LOCAL GOVERNMENT FUNDING AGENCY

Department: Legal

REASONS FOR CONFIDENTIALITY

Grounds:	S48(1)(a) - The public conduct of the part of the meeting would be likely to result in the disclosure of information for which good reason for withholding exists under section 7.
Reason:	S7(2)(g) - The withholding of the information is necessary to maintain legal professional privilege.
	S7(2)(h) - The withholding of the information is necessary to enable the local authority to carry out, without prejudice or disadvantage, commercial activities.
	S7(2)(i) - The withholding of the information is necessary to enable the local authority to carry on, without prejudice or disadvantage, negotiations (including commercial and industrial negotiations).

EXECUTIVE SUMMARY

1 Council has resolved to join the New Zealand Local Government Funding Agency Limited (**LGFA**) borrowing programme as a Guaranteeing Local Authority.

2 Dunedin City Treasury Limited (**DCTL**), a wholly owned subsidiary of Dunedin City Holdings Limited (**DCHL**), has also resolved to join LGFA as a CCO Issuer.

3 This report outlines the documentation that the Council is required to sign for:

a) the Council to join LGFA; and

b) DCTL to join LGFA.

4 A formal resolution approving the documentation is required before the documents are entered into by the Council.

5 The documentation includes:

a) Accession Deeds to LGFA's Multi-issuer Deed, Notes Subscription Agreement and Equity Commitment Deed in relation to the Council's accession to LGFA;

b) Accession Deeds to LGFA's Multi-issuer Deed and Notes Subscription Agreement in relation to DCTL's accession to LGFA;

c) an Accession Deed to the Guarantee and Indemnity in relation to the Council's accession to LGFA;

d) a Debenture Trust Deed; and

e) Security Stock Certificates in relation to the Security Stock that will be issued as a part of the Council's accession to LGFA.

6 Once Council and DCTL have joined LGFA, DCTL will be able to borrow funds from LGFA. LGFA will then be an additional potential source of funding for DCTL, who on-lend to DCC and DCHL group entities.

RECOMMENDATIONS

That the Council:

a) **Approves** the following documents:

i) Document 1: Debenture Trust Deed between Council and Trustees Executors Limited;

ii) Document 2: Registrar and Paying Agent Services Agreement between Council and Computershare Investor Services Limited;

iii) Document 3: Accession Deed to Multi-issuer Deed between Council and New Zealand Local Government Funding Agency Limited;

iv) Document 4: Accession Deed to Notes Subscription Agreement between Council and New Zealand Local Government Funding Agency;

v) Document 5: Accession Deed to Guarantee and Indemnity between Council and TEL Security Trustee (LGFA) Limited;

vi) Document 6: Accession Deed to Equity Commitment Deed between Council and New Zealand Local Government Funding Agency Limited;

vii) Document 7: Chief Executive Certificate under section 118 of the Local Government Act 2002 in relation to the four accession deeds, three security stock certificates and the stock issuance certificate involved in the Council's accession to the New Zealand Local Government Funding Agency;

viii) Document 8: Chief Executive Certificate under section 118 of the Local Government Act 2022 in relation to the Debenture Trust Deed and the Registrar and Paying Agent Services Agreement;

ix) Document 9: Security Stock Certificate number 1 – evidencing the issue of security stock to New Zealand Local Government Financing Agency Limited to secure Council's obligations to New Zealand Local Government Funding Agency Limited under the Multi-Issuer Deed and related Accession Deed;

x) Document 10: Security Stock Certificate number 2 – evidencing the issue of security stock to New Zealand Local Government Financing Agency Limited to secure Council's obligations to New Zealand Local Government Funding Agency Limited under the Equity Commitment Deed and related Accession Deed;

xi) Document 11: Security Stock Certificate number 3 – evidencing the issue of security stock to TEL Security Trustee (LGFA) Limited to secure Council's obligations to TEL

Security Trustee (LGFA) Limited under the Guarantee and Indemnity and related Accession Deed;

xii) Document 12: Stock Issuance Certificate, as required by the terms of the Debenture Trust Deed, in relation to the secuity stock to be issued to New Zealand Local Government Funding Agency Limited and TEL Security Trustee (LGFA) Limited;

xiii) Document 13: Shareholder's resolution and entitled person's agreement in relation to Dunedin City Treasury Limited's accession to the New Zealand Local Government Funding Agency;

xiv) Document 14: Accession Deed to Multi-Issuer Deed between Dunedin City Treasury Limited and New Zealand Local Government Funding Agency Limited;

xv) Document 15: Accession Deed to Notes Subscription Agreement between Dunedin City Treasury Limited and New Zealand Local Government Funding Agency Limited;

xvi) Document 16: Agreement between Council and Dunedin City Treasury Limited recording that, if Borrower Notes are to be converted to redeemable preference shares in New Zealand Local Government Funding Agency Limited, a fair market value for the transfer of the Borrower Notes will be agreed by Council and Dunedin City Treasury Limited at the time immediately prior to the conversion.

xvii) Document 17: Chief Executive Certificate under section 118 of the Local Government Act 2022 in relation to the Council's acknowledgement of the Accession Deed to Multi-issuer Deed and Accession Deed to Notes Subscription Agreement involved in Dunedin City Treasury Limited's accession to the New Zealand Local Government Funding Agency.

b) **Delegates** to the Mayor and any elected member, or to any two elected members, the authority to sign Documents 1- 6 (inclusive) and Documents 13 – 16 (inclusive) on behalf of the Council.

c) **Delegates** to Council's Chief Executive Officer the authority to sign Documents 7 – 12 (inclusive) and Document 17.

d) **Delegates** to Council's Chief Executive Officer, in consultation with Council's solicitors, the authority to execute such other documents and take such other steps on behalf of the Council as the Chief Executive Officer considers is necessary or desirable to execute or take to give effect to the accession of Council and Dunedin City Treasury Limited to the New Zealand Local Government Funding Agency.

e) **Designates** the Council's Chief Executive Officer as the spokesperson in relation to joining the New Zealand Local Government Funding Agency.

BACKGROUND

LGFA

7 LGFA is a limited liability company established to borrow funds and then on-lend those funds to local authorities and (now) Council Controlled Organisations (**CCOs**). Although LGFA was established in 2011, it is only in recent years that LGFA has agreed to lend funds to CCOs.

8 LGFA's shares are held entirely by central government and local authorities. Central government currently holds 20% of the paid-up ordinary shares in LGFA, with the remaining 80% being held by 30 local authorities (**Principal Shareholding Local Authorities**). Given its ownership structure, LGFA is itself a CCO.

9 LGFA has a long-term foreign currency credit rating of AA+ and a long-term local currency credit rating of AAA from Standard & Poor's. The Crown does not guarantee the obligations of LGFA, but LGFA has a $1.5b Crown liquidity facility and holds a certain amount of cash and other liquid investments to safeguard against short term default risks. Long term default risks are managed by a variety of mechanisms, including a requirement that all local authorities:

a) that want to borrow more than $20 million from LGFA; and/or

b) hold an interest in a CCO that wants to borrow from LGFA directly (regardless of the amount being borrowed by the CCO from LGFA),

must have acceded to LGFA as a Guaranteeing Local Authority (please see later in this report for an overview of the LGFA Guarantee and Indemnity).

10 Information published by LGFA in January this year records that 74 local authorities and one CCO have joined LGFA.

Current Financial Arrangements

11 Council's current borrowing is solely from Dunedin City Treasury Limited (**DCTL**). This borrowing is unsecured. However, Dunedin City Holdings Limited (**DCHL**), the sole shareholder in DCTL, can call on the Council for unpaid and uncalled capital in DCHL.

12 DCTL borrows its funds from external investors. DCTL then on-lends to Council and the DCHL group of companies (**DCC Group**).

