borrowing margins, rather than being passed to shareholders as maximised profits.

WDC 23.24.59 Released under LGOIMA

Design to minimise default risk

17. One of the things which is critical to the LGFA Scheme delivering its anticipated benefits is the achievement of a high credit rating for the LGFA (to achieve the credit rating arbitrage referred to in paragraph 10(a)). Consequently there are a number of features of the LGFA Scheme which are included to provide the protections for creditors which rating agencies require before agreeing to a high credit rating. These features are described in paragraphs 19 to 54 below.

18. Before agreeing to a high credit rating, rating agencies will consider the risks of both short term and long term default. Short term default is where a payment obligation is not met on time. Long term default is where a payment obligation is never met. In many cases short term default will inevitably translate into long term default, but this is not always the case – a short term default may be caused by a temporary liquidity problem (ie a temporary shortage of readily available cash).

Features of the LGFA Scheme designed to reduce short term default risk

19. When a local authority borrows, the risk of short term default, although low, is probably significantly higher than its risk of long term default. In the long term it can assess and collect sufficient rates revenue to cover almost any shortfall, but such revenue cannot be collected quickly. Consequently, there is a risk that inadequate liability and revenue management could lead to temporary liquidity problems and short term default.

20. The principal asset of the LGFA will be local authority debt, so such temporary liquidity risks are effectively passed on to the LGFA. Consequently, the rating agencies will look for safeguards to ensure that liquidity problems of a Participating Local Authority will not lead to a default by the LGFA.

21. There are two principal safeguards that the LGFA has put in place to manage short term default (liquidity) risk:

(a) It holds a certain amount of cash and other liquid investments (investments which can be quickly turned into cash).

(b) It has a borrowing facility with central government which allows it to borrow funds from central government if required.

22. It is expected that these safeguards will sufficiently reduce any short term default risk.

Features of the LGFA Scheme designed to reduce long term default risk

23. There are a number of safeguards that the LGFA has put in place to manage long term default risk, the most important of which are set out below:

(a) The LGFA requires all local authorities that borrow from it to secure that borrowing with a charge over that local authority's rates revenue (**Rates Charge**).

(b) The LGFA maintains a minimum capital adequacy ratio (or have some equivalent capital adequacy safeguard).

WDC 23.24.59 Released under LGOIMA

(c) The Principal Shareholding Local Authorities are required to subscribe for uncalled capital in an equal amount to their paid up equity contribution.

(d) The LGFA require most, or possibly all, Participating Local Authorities (**Guaranteeing Local Authorities**) to guarantee the obligations of all other Guaranteeing Local Authorities and the obligations of the LGFA.

(e) The Guaranteeing Local Authorities will commit to contributing additional equity to the LGFA if there an imminent risk that the LGFA will default.

(f) The LGFA hedge any exposure to interest rate and foreign currency fluctuations to ensure that such fluctuations do not significantly affect its ability to meet its payment obligations.

(g) The LGFA put in place risk management policies in relation to its borrowing and lending designed to minimise its risk. For example, it will impose limits on the percentage of lending which is made to any one local authority to ensure that its credit risk is suitably diversified.

(h) The LGFA ensure that its operations are run in a way that minimises operational risk.

24. Additional detail in relation to the features referred to in paragraphs 24(a) to 24(e) is set out below.

Rates Charge

25. All local authorities borrowing from the LGFA arerequired to secure that borrowing with a Rates Charge. Many but not all local authorities have a Rates Charge in place already.

26. This is a powerful form of security for the LGFA, because it means that, if the relevant local authority defaults, a receiver appointed by the LGFA can assess and collect sufficient rates in the relevant district or region to recover the defaulted payments. Consequently, it significantly reduces the risk of long term default by a local authority borrower.

27. From a local authority's point of view it is also advantageous, because, so long as the local authority does not default, it is entitled to conduct its affairs without any interference or restriction. This contrasts with most security arrangements, which involve restrictions being imposed on a borrower's use of its own assets by the relevant lender.

Minimum capital

28. One important safeguard against long-term default for the LGFA will be having a minimum capital adequacy ratio (a ratio which measures the relative amounts of equity and debt-based assets which an entity has). This ratio is important, because it provides an indication of the ability of the LGFA to ultimately repay all of its debts despite local authorities that have borrowed from it defaulting or some other loss occurring.

29. The minimum capital adequacy ratio requirement is likely to be that the equity of the LGFA is an amount equal to at least 1.6% of its total assets.

