

Report 11.539
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Committee Council
Author Mike Timmer, Treasurer

Local Government Funding Agency update

1. Purpose

To provide the Council with an update on the Local Government Funding Agency (LGFA) and to seek Council ratification of the Directors' appointments to LGFA.

2. The decision-making process and significance

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

2.1 Significance of the decision

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.

3. Background

The LGFA has been established with the sole aim of reducing the borrowing costs to Local Authorities.

It has the support of the Crown as a shareholder. Further, the Debt Management Office/Treasury is supplying a substantial line of credit to provide liquidity support.

A group of nine Councils or the 'tight nine' have been promoting and steering the establishment of the LGFA. The Councils are:

Auckland Council
Christchurch City Council
Greater Wellington Regional Council
Hamilton City Council
Tasman District Council
Tauranga City Council
Wellington City Council
Western Bay of Plenty District Council
Whangarei District Council.

4. Update on Progress

Since the previous report on this matter in June (Report 11.273), a number of milestones have been reached towards completion of the establishment of the LGFA.

Legislation

A key milestone was the passing of legislation (Local Government Borrowing Act 2011) on 19 September 2011 after its introduction to the House on 6 April 2011.

This legislation enacted the LGFA. The LGFA will be formally constituted as a company in late November or early December 2011

Funds contributed

The Council recently contributed \$100,000 toward LGFA establishment costs; this brings the total contributed to \$200,000. It was initially agreed that this amount, less the first \$50,000, would be refunded prior to our capital contribution. Recently the decision on the \$50,000 being a sunk cost has been revisited, due mainly to the efforts of the 'tight nine' and the strong support by the sector. At this juncture we are expecting the \$50,000 to be returned to us.

Personal appointment

Craig Stobo has been appointed as Chair of the LGFA Establishment Board and more recently six other directors have been identified, who will be formally appointed on establishment of the LGFA.

Two directors are from the Local Authorities, with the balance as independents. A brief description of each of them is attached as **Attachment 1**.

The selection process has been undertaken with the assistance of Hobson Leavy an executive search agency. The process followed is attached as **Attachment 2**.

The 'tight nine' will become the founding members of the Shareholders Council. This body will monitor the LGFA, receive the SOI from the LGFA, and provide a communication link between the sector and the LGFA. The

inaugural Chair of this Council is Mathew Walker, Chief Financial Officer of Hamilton City Council.

As a minority shareholder, Greater Wellington has the right to vote on the election of Directors but with limited influence in their selection. Officers have carefully followed the process to ensure fairness and transparency in the selection of the Directors.

Support from the Local Authority sector

The current update on support from the sector is as follows:

- 19 Initial shareholders, composed of the “tight nine” and 10 other Councils
- 17 Councils have indicated they want to become shareholders in June 2012
- 14 Councils indicated they will become borrowers/guarantors of the LGFA.

This totals 50 Councils out of approximately 78 Local Authorities, 64% by number, however, this will be in the vicinity of 80-90% by level of debt.

Capital Contribution and Dividend

Initial establishment capital of the LGFA has been set at \$25 million, with the Crown contributing \$5 million and the balance coming from the Local Authorities.

At this point our capital contribution has not been determined pending the finalisation of the actual shareholder contributions of the other contributors, principally the non ‘tight nine’ members. This will be finalised in the near future and our capital contribution may reduce going forward, as other Councils join and wish to obtain shares.

This reduction may be on a pro-rata basis or as agreed between Councils wanting shares and those wanting to offload shares. It is envisaged that the ‘tight nine’ would retain a majority by shareholding after all shares are allocated.

It is expected that Greater Wellington’s final shareholding is likely to be in the range of 7% to 9%, being around \$2 million of the \$25 million initial capital subscription.

The business case for the LGFA has been updated and a draft SOI has been prepared. The business case is presently indicating that a dividend on capital contributed will not be paid by the LGFA until 2013. A reduced dividend is forecast to be paid in 2013, with a full dividend paid from 2014 onwards.

Rating Agencies and expected saving from the LGFA

Fitch has met with each of the ‘tight nine’ Councils to obtain an understanding of our businesses as part of its due diligence to give a rating to the LGFA. Standard & Poor’s have a much higher sector profile than Fitch, with Fitch only currently rating one Council. This could be an opportunity for them to

gain more business in the sector given Standard & Poor's current monopoly. It is anticipated that at two credit ratings will be available before the LGFA is incorporated.

The expected saving (about 40 points (0.40%) for a 5 year term borrowing) from using the LGFA presented in the amendment to the 2009/19 LTCCP is still current. If anything it may have improved slightly. Over time, once the LGFA has developed a track record of debt issuance, it is likely further benefits of cheaper funding may exist.

Security arrangements and LGFA documents

We are in the final stages of completing the documentation for the Debenture Trust Deed, which will enable our lenders to receive a charge over our rates and rates revenue. The Debenture Trust Deed will replace the Negative Pledge Deed and is a prerequisite for borrowing from the LGFA.

We have appointed Trustee Executors as Trustee who will monitor our financial performance and hold the security on behalf of the lenders each time we borrow funds.

The security documents will be approved and signed by the CEO as per previous delegations by Council.

Documents to recognise the relationship and rules around dealing with the LGFA are currently in draft form and are close to being finalised. They have been prepared for the LGFA by Russell McVeagh from high level commercial terms negotiated by the Shareholder Council. The documents are being reviewed by Simpson Grierson and the 'tight nine' on behalf of the all Local Authorities.

Future progress

The 'tight nine' are meeting on 26 October 2011 to finalise the draft suite of foundation LGFA documents referred to above.

In late October we expect the foundation documents and the SOI to be finalised.

In early November we anticipate approval from the Debenture Trustee, Local Authorities and the Registry Agents that the form of Security issued to the LGFA will be acceptable to all. Documents with the Debt Management Office will also be finalised at this point.

Later in the month we expect the all documents including those involving the security trustee will be confirmed/finalised and the final SOI will be then be formally issued to all shareholders.

In early November we anticipate that credit rating(s) will be received. At this point a letter from the Chair of the Establishment LGFA will indicate the credit ratings are the same as the New Zealand Government and the documents will be ready for Local Authority signing, followed by capital subscription and LGFA creation later in the month or in early December.

The inaugural issuance of debt should be some time after this.

5. Recommendations

That the Council:

- 1. **Receives** the report.*
- 2. **Notes** the content of the report.*
- 3. **Ratifies** the appointment of the six Directors to the LGFA as set out in **Attachment 1**.*

Report prepared by:

Report approved by:

Mike Timmer
Treasurer

Bruce Simpson
Chief Financial Officer

Attachment 1: LGFA Director Profiles

Attachment 2: Search Process – Director Appointments, LGFA