13 DCTL has not previously borrowed from LGFA. This is because DCTL has not previously been a member of LGFA (LGFA initially only lent to Local Authorities, but, in 2020, LGFA changed the terms of the documents for its borrowing programme to allow CCO's to join LGFA and borrow directly from LGFA).

14 There is currently a debenture in place between DCTL, DCHL and Aurora Energy Limited in favour of ANZ Bank New Zealand Limited (**ANZ**) as security agent. The debenture provides security for all DCTL's external investors by securing their lending against the assets of DCHL, DCTL and Aurora (including DCHL's uncalled capital, and its shares in other subsidiary and associate companies).

15 There is a cross guarantee from and between DCTL, Dunedin City Holdings Limited and Aurora Energy Limited.

Proposed Financial Arrangements

16 Under the proposed financial arrangements:

a) Council would join LGFA as an Issuer and Guaranteeing Local Authority;

b) DCTL would join LGFA as a CCO Issuer;

c) Council would continue to borrow its funds from DCTL; and

d) LGFA would be added as an additional potential source of funding for DCTL.

17 As part of the process, LGFA will become a "beneficiary" under the existing debenture granted by DCTL, DCHL and Aurora Energy Limited alongside the other external investors DCTL currently sources its funds from.

18 By joining LGFA as an Issuer and Guaranteeing Local Authority, Council:

a) would have the option of borrowing directly from LGFA if it chose to do so; and

b) will guarantee LGFA's obligations to LGFA's creditors (please see later in this report for an overview of the LGFA Guarantee and Indemnity).

Previous Council resolutions and Annual Plan consultation

19 On 29 January 2019, there was a report to Council called "Review of Borrowing Arrangements". That report attached a report dated January 2019 by Bancorp (**Bancorp Report**). Council resolved as follows:

Moved (Cr Mike Lord/Cr Doug Hall):

That the Council:

a) ***Approves*** *DCC supporting DCHL/DCTL in their application to add LGFA to its potential funding sources.*

b) ***Requests*** *DCHL to work with DCC to review the necessary arrangements to allow LGFA to be a potential funding source for DCC and DCC CCOs.*

c) ***Notes*** *the independent report formally recognises the benefits that the current lending structures have provided DCC to date and highlights that "DCC, through the DCTL structure, operates its Treasury function via a market 'best practice' framework".*

Division

The Council voted by division.

For:	*Crs David Benson-Pope, Rachel Elder, Christine Garey, Doug Hall, Aaron Hawkins, Marie Laufiso, Mike Lord, Damian Newell, Jim O'Malley, Chris Staynes, Conrad Stedman, Lee Vandervis, Kate Wilson and Dave Cull (14).*
Against:	*Nil*

The division was declared CARRIED by 14 votes to 0

Motion carried (CNL/2019/012)

20 In the 2020/21 Annual Plan process, Council consulted on whether Council should join LGFA as a Guaranteeing Local Authority.

21 Council received a total of 623 feedback forms indicating support or otherwise to the proposal for Council to join LGFA as a Guaranteeing Local Authority. Of the 623 feedback forms, 72% supported the proposal and 28% did not support the proposal.

22 On 27 May 2020, there was a report to the Annual Plan Deliberations meeting called "Local Government Funding Agency – Summary of Feedback and Next Steps". Council resolved:

Moved (Cr Marie Laufiso/Cr Rachel Elder):

That the Council:

*a) **Notes** community feedback on Council's proposal to join the Local Government Funding Agency (LGFA) as a Guaranteeing Local Authority.*

*b) **Approves** that the Dunedin City Council join the LGFA as a Guaranteeing Local Authority.*

***Motion carried (AP/2020/012)** with Cr Radich recording his vote against.*

Council's Treasury Risk Management Policy

23 Council's Treasury Risk Management Policy (**TRM Policy**) records that DCTL may borrow from LGFA and, in connection with that borrowing, may enter into any agreement to the extent considered appropriate. The TRM Policy also records that:

a) DCTL may contribute a portion of the borrowing back to LGFA as an equity contribution to LGFA.

b) Council may provide a guarantee over indebtedness to LGFA.

c) Council may accept a transfer from DCTL of borrower notes issued by LGFA.

d) Council may contribute additional equity (or subordinated debt) to LGFA if required.

e) Council may secure its borrowings from LGFA and the performance of other obligations to LGFA or its creditors with a charge over DCC's rates and revenue (using a debenture trust deed).

f) Council may subscribe to the shares and uncalled capital of LGFA.

g) Council and/or the DCC Group will comply with the relevant financial covenants and ratios required by LGFA.

24 The TRM Policy was one of the documents provided as part of the Ten Year Plan 2021-31 consultation process.

DISCUSSION

Terminology

25 The process of joining the LGFA is called "accession", with the relevant local authority (or CCO) "acceding" to LGFA.

Discussions with LGFA

26 Council is in a different situation to almost all 74 Councils that have already acceded to LGFA. This is because Council has a treasury company (DCTL) and intends to continue using DCTL for its borrowing. LGFA will therefore be lending to DCTL rather than the Council directly.

27 It has taken some time to work through LGFA's requirements for lending to DCTL because LGFA has only lent to one CCO to date, so the process is reasonably new.

28 DCTL and LGFA have now agreed on the terms of DCTL's accession to LGFA and wish to proceed with acceding to LGFA.

Legal Advice

29 Simpson Grierson is acting for Council and DCTL and has provided legal advice to Council and DCTL on their respective accessions to LGFA.

30 Simpson Grierson has acted for many Councils in the accession process.

31 Simpson Grierson has prepared an Information Memorandum on LGFA. This is attached as Attachment A.

Documentation required for Council to accede to LGFA

32 For Council to accede to LGFA, Council will need to sign a package of 12 documents (**LGFA Financing Documents**).

33 The LGFA Financing Documents are listed later in this report.

34 The following paragraphs provide an overview of the key LGFA Financing Documents. This overview identifies certain risks associated with the LGFA Financing Documents. Simpson Grierson has identified mitigating factors for these risks.

The Accession Deeds

35 Prior to acceding to LGFA, Council must sign an Accession Deed for each of the following four documents:

a) A Multi-issuer Deed dated 7 December 2011 (as amended and restated from time to time) between LGFA and various local authorities (**Multi-issuer Deed**).

b) A Notes Subscription Agreement dated 7 December 2011 (as amended and restated from time to time) between LGFA and various local authorities (**Notes Subscription Agreement**).

c) Guarantee and Indemnity dated 7 December 2011 (as amended and restated from time to time) between TEL Security Trustee (LGFA) Limited and various local authorities (**Guarantee and Indemnity**).

d) Equity Commitment Deed dated 7 December 2011 (as amended and restated from time to time) between LGFA and various local authorities (**Equity Commitment Deed**).

Multi-issuer Deed

36 Under the Multi-issuer Deed, local authorities and CCOs can issue debt as an issuer. Therefore, if Council and DCTL accede to LGFA, the Council and/or DCTL could issue debt as an issuer.

37 While all parties to this transaction are expecting that all DCC funding will continue to be via DCTL, it is possible that DCC could borrow directly from LGFA if Council decided at a future date that this is preferred. The Bancorp Report advised that the current model of funding via DCTL is "best practice", so there is no current proposal to change this model.

Notes Subscription Agreement

38 Under the Notes Subscription Agreement, local authorities and CCOs that borrow from LGFA subscribe for "Borrower Notes". The Borrower Notes are for an amount equal to 2.5% of the borrowed amount.

39 In circumstances where LGFA is financially distressed, these "Borrower Notes" can be converted to redeemable preference shares in LGFA, making the relevant local authority a shareholder of LGFA.

40 Only a local authority can be a shareholder in LGFA. Accordingly, if the "Borrower Notes" are held by a CCO (for example, DCTL), immediately prior to their conversion the "Borrower Notes" are transferred to the shareholding local authority so that, upon conversion, the redeemable preference shares are issued to the local authority.