WDC 23.24.59 Released under LGOIMA

Sources of equity for capital adequacy purposes

30. The equity held by the LGFA to ensure that it meets its minimum capital adequacy ratio requirement comes from two sources. First, central government and the Principal Shareholding Local Authorities contribute initial equity as the issue price of their initial shareholdings. Secondly, it is anticipated that each Participating Local Authority will, at the time that it borrows from the LGFA, contribute some of that borrowing back as equity.

31. The way the second source of equity works is that, whenever a Participating Local Authority borrows, it will not receive the full amount of the borrowing in cash. Instead, a small percentage of the borrowed amount will remain with the LGFA as equity. That percentage is to be 1.6% of the amount borrowed.

32. The equity contributed in this way is to be repaid when the borrowing is repaid, so, in effect, the amount which must be repaid will equal the cash amount actually advanced.

33. The equity is contributed by subscribing for "Borrower Notes". The LGFA may convert borrower notes into redeemable shares.

34. To illustrate with an example, if a local authority borrowed $1,000,000 for five years from the LGFA, it would receive $984,000 in cash and $16,000 of Borrower Notes. At the end of the five years, it would repay $1,000,000, but would simultaneously redeem its Borrower Notes for $16,000, meaning its net repayment was equal to the $984,000 it initially received in cash.

35. A return will be paid on the Borrower Notes, which will be in the form of a dividend if they are redeemable preference shares. The amount will be the LGFA cost of funds plus 2.00%.. While it is anticipated that this return will be paid, it will be paid at the discretion of the LGFA.

36. There is some additional risk to Participating Local Authorities from this arrangement, because redemption of the Borrower Notes will only occur if the LGFA is able to pay its other debts. For example, if at the end of five years, the LGFA was insolvent, the local authority would have to repay $1,000,000, but would not receive its $16,000 back for redeeming its Borrower Notes.

Uncalled capital

37. Each Principal Shareholding Local Authority will be required to subscribe for uncalled capital which is equal in amount to its paid up equity contribution (**Uncalled Capital**).

38. It is anticipated that the Uncalled Capital will only be able to be called by the LGFA if it determines that there is a risk of imminent default if the call is not made. However, such a call is likely to be made before the Guarantee or additional equity commitment described below are utilised.

Guarantee

WDC 23-24.59 Released under LGOIMA

39. Participating Local Authorities are required to enter into a guarantee when they join the LGFA Scheme (**Guarantee**). Under the Guarantee the Guaranteeing Local Authorities guarantee the payment obligations of other Guaranteeing Local Authoritiesto the LGFA (**Cross Guarantee**), and guarantee the payment obligations of the LGFA itself (**LGFA Guarantee**).

40. The purpose of the Guarantee is to provide additional comfort to lenders (and therefore credit rating agencies) that there will be no long term default, though it may also be used to cover a short term default if there is a default which cannot be covered using the protections described in paragraphs 20 to 23 above, but which will ultimately be fully covered using the rates charge described in paragraphs 26 to 28. The Guarantee allows the LGFA to draw upon the resource of all Guaranteeing Local Authorities to avoid defaults.

Risk from Cross Guarantee

41. There are five factors which mitigate the risk to Guaranteeing Local Authorities under the Cross Guarantee:

(a) The risk only materialises if another Participating Local Authority defaults on its debt obligations. It is believed that no such default has ever occurred, which suggests that the risk of a local authority default is very low.

(b) If a Participating Local Authority defaults, but it is because of temporary liquidity problems only, the safeguards in place to cover temporary liquidity shortages may be sufficient for the LGFA never to have to call upon the Cross Guarantee. The detail of when the LGFA will be able to call upon the Cross Guarantee is not yet finalised, but it is likely that it will be restricted to situations in which there is a risk of an imminent default by the LGFA.

(c) It is anticipated that the Guarantee will only be called if a call on the Uncalled Capital does not generate sufficient funds to eliminate the risk of an imminent default by the LGFA.

(d) If a Participating Local Authority defaults, the burden will be shared by all Guaranteeing Local Authorities.

(e) If a Participating Local Authority defaults, the LGFA will exercise its rights under the Rates Charge to recover the payments defaulted on. The funds recovered through that exercise of rights will be passed on to the local authorities who have made payment under the Cross Guarantee, so those local authorities should, in the long term, be reimbursed for a significant portion, if not all, of the amount they have paid under the Cross Guarantee. The statutory processes involved in exercising these rights suggest that funds will be able to be recovered within 18 months of default.