41 Although it is highly unlikely that there would ever need to be a transfer of Borrower Notes from DCTL to Council, Council will need to consider now whether any consideration would be payable if the event arises and, if so, whether that consideration is to be agreed upfront or addressed only if the event arises.

42 Council staff recommend that it would be prudent to agree the compensation arrangements upfront with DCTL. The compensation could be agreed as being:

a) a non-cash value (on the understanding that the transfer of the Borrower Notes is just a part of the Council support provided to DCTL); or

b) a financial value. The value of the notes (at the time of transfer) cannot be determined now, so the financial value could be determined at the time of transfer:

i) by a methodology that is agreed now; or

ii) by agreement and, failing agreement, by an independent expert; or

iii) by agreement and, failing agreement, at a non-cash value (ie without payment by Council).

43 Council staff recommend that Council enter into an upfront agreement with DCHL that records that, in the unlikely event that Borrower Notes need to be transferred to Council, a fair market value for the transfer of the Borrower Notes will be agreed by Council and DCTL at the time immediately prior to the conversion.

Guarantee and Indemnity

44 Under the Guarantee and Indemnity, local authorities provide a guarantee of LGFA's payment obligations to LGFA's creditors. This guarantee is held on trust (for those creditors) by TEL Security Trustee (LGFA) Limited. Demand for payment can be made under the guarantee when LGFA defaults on its payment obligations to LGFA's creditors.

45 Council will become a party to the LGFA Guarantee and Indemnity as a part of its accession to LGFA and, as such, may be subject to a call under the guarantee if LGFA defaults on its obligations to its creditors.

46 The risk of a call under the Guarantee and Indemnity is considered low (given the safeguards put in place to reduce the likelihood of a LGFA default occurring, such as the ability for LGFA to call for further capital from existing shareholders and the $1.5b Crown liquidity facility).

47 The amount payable following a call under the guarantee is proportionate to the rates revenue of all other local authorities that are also guaranteeing LGFA's debts (which is currently 66 other Councils).

Equity Commitment Deed

48 Under the Equity Commitment Deed, local authorities may be required to contribute additional capital to LGFA by subscribing for shares in LGFA in circumstances where LGFA is financially distressed.

49 Although Council will become a party to the Equity Commitment Deed as a part of its accession to LGFA, the risk of Council having to subscribe for shares in LGFA is considered low.

Other key documents

Debenture Trust Deed

50 For Council to accede to LGFA, it will need to sign the Debenture Trust Deed between Council and Trustees Executors Limited (**Debenture Trust Deed**).

51 Under the Debenture Trust Deed, Council will grant a security interest over its rates and rates revenue, with that security interest held by Trustees Executors Limited for the benefit of stockholders. If Council were to default on its obligations to a stockholder, Trustees Executors Limited could (on behalf of the relevant stockholder) enforce the charge over Council's rates and rates revenue.

52 For example, if Council did not comply with its obligations under the Guarantee and Indemnity, Trustees Executors Limited could enforce the security over Council's rates and rates revenue on behalf of TEL Security Trustee (LGFA) Limited (as a holder of security stock) to recover the amounts outstanding. In enforcing the security, Trustees Executors Limited could appoint a receiver to Council under the Debenture Trust Deed and that receiver could look to assess and collect a rate sufficient to provide for the payment of the outstanding amount (in accordance with section 115 of the Local Government Act 2002).

Registrar and Paying Agent Services Agreement between Council and Computershare Investor Services Limited

53 Under the Registrar and Paying Agent Services Agreement, Computershare Investor Services Limited will keep a record of all stock issued by Council and advise when payments are due. Given that Council will not be issuing stock (beyond the security stock that Council is required to issue to LGFA and TEL Security Trustee (LGFA) Limited as a part of Council's accession to LGFA), Computershare should have little to do for Council.

54 DCTL will have a separate agreement with Computershare.

List of the LGFA Financing Documents

55 The LGFA Financing Documents are:

a) Document 1: Debenture Trust Deed between Council and Trustees Executors Limited;

b) Document 2: Registrar and Paying Agent Services Agreement between Council and Computershare Investor Services Limited;

c) Document 3: Accession Deed to Multi-issuer Deed between Council and LGFA;

d) Document 4: Accession Deed to Notes Subscription Agreement between Council and LGFA;

e) Document 5: Accession Deed to Guarantee and Indemnity between Council and TEL Security Trustee (LGFA) Limited;

f) Document 6: Accession Deed to Equity Commitment Deed between Council and LGFA;

g) Document 7: Chief Executive Certificate under section 118 of the Local Government Act 2002 in relation to the four accession deeds, three security stock certificates and the stock issuance certificate involved in the Council's accession to the LGFA;

h) Document 8: Chief Executive Certificate under section 118 of the Local Government Act 2002 in relation to the Debenture Trust Deed and the Registrar and Paying Agent Services Agreement;

i) Document 9: Security Stock Certificate number 1 – evidencing the issue of security stock to LGFA to secure Council's obligations to LGFA under the Multi-Issuer Deed and related Accession Deed;

j) Document 10: Security Stock Certificate number 2 – evidencing the issue of security stock to LGFA to secure Council's obligations to LGFA under the Equity Commitment Deed and related Accession Deed;

k) Document 11: Security Stock Certificate number 3 – evidencing the issue of security stock to TEL Security Trustee (LGFA) Limited to secure Council's obligations to TEL Security Trustee (LGFA) Limited under the Guarantee and Indemnity and related Accession Deed;

l) Document 12: Stock Issuance Certificate, as required by the terms of the Debenture Trust Deed between Council and Trustees Executors Limited in relation to the security stock to be issued to LGFA and TEL Security Trustee (LGFA) Limited.

56 As set out earlier in this report, Council will need to sign all of the LGFA Financing Documents if it wants to accede to the LGFA (ie Council will need to sign all 12 documents).

57 Documents 1-6 will need to be signed by Council. Documents 7-12 will need to be signed by Council's Chief Executive Officer.

58 The LGFA Financing Documents are further described in the table attached as Attachment B.

59 A copy of the Financing Documents will be made electronically available to elected members, together with a copy of the most recent versions of the:

a) Multi-Issuer Deed;

b) Notes Subscription Agreement;

c) Guarantee and Indemnity; and

d) Equity Commitment Deed.

Summary of Council's ongoing obligations

Reporting

60 Under the Debenture Trust Deed, Council has certain ongoing obligations to Trustees Executors Limited, including certain reporting obligations.

61 Council also has certain ongoing obligations under the Multi-Issuer Deed, including an obligation to provide LGFA with copies of all information provided to Trustees Executors Limited under the reporting provisions in the Debenture Trust Deed.

Financial covenants

62 Council will need to comply with the financial covenants set out in the Multi-issuer Deed and provide LGFA with a compliance certificate (certifying compliance with those covenants) when Council delivers its financial statements for the preceding financial year to LGFA. The financial covenants recorded in the Multi-issuer Deed are the ratio that:

a) Net Debt bears to Total Revenue;

b) Net Interest bears to Total Revenue;

c) Net Interest bears to Annual Rates Income; and

d) Available Financial Accommodation bears to External Indebtedness.

63 The applicable ratios are set by LGFA and, in the case of Council, LGFA has confirmed that the ratio that:

a) Net Debt bears to Total Revenue (expressed as a percentage) must not exceed 300% for 2021/22 year and then 295% for 2022/23 year, 290% for 2023/24, 285% for 2024/25 and 280% thereafter;

b) Net Interest bears to Total Revenue (expressed as a percentage) must not exceed 20%;

c) Net Interest bears to Annual Rates Income (expressed as a percentage) must not exceed 30%; and

d) Available Financial Accommodation bears to External Indebtedness (expressed as a percentage) must not exceed 110%.

64 The above percentages match those in the Treasury Risk Management Policy.

65 The financial covenants will be tested on a DCC Group basis.

Representations, warranties and undertakings

66 Council will need to comply with representations, warranties and undertakings (each of which are typical for financing documents) under the LGFA Financing Documents. These include such representations, warranties and undertakings as confirming the legal authority to meet obligations under the Financing Documents and there being no events of default.

DCTL's accession to the LGFA

67 As set out earlier in this report:

a) once Council has acceded to LGFA, DCTL can accede to LGFA; and

b) following DCTL’s accession to LGFA, DCTL will be able to borrow directly from LGFA.

68 Council should be aware of the following:

a) Council will need to enter into new contracts (ie in addition to the LGFA Financing Documents) as a part of DCTL’s accession to LGFA (**DCTL Accession Documentation**) (please see the list of documents below);

b) in connection with DCTL’s accession, LGFA will require “CCO Credit Support” to be provided. To provide this “CCO Credit Support”, the benefit of DCTL’s existing debenture will need to be extended to LGFA and the amount of uncalled capital held by DCHL has been increased to $1,200,000; and

c) DCTL would only be able to borrow from LGFA to the extent that the amount borrowed would be less than or equal to the amount of uncalled capital subscribed for by Council. If DCTL needed to borrow further funds from LGFA (so that the amount borrowed would exceed the amount of uncalled capital held by Council), Council would need to consider subscribing for further uncalled capital in DCTL.

69 The DCTL Accession Documents are:

a) Document 13: Shareholder’s resolution and entitled person’s agreement in relation to DCTL’s accession to LGFA;

b) Document 14: Accession Deed to Multi-issuer Deed between DCTL and LGFA;

c) Document 15: Accession Deed to Notes Subscription Agreement between DCTL and LGFA;

d) Document 16: Agreement between Council and DCTL recording that, if Borrower Notes are to be converted to redeemable preference shares in LGFA, a fair market value for the transfer of the Borrower Notes will be agreed by Council and DCTL at the time immediately prior to the conversion; and

e) Document 17: Chief Executive Certificate under section 118 of the Local Government Act 2002 in relation to the Council's acknowledgement of the Accession Deed to Multi-issuer Deed and Accession Deed to Notes Subscription Agreement between DCTL and LGFA.

70 Council will need to sign all of the DCTL Accession Documents so that DCTL can accede to LGFA (ie Council will need to sign all four documents).

71 Documents 13 – 16 (inclusive) will need to be signed by Council (by the Mayor and one elected member, or two elected members).

72 The DCTL Accession Documents are further described in the table attached as Attachment B and a copy of the DCTL Accession Documents will be made electronically available to elected members.

73 DCTL, DCHL and Aurora Energy Limited have approved all the documents and transactions required for DCTL to accede to LGFA. A meeting of the beneficiaries of the debenture will be called for 29 September 2022 to seek approval for the required changes to enable LGFA to benefit from its security. This approval is required before the accession can occur.

OPTIONS

74 The two key options here are that either:

a) Council accedes to LGFA as a Guaranteeing Local Authority by signing the LGFA Financing Documents and signs the DCTL Accession Documents so that DCTL can accede to LGFA; or

b) Council retains the status quo and does not accede to the LGFA and does not sign the DCTL Accession Documents.

Option One – Recommended Option - Council accedes to the LGFA as a Guaranteeing Local Authority by signing the LGFA Financing Documents and signs the DCTL Accession Documents so that DCTL can accede to LGFA

75 Under this option, Council would:

a) Approve the LGFA Financing Documents.

b) Approve the DCTL Accession Documents.

c) Delegate to the Mayor and any elected member, or to any two elected members, the authority to sign Documents 1- 6 (inclusive) and Documents 13 – 16 (inclusive) on behalf of Council.

d) Delegate to Council's Chief Executive Officer the authority to sign Documents 7 – 12 (inclusive) and Document 17.

e) Delegate to the Council's Chief Executive Officer, in consultation with Council's solicitors, the authority to execute such other documents and take such other steps on behalf of the Council as the Chief Executive Officer considers is necessary or desirable to execute or take to give effect to the accession of Council and DCTL to LGFA.

f) Designate the Council's Chief Executive Officer as the spokesperson in relation to joining the LGFA.

Advantages

- This option would allow both Council and DCTL to accede to the LGFA borrowing programme. Council must accede to LGFA before LGFA will allow DCTL to accede to the LGFA.

- DCTL would be able to borrow from LGFA, providing DCTL with a further potential source of funding compared to the status quo. Council could also choose to borrow directly from the LGFA, but this is not recommended, as the Bancorp Report advised that the Treasury model is "best practice".

- Council's and DCTL's current Standard and Poor's credit rating is premised on Council joining the LGFA. The current rating is the strongest credit rating provided to Councils in New Zealand. If Council did not join the LGFA then this may have an impact on Council's and/or DCTL's credit rating.

Disadvantages

- Council will become a party to the Guarantee and Indemnity and the Equity Commitment Deed and a call may be made under either of these documents (which presents the low level risks outlined in this report).

Option Two – Status Quo

76 Under this option, Council would retain the status quo and would not accede to LGFA.

Advantages

- Council would not take on any of the risks (albeit low level risks) associated with accession to LGFA.

Disadvantages

- DCC would not be able to borrow from LGFA and would not be able to access potentially more favourable borrowing terms.

- DCTL would not be able to accede to, or borrow from, LGFA.

- This option does not provide Council or DCTL with an additional diversified funding source and potentially lower costs of funds.

NEXT STEPS

77 If Council approves the Financing Documents and the DCTL Accession Documents then:

a) These will be signed and sent to Simpson Grierson in escrow (i.e. the Financing Documents and the DCTL Accession Documents will be held by Simpson Grierson until DCTL has confirmed that they have met all conditions to allow them to accede to the LGFA, including approval from the meeting of beneficiaries). This is so that Council and DCTL can accede to the LGFA in quick succession, meaning that Council does not assume any risk until DCTL accedes and can borrow from LGFA.

b) Council's Chief Executive Officer will liaise with LGFA regarding any media comments or releases regarding Council joining the LGFA.

78 If Council does not approve the recommendations in this report, Council staff will advise LGFA, DCHL and DCTL accordingly.

Signatories

Author:	Karilyn Canton - Chief In-House Legal Counsel
Authoriser:	Sandy Graham - Chief Executive Officer

Attachments

	Title	Page
⇩A	Legal Advice dated 8 September 2022 from Simpson Grierson to Council	38
⇩B	List of documents for signing by Council and Council's Chief Executive Officer	52

SUMMARY OF CONSIDERATIONS

Fit with purpose of Local Government

This decision promotes the economic well-being of communities in the present and for the future.

Fit with strategic framework

	Contributes	Detracts	Not applicable
Social Wellbeing Strategy	☐	☐	☒
Economic Development Strategy	☐	☐	☒
Environment Strategy	☐	☐	☒
Arts and Culture Strategy	☐	☐	☒
3 Waters Strategy	☐	☐	☒
Spatial Plan	☐	☐	☒
Integrated Transport Strategy	☐	☐	☒
Parks and Recreation Strategy	☐	☐	☒
Other strategic projects/policies/plans	☒	☐	☐

This report fits with Council's Treasury Risk Management Policy that was consulted on through Council's 10 Year Plan 2021-31 process. The Treasury Risk Management Policy records that Dunedin City Treasury Limited may borrow from the LGFA and that Council may provide a guarantee. Further details of the references to the LGFA in Council's Treasury Risk Management Policy are contained in the report.

Māori Impact Statement

No discussions have taken place with mana whenua about this decision.

Sustainability

This report could impact on Council's, and the Council Group's, long term financial results and risk profile.

LTP/Annual Plan / Financial Strategy /Infrastructure Strategy

Council consulted on joining the LGFA through the 2020/21 Annual Plan Process and the Treasury Risk Management Policy was consulted on through the 10 Year Plan 2021-31.

Financial considerations

The financial considerations are detailed in the report.