LGFA Guarantee

42. The LGFA Guarantee will only ever be called if the LGFA defaults. Consequently, a call on the LGFA Guarantee will only occur if the numerous safeguards put in place to prevent an LGFA default fail. This is highly unlikely to happen.

WDC 23-24-59 Released under LGOIMA

43. If any such default did occur, and the Guaranteeing Local Authorities were called on under the LGFA Guarantee they could potentially be called on to cover any payment obligation of the LGFA. Such payment obligations may (without limitation) include obligations under the following transactions:

(a) A failure by the LGFA to pay its principal lenders.

(b) A failure by the LGFA to repay drawings under the liquidity facility with central government.

(c) A failure by the LGFA to make payments under the hedging transactions referred to in paragraph 24(f).

Guarantee risk shared

44. There is a mechanism to ensure that payments made under the Guarantee are shared between all Guaranteeing Local Authorities. The proportion of any payments borne by a single Guaranteeing Local Authority is likely to be based on the number of ratepayers in its district or region, or on some other statistic which is a proxy for its relative ability to make payments.

Rates Charge

45. It is possible that Guaranteeing Local Authorities will be required to provide a Rates Charge to secure their obligations under the Guarantee.

Benefits of being a Guaranteeing Local Authority

46. Participating Local Authorities are permitted not to be Guaranteeing Local Authorities, it will be on the basis that their borrowings are only allowed to reach a limited level, less than $20,000,000. Such local authorities will also be required to pay higher interest margins.

47. Guaranteeing Local Authorities will, therefore, have the benefit of not having this low limit on borrowing, and will pay lower funding costs.

Additional equity commitment

48. In addition to the equity contributions made in conjunction with borrowing, all Guaranteeing Local Authorities are likely to be required to commit to contributing equity if required under certain circumstances. It is expected that calls on any such commitments will be limited to situations in which there is a risk of imminent default by the LGFA.

49. A call for additional equity contributions will only be made if calls on the uncalled Capital and on the Cross Guarantee will not be sufficient to eliminate the risk of imminent default by the LGFA. Consequently, the factors which limit the risk in relation to the Cross Guarantee also apply here.

50. If an additional equity contribution is required, the LGFA will lend the money required to make that contribution to the relevant local authority. For example, if $100,000 was required, the LGFA might issue $100,000 of shares to the local authority and, in return, the local authority would owe it a debt of $100,000. Consequently, there would be no requirement on the local authority to immediately make a cash payment. However, such a debt would ultimately have to be paid if the LGFA never regained a position in which it could buy back the shares.

WDC 23-24:59 Released under LGOIMA

51. It is possible that Guaranteeing Local Authorities will be required to provide a Rates Charge to secure their obligations to contribute additional equity.

Initial purchase of a single share

52. It is possible that Guaranteeing Local Authorities may be required to initially subscribe for 1 share in the LGFA. This is so that, if they have an ongoing commitment to subscribe for shares when required, they will already be a shareholder in the LGFA. The significance of this is that they will not be required, when subscribing for further shares, to go through the special consultative process associated with becoming a shareholder in a council-controlled organisation.

Characteristics designed to make the LGFA Scheme fair for all Participating Local Authorities

53. The principal risk involved with the LGFA Scheme is that Participating Local Authorities will default on their payment obligations. The greater this risk is, the less attractive participation in the LGFA Scheme is for all Participating Local Authorities.

54. The Participating Local Authorities do not create this risk in equal amounts. There are some that carry a greater default risk than others, and therefore contribute disproportionately to the overall risk in the LGFA Scheme. Those local authorities are also the local authorities that would be likely to pay the highest interest margins if they borrowed outside the LGFA Scheme, and so potentially benefit the most from the LGFA Scheme.

55. To avoid, or at least minimise, what is effectively cross subsidisation of the higher risk local authorities by the lower risk local authorities different interest margins will be paid by different local authorities when they borrow from the LGFA, with those carrying the higher default risk paying the higher interest margins.

Viability of the LGFA Scheme dependent on participation levels

56. The modelling and other analysis done by Cameron Partners and Asia Pacific Risk Management (**APRM**) suggests that the LGFA Scheme will be viable (in that it will deliver sufficient benefits to justify its establishment and continued existence) if:

(a) the LGFA maintains a high enough credit rating; and

(b) sufficient funds are borrowed through it to obtain the economies of scale benefits referred to in paragraph 10(b).