Significance

Given that the Council has already undertaken consultation processes regarding LGFA (including through the 2020/21 Annual Plan engagement process), this decision is considered low in in terms of the Council's Significance and Engagement Policy.

Engagement – external

The community has been consulted regarding the LGFA, using the Special Consultative Procedure. Council staff have had discussions with DCTL regarding LGFA's requirements for DCTL to accede to the LGFA. Simpson Grierson has provided legal advice regarding the financing documentation.

Engagement - internal

This matter has been discussed internally between the Finance and Legal Teams.

SUMMARY OF CONSIDERATIONS

Risks: Legal / Health and Safety etc.

The legal risks are outlined in this report. The key risk is that a call may be made under the guarantee of LGFA's debts. Council's share of the joint and several guarantee may change over time as the percentage of total rates incomes changes. If some councils fail to meet their obligations, other councils may be required to make up the shortfall.

Conflict of Interest

There are no known conflicts of interest.

Community Boards

There are no implications for Community Boards.

Simpson Grierson

To	Dunedin City Council	**8 September 2022**
From	Josh Cairns and Daniel Bowman, Simpson Grierson	
Subject	**New Zealand Local Government Funding Agency Limited – Information Memorandum**	

Part A – Introduction and Purpose

Purpose of Information Memorandum

1. This Information Memorandum provides a description of the structure of the New Zealand Local Government Funding Agency Limited (**LGFA**) and its debt issuance programme (**Debt Programme**). LGFA is a council controlled organisation (**CCO**), incorporated as a company, which was established to enable:

    (a) participating local authorities (**Participating Local Authorities**); and

    (b) following recent amendments to the Debt Programme, approved participating CCOs (**Participating CCOs**),

    to borrow at lower interest margins than they might otherwise pay.

2. The purpose of this Information Memorandum is to provide information to local authorities and CCOs that are considering joining the Debt Programme as shareholders, guarantors and/or borrowers (as applicable).

3. This Information Memorandum is divided into five 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, LGFA.

    (b) **Part B (How LGFA Operates):** which sets out the characteristics of LGFA.

    (c) **Part C (Costs and Benefits):** which sets out some of the costs and benefits of the Debt Programme.

    (d) **Part D (Local Authorities as Issuers):** which sets out requirements for local authorities joining the Debt Programme, including the transactions that local authorities will be required to enter into.

    (e) **Part E (CCOs as Issuers):** which:

        (i) sets out the key requirements for CCOs joining the Debt Programme;

        (ii) identifies what security is likely to be required by LGFA in relation to any particular Participating CCO; and

        (iii) identifies aspects of the Debt Programme (as it relates to CCOs) that are likely to be subject to negotiation.

Rationale for LGFA

New Zealand Local Authority debt market

4. New Zealand local authorities historically faced a number of debt-related issues. First, local authorities have significant debt requirements. Secondly, pricing, length of funding term and other terms and conditions had historically varied considerably across the sector and, prior to the establishment of LGFA, were less than optimal. This was due to:

   (a) **Limited debt sources:** Local authorities' debt funding options had been limited to the banks, private placements and wholesale bonds (issuance to wholesale investors), and, to a lesser extent, retail bonds. Increasing sector funding requirements, and domestic funding capacity constraints, had the potential to further adversely impact upon local authority debt.

   (b) **Fragmented sector:** There are 78 local authorities. Individually, a significant proportion of these local authorities lack scale.

   (c) **Regulatory restrictions:** Offshore (foreign currency) capital markets had been closed to local authorities (other than Auckland Council) and the compliance process for local authority retail bond issuance is burdensome.

Addressing the local authority debt issues

5. Each of these issues needed to be addressed to rectify this situation. This was not likely to happen without an intervention, like LGFA, for the following reasons:

   (a) New Zealand debt markets (at least in the foreseeable future) were likely to maintain the status quo.

   (b) Individually, a majority of local authorities would not have been able to attain significant scale.

   (c) At a sector level, it may have been possible to address the issue regarding regulation, but regulators were likely to remain reluctant to significantly ease restrictions on financial management without gaining significant comfort as to the sophistication of the financial management of all local authorities. And, even if this issue had been addressed by regulators, it may have been insufficient to provide a major step change.

6. LGFA was established because the homogenous nature of local authorities, the large sector borrowing requirements, and the high credit quality / strong security position (ie charges over rates) of local authorities, created an opportunity for a centralised local authority debt vehicle to generate significant borrowing benefits for local authorities.

7. There are numerous precedents globally of successful vehicles that pool local authority debt and fund themselves through issuing their own financial instruments to investors. Such vehicles (including LGFA) 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 dollar of debt raised.

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

8. The offshore precedents are typically owned by the local authorities in the relevant jurisdiction (often with central government involvement), as is the case for LGFA.

Part B – How LGFA Operates

9. In this part, we have addressed:

(a) an overview of the basic corporate structure of LGFA;

(b) LGFA's objective to minimise default risk;

(c) features of LGFA designed to reduce short term default risk;

(d) features of LGFA designed to reduce long term default risk;

(e) characteristics of LGFA and the Debt Programme that are designed to make borrowing from LGFA fair for all Participating Local Authorities and Participating CCOs; and

(f) how the viability of LGFA is dependent on participation levels.

Basic corporate structure of LGFA

10. LGFA is a limited liability company (and a CCO) established to borrow funds and then on-lend those funds to local authorities and (now) CCOs, at lower interest margins than those local authorities and CCOs would otherwise pay.

11. LGFA's shares are held entirely by central government and local authorities. Central government currently holds 20% of the paid-up ordinary shares in LGFA, with the remaining 80% being held by local authorities (**Principal Shareholding Local Authorities**).

12. The Principal Shareholding Local Authorities have contributed capital and, as compensation for their capital contribution, may receive a return on this capital. However, the over-arching objective is that the benefit of LGFA to local authorities is delivered through lower borrowing margins, rather than through dividends passed to shareholders.

13. Also, as discussed below at paragraph 27, it is possible that local authorities:

(a) that borrow from LGFA; and/or

(b) whose CCOs borrow from LGFA,

may be required to hold redeemable preference shares in LGFA.

LGFA – designed to minimise default risk

14. One of the things that is critical to LGFA being able to deliver cheaper debt finance is it holding, and maintaining, a high credit rating (to achieve the credit rating arbitrage referred to in paragraph 7(a)).

15. Consequently, there are a number of features of LGFA that are designed to protect LGFA's creditors, which rating agencies required before agreeing to a high credit rating. These features are described in paragraphs 18 to 35 below.

16. Before bestowing a high credit rating, rating agencies 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 turn 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).

17. LGFA has been assigned a long-term foreign currency credit rating of AA and a long-term local currency credit rating of AA+ by Fitch Ratings.

Features of LGFA designed to reduce short term default risk

18. When a Participating Local Authority or Participating CCO borrows, the risk of short term default, although low, is still significantly higher than its risk of long term default. For instance, in the long term a local authority can assess and collect sufficient rates revenue to cover almost any shortfall, but such revenue cannot be collected quickly.

19. 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 LGFA is local authority and (now) CCO debt, so such temporary liquidity risks are effectively passed on to LGFA. Consequently, the rating agencies look for safeguards to ensure that liquidity problems of a Participating Local Authority or a Participating CCO will not lead to a default by LGFA.

21. There are two principal safeguards to manage short term default (liquidity) risk:

    (a) **Cash**: LGFA holds a certain amount of cash and other liquid investments (investments that can be quickly turned into cash).

    (b) **Liquidity facility**: LGFA has a borrowing facility with central government.

Features of LGFA designed to reduce long term default risk

22. There are also a number of safeguards to manage long term default risk, the most important of which are that LGFA:

    (a) **Rates charge:** requires all Participating Local Authorities to provide a charge over rates and rates revenue (**Rates Charge**) to secure various obligations to LGFA (including borrowings);

    (b) **Equity:** maintains several sources of equity (see paragraph 27 below);

    (c) **Guarantee LGFA:** requires:

(i) all Participating Local Authorities that wish to borrow more than $20 million; and

(ii) all Participating Local Authorities that hold an interest in a Participating CCO (regardless of the amount borrowed by the CCO) or the size of the interest in the CCO,

(together, **Guaranteeing Local Authorities**) to guarantee the obligations of LGFA to its creditors;

(d) **Hedging:** hedges its exposures to interest rate and foreign currency fluctuations to ensure that such fluctuations do not significantly affect its ability to meet its payment obligations;

(e) **Risk management:** has risk management policies in place in relation to its borrowing and lending – for example, LGFA will impose limits on the percentage of lending made to any one entity to ensure that its credit risk is suitably diversified; and

(f) **Operational risk:** ensures its operations are run in a way that minimises operational risk – it has done this by outsourcing its operations to the New Zealand Debt Management Office, which has robust processes in place to manage operational risk.

23. Additional detail in relation to the features referred to in paragraphs 22(a) to 22(c) is set out below.

Rates Charge

24. All Participating Local Authorities borrowing from LGFA are required to secure that borrowing with a Rates Charge. In addition, a Participating Local Authority that provides credit support for a Participating CCO (see further at paragraph 64 below) may be required to secure the credit support with a Rates Charge.

25. This is a powerful form of security for LGFA, because it means that, if the relevant local authority defaults, a receiver can assess and collect sufficient rates to recover the defaulted payments.

26. From a Participating 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.

Sources of equity

27. LGFA has several sources of equity to safeguard its capital adequacy:

(a) **Ordinary equity:** Central government and the Principal Shareholding Local Authorities have contributed initial equity as the issue price of their initial shareholding;

(b) **Uncalled capital:** each Principal Shareholding Local Authority is required to hold uncalled capital equal in amount to its paid up equity contribution (**Uncalled**

Capital), which is able to be called by LGFA if it determines that there is a risk of imminent default;

(c) **RPS:** each Participating Local Authority and Participating CCO must, at the time that it borrows from LGFA, contribute some of that borrowing back in the form of subordinated debt issued by LGFA (**Borrower Notes**), which in certain circumstances may convert to redeemable preference shares in LGFA (however, because a CCO is not permitted to be a shareholder in LGFA, its Borrower Notes are transferred to its parent local authority/ies immediately prior to conversion, such that the redeemable preference shares are issued to the local authority/ies – see paragraph 28 below); and

(d) **Equity commitments:** in addition to the equity contributions made in conjunction with borrowing, all Guaranteeing Local Authorities are required to commit to contributing equity in certain circumstances (calls on any such commitments are limited to situations in which there is a risk of imminent default by LGFA).

28. As noted in paragraph 27(c) above, where a CCO holds Borrower Notes that are to convert to redeemable preference shares in LGFA, the Borrower Notes are transferred to the relevant parent local authority (or local authorities) immediately prior to conversion, such that the redeemable preference shares are issued to the local authority/ies. The Debt Programme documentation provides that the consideration (if any) for that transfer will need to be separately agreed as between the relevant CCO and local authority/ies. The relevant parties will therefore need to consider:

(a) whether any consideration is to be paid by the local authority/ies to the CCO;[1] and

(b) if so, whether that consideration is to be agreed up front at the time of accession (under a side agreement between the CCO and relevant local authority/ies), or addressed only if there is a conversion of Borrower Notes held by the CCO.

Guarantee

29. Under the Guarantee, the Guaranteeing Local Authorities guarantee the payment obligations of LGFA to LGFA's creditors.

30. The purpose of the Guarantee is to provide additional comfort to lenders and other creditors (and therefore credit rating agencies) that there will be no long term default. It may also be used to cover a short term default if there is a default that cannot be covered using the protections described in paragraphs 18 to 21 above, but which will ultimately be fully covered using the rates charge described in paragraphs 24 to 26.

31. The Guarantee would only be called if LGFA itself defaults. It is not a direct guarantee of other local authorities' borrowing. Consequently, a call on the Guarantee would only occur if the numerous safeguards put in place to prevent an LGFA default fail.

32. If any such default did occur, and the Guaranteeing Local Authorities were called on under the Guarantee, they could potentially be called on to cover any payment obligation that

[1] In the event of a conversion, there will be a transfer of property (the Borrower Notes) from the CCO to the local authority/ies, however it is for the parties (CCO and local authority/ies) to decide whether any compensation should be provided to a CCO for that transfer, or if this unlikely event is to be treated as part of the cost of the credit support to be provided by the local authority/ies for CCO borrowings.

LGFA failed to meet. Such payment obligations may (without limitation) include obligations owed to:

(a) LGFA's principal lenders;

(b) central government (in respect of the liquidity facility referred to at paragraph 21(b)); and

(c) hedging counterparties (in respect of the hedging transactions referred to in paragraph 22(d)).

33. While guaranteeing LGFA's payment obligations obviously presents some risks to the Guaranteeing Local Authorities, there are also benefits:

(a) at a global level, the provision of the guarantees has contributed to LGFA's high credit rating, with consequential benefits for borrowers; and

(b) in relation to each Guaranteeing Local Authority, further benefits can accrue:

(i) it will be able to borrow in excess of $20 million from LGFA; and

(ii) such local authorities may also be offered lower funding (interest) costs.

34. While all Guaranteeing Local Authorities are jointly and severally liable for the entire LGFA debt guaranteed, claims against individual local authorities will initially be based on their proportion of the total Annual Rates Income of all Guaranteeing Local Authorities.

35. Guaranteeing Local Authorities are required to provide a Rates Charge to secure their obligations under the Guarantee and their obligations to contribute additional equity.

Characteristics designed to make borrowing from LGFA fair for all Participating Local Authorities

36. The principal risk involved with LGFA is that Participating Local Authorities or Participating CCOs default on payment obligations, which could, in turn, result in LGFA defaulting on its own payment obligations. The greater this risk is, the less attractive participation in LGFA is.

37. However, Participating Local Authorities and Participating CCOs will not create this risk in equal measures. There are some that carry a greater default risk than others, and therefore contribute disproportionately to the overall risk of LGFA. Those local authorities and CCOs are also the local authorities and CCOs that would be likely to pay the highest interest margins if they borrowed outside LGFA, and so have benefitted the most from the establishment of LGFA.

38. To minimise this cross-subsidisation, of the higher risk borrowers by the lower risk borrowers, different interest margins are paid by different local authorities and CCOs when they borrow from LGFA, with those carrying the higher default risk paying higher margins.

Viability of LGFA dependent on participation levels

39. The modelling and other analysis done prior to the establishment of LGFA suggested that LGFA would be viable (in that it will deliver sufficient benefits to justify its establishment and continued existence) if:

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

    (b) sufficient funds were borrowed through it to obtain the economies of scale benefits referred to in paragraph 7(b).

40. Consequently, the participation of sufficient local authorities and (now) CCOs is critical. To this end, Principal Shareholding Local Authorities were required to meet a certain proportion of their individual borrowing needs through LGFA for an initial amount, to ensure the critical amount of utilisation was achieved. LGFA now has over $9 billion of debt on issue, and has been a resounding success.

Part C – Costs and Benefits

41. In this part, we have identified the key costs and benefits to participating in LGFA.

Benefits to borrowing through LGFA

42. LGFA has been able to borrow at low enough rates for LGFA to be attractive because of the three key advantages LGFA has over a local authority borrower described in paragraph 7. That is – exploiting credit rating arbitrage, economies of scale and regulatory arbitrage.

43. In addition, LGFA is providing increased certainty of access to funding and terms and conditions (including the potential access to longer funding terms).

44. The potential savings for a local authority or a CCO in terms of funding costs will depend on the difference between its funding cost when it borrows from LGFA and the funding cost when it borrows from alternative sources. This difference will vary between and among local authorities and CCOs.