57. An AA+ credit rating with Standard and Poor and Fitch is maintained.

58. Consequently, the participation of sufficient local authorities, both initially as Principal Shareholding Local Authorities (to contribute initial capital) and in meeting their ongoing borrowing requirements through the LGFA Scheme is critical.

59. The Principal Shareholding Local Authorities has collectively contributed $20 million by way of initial capital contribution. What this amounts to on a per-local authority basis will depend on the number of Principal Shareholding Local Authorities.

WDC23.24.59 Released under LGOIMA

60. The Principal Shareholding Local Authorities are required to meet a certain proportion of their borrowing needs through the LGFA Scheme for an initial period, to ensure that the critical amount of utilisation is achieved.

Summary of transactions a Council will enter into if it joins the LGFA Scheme

61. If a Council joins the LGFA Scheme as a Principal Shareholding Local Authority, it will:

(a) subscribe for shares in the LGFA to provide it with capital (see paragraphs 16 and 31);

(b) possibly commit to meeting a certain proportion of its borrowing needs from the LGFA (see paragraph 62);

(c) borrow from the LGFA;

(d) subscribe for Uncalled Capital in the LGFA (see discussion in paragraphs 38 to 39 above);

(e) subscribe for Borrower Notes (see discussion in paragraphs 32 to 37);

(f) enter into the Guarantee (see discussion in paragraphs 40 to 45 above);

(g) commit to providing additional equity to the LGFA under certain circumstances (see discussion in paragraphs 49 to 53 above);

(h) possibly purchase one share in the LGFA at the time of joining the LGFA Scheme (see discussion in paragraph 54 above); and

(i) provide a Rates Charge to secure some or all of its obligations under the LGFA Scheme (see discussion in paragraphs 26 to 28, 46 and 53 above).

62. If a Council joins the LGFA Scheme as a Guaranteeing Local Authority, but not as a Principal Shareholding Local Authority, it will enter into the transactions described in paragraph 63, other than those described in paragraphs 63(a), 63(b) and 63(d).

63. If a Council joins the LGFA Scheme, but not as a Guaranteeing Local Authority (and therefore also not as a Principal Shareholding Local Authority) it will only enter into the transactions described in paragraph 63(e) and 63(i).

PART C - LOCAL AUTHORITY COSTS AND BENEFITS

64. The costs and benefits to a Participating Local Authority will depend on whether it participates as a Principal Shareholding Local Authority, a Guaranteeing Local Authority, or as neither.

Benefits to local authorities that borrow through the LGFA Scheme

65. The LGFA is able to borrow at a low enough rate for the LGFA Scheme to be attractive because of the three key advantages the LGFA will have over a local authority borrower described in paragraph 10. That is – exploiting a credit rating arbitrage, economies of scale and a regulatory arbitrage.

WDC 23.24.59 Released under LGOIMA

66. In addition, the LGFA provides local authorities with increased certainty of access to funding and terms and conditions (including the potential access to longer funding terms eg ~ 10 yrs+).

67. The potential savings for a local authority in terms of funding costs will depend on the difference between the funding cost to that local authority when it borrows from the LGFA and the funding cost to the local authority when it borrows from alternative sources. This difference will vary between local authorities.

68. The funding costs each local authority pays when it borrows from the LGFA will be affected by the following factors, some of which are specific to the local authority:

(a) the borrowing margin of the LGFA;

(b) the operating costs of the LGFA;

(c) any price adjustment made by the LGFA for that specific local authority as a result of:

(i) the credit quality of the local authority;

(ii) the size of the borrowings of that local authority from the LGFA; and

(iii) the local authority being a Guaranteeing Local Authority or not.

69. A diagram which shows what will affect the amount of any funding cost savings is set out as Annex 1.

70. Cameron Partners and APRM have developed a detailed financial model of the LGFA Scheme and analysed the current debt markets. The table set out in Annex 2 summarises the potential savings for local authorities depending on their credit status. (The modelling is based on conditions prevailing at December 2010 and on a number of assumptions regarding the LGFA, including its credit rating and the amount of loans it makes to local authorities.)

Costs to local authorities that borrow through the LGFA Scheme

71. The costs to Participating Local Authorities as a result of their borrowing through the LGFA Scheme take two forms:

(a) First, there are some risks that they will have to assume to participate in the Scheme, which create contingent liabilities (ie costs which will only materialise in certain circumstances).

(b) Secondly, there is some cost associated with the Borrower Notes.

WDC 23.24.59 Released under LGOIMA

Risks

72. The features of the LGFA Scheme described above which are included to obtain a high credit rating are essentially steps which remove risk from lenders to make their residual risk low enough to justify the high credit rating. These features remove risk, in part, by transferring it to Participating Local Authorities.

73. These risks are that:

(a) in the case of Guaranteeing Local Authorities, a call is made under the Guarantee (see discussion in paragraphs 40 to 45 above);

(b) in the case of Guaranteeing Local Authorities, a call is made for a contribution of additional equity to the LGFA (see discussion in paragraphs 49 to 53 above); and

(c) in the case of all Participating Local Authorities, the LGFA is not able to redeem their Borrower Notes (see discussion in paragraphs 32 to 37).

74. Each of these risks is discussed in some detail in the paragraphs indicated next to the relevant risk. For the reasons set out in those discussions, it is anticipated that each of the risks is low.

Cost of Borrower Notes

75. As discussed in paragraphs 32 to 37, all Participating Local Authorities will be required to invest in Borrower Notes when they borrow from the LGFA. This carries a cost in addition to the risk referred to in paragraph 75(c), because the investment in Borrower Notes will be funded by borrowing from the LGFA, and the cost of this funding will be higher than the return paid on the Borrower Notes.

76. It is anticipated that the Borrower Notes will pay a discretionary payment equal to the LGFA's own cost of funds. Any discretionary payment is likely to be capitalised until maturity.

77. As noted in paragraph 36, while it is the intention for the LGFA to always pay the proposed annual payment on the Borrower Notes, such payments are at the LGFA's discretion so, in some situations, those payments may not be made.

Cost/benefit analysis for the investment by Principal Shareholding Local Authorities

78. In addition to those costs and benefits that all Participating Local Authorities are expected to receive in relation to their borrowing from the LGFA, Principal Shareholding Local Authorities will also hold shares in the LGFA (**Establishment Shares**).

79. Establishment shares will pay a discretionary annual payment, which is an amount up to the LGFA's own cost of funds plus 200 bps[1].

80. While it is the intention for the LGFA to always pay the annual payment on the Establishment Shares, this payment will not be made, or will be reduced, if the performance of the LGFA means that the LGFA does not consider it appropriate to make the payment.

---

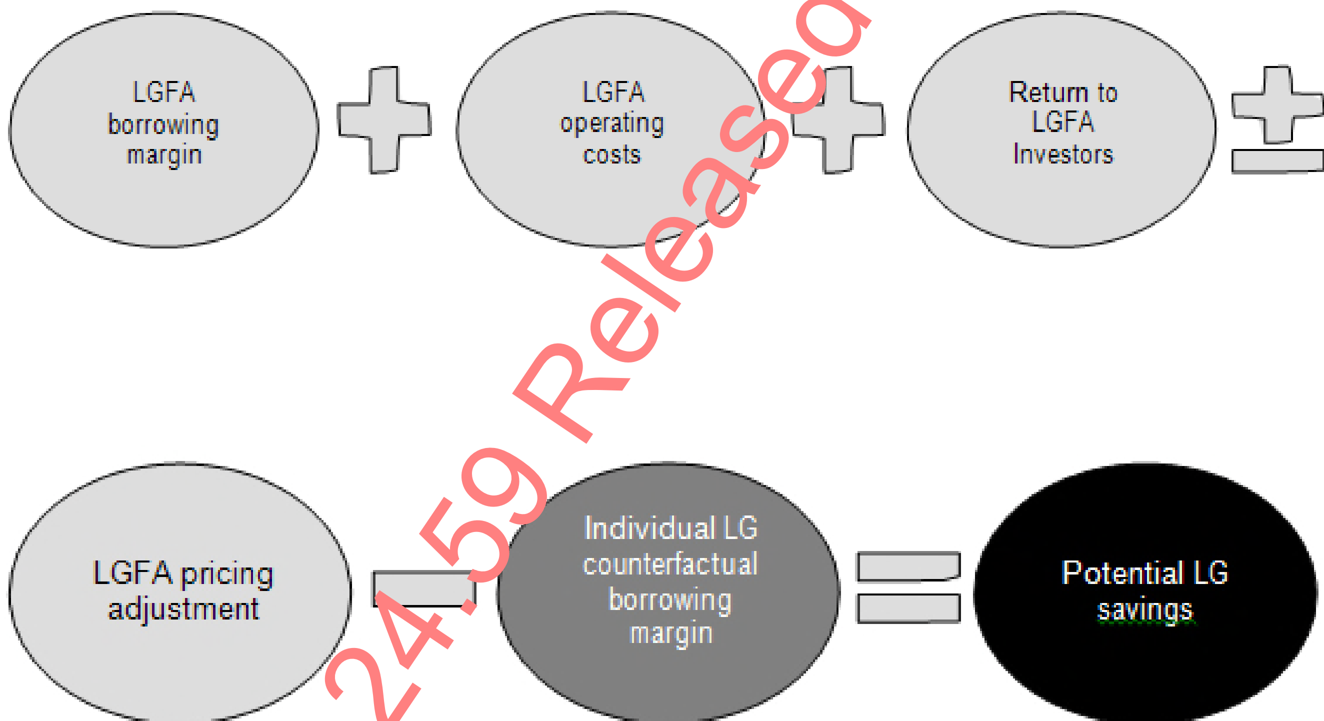
[1] A "bp" is a "basis point", which is a term that means "0.01%". 200 bps therefore refers to 2% of the amount invested.