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

    (a) the borrowing margin of LGFA;

    (b) the operating costs of LGFA; and

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

        (i) credit quality;

        (ii) the size of the borrowings from LGFA;

        (iii) if a local authority, whether it's a Guaranteeing Local Authority; and

        (iv) if a CCO, the covenants and credit support package available.

Costs to borrowing through LGFA

46. The costs to Participating Local Authorities or CCOs as a result of their borrowing through LGFA take two forms:

    (a) First, risks assumed in order to participate, which create contingent liabilities (ie costs that will only materialise in certain circumstances).

    (b) Secondly, the Borrower Notes.

Risks

47. The features of the LGFA structure described above, which are included to obtain a high credit rating, are essentially steps that 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 and CCOs.

48. These risks are that:

    (a) in the case of Guaranteeing Local Authorities, a call is made under the Guarantee (see discussion in paragraphs 29 to 35 above);

    (b) in the case of Guaranteeing Local Authorities, a call is made for a contribution of additional equity to LGFA (see paragraph 27 above); and

    (c) in the case of all Participating Local Authorities and Participating CCOs, LGFA is not able to redeem their Borrower Notes (see paragraph 27 above).

49. It is anticipated, however, that the prospect of these risks arising is low.

Cost of Borrower Notes

50. As discussed in paragraph 27(c), all Participating Local Authorities and Participating CCOs are required to invest in Borrower Notes when they borrow from LGFA. This carries a cost in addition to the risk referred to in paragraph 48(c), because the investment in Borrower Notes has, in most cases, been funded by borrowing from LGFA, and the cost of this funding will be higher than the return paid on the Borrower Notes.

51. For Participating CCOs this cost is potentially greater (depending on how they agree to share the cost with local authorities – see paragraph 28 above) as, in certain circumstances (ie where there is a risk of LGFA default), the Borrower Notes may be transferred to a parent local authority at the time of the automatic conversion to redeemable preference shares in LGFA.

Part D – Local Authorities as Issuers

52. In this part we have addressed the transactions that local authorities wishing to join the Debt Programme will be required to enter into.

53. The transactions and accession requirements that apply to local authorities are standardised, such that the same requirements will apply to all local authorities. However, the applicable requirements differ depending on whether the local authority is to join as:

(a) a borrower only (referred to as an "**Issuer**" under the Debt Programme);

(b) an Issuer and a Guaranteeing Local Authority; or

(c) an Issuer, a Guaranteeing Local Authority and a Principal Shareholding Local Authority.[2]

Issuer

54. If a local authority joins LGFA as an Issuer only, it will:

(a) be able to borrow from LGFA (up to $20m);

(b) need to subscribe for Borrower Notes (see paragraph 27(c)); and

(c) provide for the Rates Charge to be extended to LGFA (through the issuance of security stock), to secure its borrowing obligations to LGFA (see discussion in paragraphs 24 to 26).

55. The Debt Programme documents that a local authority will need to accede to are:

(a) a multi-issuer deed (under which the local authority can issue debt as an Issuer); and

(b) a notes subscription agreement (under which the local authority will subscribe for Borrower Notes).

56. A local authority will also need to have a debenture trust deed (to provide for the Rates Charge) and an agency agreement.

Issuer and Guarantor

57. If a local authority joins LGFA as an Issuer and a Guaranteeing Local Authority, it will:

(a) undertake the transactions referred to in paragraph 54 above; and

(b) in addition, also need to:

(i) commit to providing additional equity to LGFA under certain circumstances (see paragraph 27(d) above);

(ii) commit to meeting a certain proportion of its borrowing needs from LGFA;

(iii) enter into the Guarantee (see discussion in paragraphs 29 to 35 above); and

(iv) provide for the Rates Charge to be extended to a security trustee on behalf of LGFA's creditors (through the issuance of security stock), to secure its obligations under the Guarantee.

[2] Note that the ability to become a Principal Shareholding Local Authority is limited to particular shareholder openings offered by LGFA from time to time.

58. The Debt Programme documents that a local authority will need to accede to in order to enter into these transactions are:

(a) those listed in paragraph 55 above;

(b) an equity commitment deed (under which the local authority will be required to provide additional equity to LGFA under certain circumstances); and

(c) a guarantee and indemnity (to provide for the Guarantee).

Issuer, Guarantor and Principal Shareholding Local Authority

59. If a local authority is to join LGFA as a Principal Shareholding Local Authority, it would, in addition to the transactions and documents required as an Issuer and Guaranteeing Local Authority, also need to subscribe for paid-up shares in LGFA to provide it with capital (see paragraphs 12 and 27(a)) and subscribe for Uncalled Capital in LGFA (see paragraph 27(b) above). There would be additional documentation to accede to as well, including a shareholders' agreement.

Part E – CCOs as Issuers

60. In this part, we have:

(a) set out the key requirements for CCOs joining the Debt Programme;

(b) identified what security is likely to be required by LGFA in relation to any particular Participating CCO; and

(c) identified aspects of the Debt Programme (as it relates to CCOs) that are likely to be subject to negotiation.

Key requirements

61. LGFA has recently amended the Debt Programme in order to allow CCOs to accede as Issuers and therefore borrow directly by issuing securities to LGFA.

62. A Participating CCO may not (and is not required to), however, join as Guaranteeing Local Authority or a Principal Shareholding Local Authority.

63. The amendments made to the Debt Programme to facilitate the accession of CCOs as an Issuer enable flexibility in the range of covenant and credit support options that may be required from particular Participating CCOs. This means that the accession process for a CCO will usually be more complex and involve more commercial negotiation (and therefore potentially greater initial costs) than an equivalent process for a local authority.

64. LGFA may, in its discretion, allow a CCO to accede as an Issuer provided that (among other things):

(a) the CCO is a company (and 100% of its shares are held by one or more local authorities and/or the Crown);

(b) it has acceded to:

(i) the multi-issuer deed (which now includes a separate standard package of representations, warranties, undertakings, covenants and defaults that will apply specifically to CCOs, that each Participating CCO would be subject to (except where any exceptions, for any individual Participating CCO, are negotiated at the time of accession – see paragraph 73 below)); and

(ii) the notes subscription agreement;

(c) an agreed package of "CCO Credit Support" is provided, which may include:

(i) security over the CCO's assets;

(ii) a negative pledge and covenant deed (which could provide for a limit on borrowings relative to the amount of uncalled and unpaid equity capital in the CCO at any time, and an arrangement for LGFA to be able to require a call on that capital);

(iii) a guarantee (see paragraph 66 below); and/or

(iv) any other security arrangements required by LGFA;

(d) each shareholder that is a local authority has itself acceded to the multi-issuer deed, notes subscription agreement, guarantee and indemnity and the equity commitment deed (whether or not otherwise required to accede to those documents – ie even if it has not itself borrowed in excess of $20m); and

(e) any further eligibility criteria required from time to time in accordance with LGFA's policies have been satisfied, and any further conditions that may be specified by LGFA in the accession documents have been satisfied.

Security requirements

65. As noted at paragraph 64(c), LGFA has considerable flexibility and discretion as to what "CCO Credit Support" is required in the case of any Participating CCO. At a minimum, it is intended that:

(a) any Participating CCO that is not a council controlled trading organisation[3] (**CCTO**) will be required to obtain a guarantee[4] from its parent local authority/ies in respect of the Participating CCO's obligations to LGFA (and the local authority/ies will need to extend the benefit of the Rates Charge to LGFA to cover the guarantee obligations); and

(b) any Participating CCO that is a CCTO will instead[5] be required to provide LGFA with security over an amount of uncalled and unpaid equity capital subscribed for by its parent local authority/ies.

66. An uncalled capital credit support structure (as referred to in paragraph 65(b) above) is intended to, to some extent, replicate the commercial effect of a guarantee (without being a guarantee). In general terms, it involves:

[3] As defined in section 6 of the Local Government Act 2002.
[4] Note that this is a guarantee of the Participating CCO's obligations to LGFA, and is therefore different to the Guarantee referred to at paragraphs 29 to 34 above (which is a guarantee of the obligations of LGFA to its creditors).
[5] On the basis that section 62 of the Local Government Act 2002 prohibits local authorities from guaranteeing the obligations of CCTOs.

(a) the parent local authority/ies subscribing for an amount of uncalled and unpaid equity capital in the Participating CCO (of an amount at least equal to the Participating CCO's obligations to LGFA);

(b) a requirement for that capital to be called, and paid for, following a default by the Participating CCO; and

(c) the Participating CCO providing LGFA with security (or other rights) over the ability to call for that capital, and the proceeds of the call.

67. As noted above, LGFA can also require further security in respect of any particular Participating CCO, including security over the other assets of the CCO.

68. In addition, the Debt Programme recognises that the range of security that may be provided by a CCO may necessitate intercreditor arrangements to be put in place. For instance, if a CCO has already provided security over its assets, or over an uncalled capital credit support structure, to existing creditors, LGFA may need to share in that security (or take security over the same collateral).

69. The Debt Programme therefore contemplates that intercreditor arrangements (providing for the basis upon which the different creditors will share, or benefit from, the security or collateral), which are acceptable to LGFA, may be required.

70. This will be particularly relevant where a Participating CCO's existing financing arrangements are to be refinanced by LGFA over a period of time (eg as bonds mature), with the creditors relying on the same security in the transitional period.

Ability to negotiate

71. As noted at paragraph 64(b)(i) above, a separate standard package of representations, warranties, undertakings, covenants and defaults that will apply specifically to CCOs has been introduced into the Debt Programme.

72. However, LGFA has also recognised that the business, assets, revenue sources, ownership, credit-strength and financing requirements of CCOs can vary significantly from CCO to CCO, and has therefore provided for a significant amount of flexibility and discretion to negotiate particular terms in the Debt Programme.

73. In this regard, there is scope for the following matters (among others) to be negotiated on a case-by-case basis:

(a) the financial covenants (that will apply at the Participating CCO level, as opposed to the parent local authority or consolidated group);

(b) the representations and undertakings to be given by the Participating CCO (including the scope of agreed "permitted" exceptions in relation to certain undertakings, such as restrictions on CCO's granting security, disposing of assets, making distributions and acquiring assets); and

(c) change of control redemption events.

74. Therefore, whereas when a Participating Local Authority joins the Debt Programme it can simply join up to set pre-existing borrowing terms, a Participating CCO will need to carefully review the borrowing terms that will apply to it and consider whether any changes may be necessary or desirable.

DOCUMENTS TO BE SIGNED BY DCC		
Document	**PARTIES**	**COMMENT**
Debenture Trust Deed (**DTD**)	DCC and Trustees Executors Limited (**TEL**)	Under the DTD, DCC grants a security interest over its rates and rates revenue in favour of TEL. The DTD provides for the Council to issue security stock to entities (such as LGFA), with the holders of security stock receiving the benefit of the security under the DTD (as TEL holds the security interest over the Council's rates and rates revenue for the benefit of holders of stock issued under the DTD).
Registrar and Paying Agent Services Agreement (**PAA**)	DCC and Computershare Investor Services Limited (**Computershare**)	Under the PAA, DCC appoints Computershare as DCC's registrar and paying agent. Computershare's role as registrar and paying agent is to maintain DCC's stock register and, if required by DCC, act as paying agent for DCC for payments that need to be made by DCC to holders of stock issued by DCC.
Accession Deed to Multi-issuer Deed - DCC's Accession	DCC and LGFA	This accession deed provides for DCC to become a party to the LGFA Multi-issuer Deed. Under the LGFA Multi-issuer Deed, local authorities and CCOs can issue debt securities to LGFA so that those local authorities and CCOs can borrow funds from LGFA.
Accession Deed to Multi-issuer Deed – DCTL's Accession	DCTL and LGFA (acknowledged by DCHL and DCC)	This accession deed provides for DCTL to become a party to the LGFA Multi-issuer Deed.
Accession Deed to Notes Subscription Agreement – DCC's Accession	DCC and LGFA	This accession deed provides for DCC to become a party to the LGFA Notes Subscription Agreement. Under the Notes Subscription Agreement, each local authority and CCO that borrows from LGFA subscribes for "Borrower Notes" (subordinated debt issued to LGFA).
Accession Deed to Notes Subscription Agreement – DCTL's Accession	DCTL and LGFA (acknowledged by DCC)	This accession deed provides for DCTL to become a party to the LGFA Notes Subscription Agreement.

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DOCUMENTS TO BE SIGNED BY DCC		
Accession Deed to Guarantee and Indemnity	DCC and TEL Security Trustee (LGFA) Limited	This accession deed provides for DCC to become a party to the LGFA Guarantee and Indemnity. Under the LGFA Guarantee and Indemnity all guaranteeing local authorities provide a guarantee of LGFA's debt obligations to LGFA's creditors.
Accession Deed to Equity Commitment Deed	DCC and LGFA	This accession deed provides for DCC to become a party to the LGFA Equity Commitment Deed. Under the LGFA Equity Commitment Deed local authorities agree to contribute additional capital by subscribing for shares in LGFA (in circumstances in which LGFA is financially distressed).
Borrower Notes Consideration Deed	DCC and DCTL	This is an agreement between DCC and DCTL recording that, if "Borrower Notes" are to be converted to redeemable preference shares in LGFA, a fair market value for the transfer of the "Borrower Notes" from DCTL to DCC will be agreed by DCC and DCTL at the time immediately prior to the conversion.

CERTIFICATES

CERTIFICATES TO BE SIGNED BY CHIEF EXECUTIVE OF DCC	
CERTIFICATE	**COMMENT**
Chief Executive (**CE**) Certificate relating to the DTD and PAA	A standard form section 118 certificate that will be signed by the CE in relation to DCC's entry into the DTD and PAA.
CE Certificate relating to: - four accession deeds for DCC's accession, - three security stock certificates and stock issuance certificate	A standard form section 118 certificate that will be signed by the CE in relation to DCC's entry into the four accession deeds, three security stock certificates and stock issuance certificate involved in DCC's accession to LGFA (please see the below for comments on the security stock documents).
CE Certificate relating to DCTL's accession to LGFA	A standard form section 118 certificate that will be signed by the CE acknowledging DCTL's entry into Accession Deed to Multi-issuer Deed and Accession Deed to Notes Subscription Agreement

CERTIFICATES TO BE SIGNED BY CHIEF EXECUTIVE OF DCC	
Security Stock Certificate – Multi-issuer Deed	A security stock certificate signed by the CE that evidences security stock issued by DCC to LGFA to secure DCC's obligations to LGFA under the Multi-issuer Deed (and related accession deed).
Security Stock Certificate – Equity Commitment Deed	A security stock certificate signed by the CE that evidences security stock issued by DCC to LGFA to secure DCC's obligations to LGFA under the Equity Commitment Deed (and related accession deed).
Security Stock Certificate – Guarantee and Indemnity	A security stock certificate signed by the CE that evidences security stock issued by DCC to TEL Security Trustee (LGFA) Limited to secure DCC's obligations to TEL Security Trustee (LGFA) Limited under the Guarantee and Indemnity (and related accession deed).
Stock Issuance Certificate	A certificate signed by the CE relating to the issue of security stock evidenced by the above three security stock certificates. The certificate must be provided as a part of the stock issuance process outlined in DCC's new DTD.

OTHER DOCUMENTS

OTHER DOCUMENTS TO BE SIGNED BY DCC	
DOCUMENT	**COMMENT**
Shareholder's Resolution and Entitled Person's Agreement	This is a shareholder's resolution and entitled person's agreement that relates to DCTL's accession to LGFA.