WDC 23.24.59 Released under LGOIMA

81. Any local authority investor in Establishment Shares will also be required to subscribe for the same amount of Uncalled Capital in the LGFA. This Uncalled Capital can be called at the discretion of the LGFA under certain circumstances to ensure the ongoing viability of the LGFA. Once called the Uncalled Capital is called, it will have the same characteristics as Establishment Shares. This is an additional risk (and therefore contingent cost) for Principal Shareholding Local Authorities. Uncalled Capital is discussed in more detail in paragraphs 38 to 39 above.

Annex 1

DIAGRAM SHOWING FACTORS AFFECTING POTENTIAL SAVINGS



WDC 23.24.59 Released under LGOMA

TABLE SHOWING ANTICIPATED PRICING BENEFITS

Cameron Partners and APRM have developed a detailed financial model of the LGFA Scheme and analysed the current debt markets. The following table summarises the potential savings for local authorities depending on their credit status and based on conditions prevailing at December 2010 and a number of assumptions regarding the LGFA (including its credit rating and the amount of loans it makes to local authorities).

Potential LGFA 5 Year Pricing Benefits (all bps*)						
LA Borrowers	LGFA Borrowing Margin	LGFA Operating Costs & Investor Returns	LGFA Pricing Adjustment	LGFA Pricing	Standalone LA Borrowing Rate	Potential LA Savings
AA+ rated	65	25	-10	80	120	40
AA rated	65	25	-5	85	125	40
AA- rated	65	25	0	90	130	40
A+ rated	65	25	5	95	135	40
A rated	65	25	10	100	140	40
Un-rated	65	25	15	105	155	50
As at December 2010						

* A "bp" is a "basis point", which is a term that means "0.01%".

WDC 23.24.59 Released under LGOIMA

Appendix 2

WDC 23.24.59 Released under LGOIMA

LIST OF ACTIONS FOR JOINING THE LGFA

1. LGFA notified of Westland's desire to join. This prompts LGFA to commence two processes:
    - The first is a credit analysis of Westland, and the
    - Second is an application for Westland to be accorded "Eligible Investor" status under the Securities Act.

Credit analysis takes about a week, but that a lot longer can be required if more than one Council is joining at the same time. For example, 3-4 weeks was not enough for one Council because a number of other Councils were joining at the same time.

The "Eligible Investor" application takes 2-3 weeks. Either way, the LGFA should be notified as soon as possible to get these processes under way.

2. Russell McVeagh (LGFA lawyers) are provided with Westland's Debenture Trust Deed and Registry Agreement, (refer to note 1) which they review and then provide a required list of amendments. Allow 2-3 weeks for this.

3. Then Council's lawyers prepare the required amendments (if any). This can be done within a few days.

4. Amendments are negotiated with the Registrar and Trustee. This can be done within a few days.

5. Russell McVeagh prepare accession documentation and Council lawyers review. This can be done within a few days.

6. Council lawyers prepare various ancillary documentation and Russell McVeagh reviews. This can be done within a few days.

7. Council lawyers send all documents out for signing. Elected members need to sign some documents, so this is sometimes held up a bit by constraints on their availability.

8. Council lawyers and Russell McVeagh check all documents as they come back. This is usually done within a day.

9. Council lawyers arrange for security stock to be issued and get registrar extracts. This can be done within a day.

10. Westland provides its Annual Rates Income number for the year ended 30 June. (This can be done any time in the process.)

11. Council lawyers prepare a legal opinion for the LGFA and the LGFA Security Trustee (Trustee Executors).

12. Council lawyers provide a conditions precedent sign-off to the LGFA Security Trustee.