REPORTS OF THE

GOVERNMENT SUPERANNUATION FUND AUTHORITY

FOR THE YEAR ENDED
30 JUNE 2005

Presented to the House of Representatives
pursuant to Section 44A of the Public Finance Act 1989

GOVERNMENT SUPERANNUATION FUND
Te Pūtea Penihana Kāwanatanga

FOR THE YEAR ENDED
30 JUNE 2005

Presented to the House of Representatives
pursuant to Section 93B of the Government Superannuation Fund Act 1956

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GOVERNMENT SUPERANNUATION FUND AUTHORITY

CHAIRMAN'S REPORT

On behalf of the Government Superannuation Fund Authority Board ("the Board"), I am pleased to present the annual report of the Government Superannuation Fund Authority ("the Authority") for the year ended 30 June 2005.

A separate annual report has been prepared by the Authority for the Government Superannuation Fund ("GSF" or the "Fund"), commencing on page 31.

The Authority was established as a Crown entity by section 15A of the Government Superannuation Fund Act 1956 ("the Act") and became an autonomous Crown entity under the Crown Entities Act 2004.

The Authority's mission is to use best practice to manage the Fund and administer the GSF Schemes, in accordance with the Act, with the prime objectives of enabling:

- returns to be maximised without undue risk
- the cost of the Crown's contribution to GSF to be minimised, and
- the needs and reasonable expectations of stakeholders to be met.

The Authority is also responsible for interpreting the provisions of the Act relating to the GSF Schemes and exercising discretionary provisions. Management carries out these functions under delegation from the Board.

Highlights of the 2005 Year

- Successful transition of administration for the GSF Schemes from AXA New Zealand to Datacom Employer Services Limited
- Implementation of changes with respect to -
    - Reinstatement of the $500 cost of living allowance
    - Reduction in contribution rate from 7% to 6.5% for some contributors
    - Introduction of a transfer option for Police Sub-Scheme members
- Pre-tax investment return of 11.83% and after-tax return of 7.38% following good results from New Zealand equities and international fixed interest
- Net assets increasing from $3.37 billion to $3.52 billion
- Appointment of three investment managers for property
- Redevelopment of the Authority's website

GSF Schemes

In last year's report, I commented on the tender carried out for the role of the administrator of the GSF Schemes when the agreement with AXA New Zealand ("AXA") expired on 30 April 2005. During the tender, AXA decided to withdraw, advising that its strategic focus was on continuing to grow its own superannuation and fund management schemes. Following a detailed and comprehensive process, the Authority appointed Datacom Employer Services Limited ("Datacom"), a subsidiary of Datacom Group, as the new administrator.

The Authority, Datacom and AXA sought to achieve a seamless transition of GSF Schemes' administration with the objective of ensuring contributors, annuitants and employers would notice no change in service. The process was assisted by Datacom taking over management of the computer hardware and operating systems owned by the Authority and employing all of the GSF Schemes' administration staff previously with AXA.

I am pleased to advise the objective of seamless transition was achieved when Datacom took over the administration after ANZAC weekend. The Authority expresses its appreciation to Datacom, AXA and the Authority's Management team for the highly professional manner in which the transition was managed.

During the year under review, the Authority successfully implemented changes made by the Government to the GSF Schemes -

- enhancing the entitlements for some annuitants by reinstating the $500 cost of living allowance revoked in 1991
- reducing the contribution rate for contributors to the Old Scheme from 7% to 6.5% and
- introducing a new transfer option for members of the Police Sub-Scheme, effective 1 August 2005.

Each of the changes required significant modifications to systems and administrative procedures.

Investment strategy

The Authority is required to invest the Fund on a prudent, commercial basis. In doing so, it must manage and administer the Fund in a manner consistent with best practice portfolio management, maximising returns without undue risk to the Fund as a whole.

The Authority has implemented an investment strategy and asset allocation which reflects the requirements of the Act. Further details of the strategic asset allocation and investment results for the year are included in the Investment Commentary of the Fund's annual report on page 35.

The investment objective adopted by the Board for the Fund remains unchanged as:

"The risk and return for the overall Fund is balanced with a strategic portfolio that meets the Authority Board's investment objective for the Fund of:

- *achieving an average rate of return of 2.5% per annum over the returns on a portfolio of New Zealand Government Stock (after tax) measured over rolling ten year periods. This is expected to generate improved investment performance (*from October 2001*) over the remaining life of the Fund of a net present value of approximately $1.2 billion, relative to a portfolio invested entirely in New Zealand Government Stock.*
- *having no more than a 1 in 10 chance in any one year of a loss in the total Fund being greater than $100 million (after tax)."*

Investment returns

The Fund's pre tax investment return for the year was 11.83%.

New Zealand equities again produced an excellent result returning 21.34% (2004: 21.13%) while international fixed interest returned 12.64%. The return from international equities was lower than in 2004, but greater than the return from New Zealand fixed interest. Both New Zealand and international fixed interest produced better returns than 2004.

The Fund's surplus after tax, represents a return on average assets of 7.38%. This compares with the median superannuation scheme after-tax return in the Watson Wyatt Investment Performance Survey (covering 78 superannuation schemes), for the year ended 30 June 2005, of 7.92 %. The average after-tax return for the Fund over the last three years was 6.11%. This compares with the median average after-tax return in the Watson Wyatt survey, over the same period, of 5.96%.

It is important to take a long-term view of investment returns as the Fund is expected to exist for at least 60 years. As a result, performance in any particular year is not indicative of the long-term performance of the Fund.

The Board is confident that, over the medium to long term, the returns from investing in a wide diversity of asset classes will out-perform the returns available from investing solely in New Zealand Government Stock.

Details of the investment returns and the benchmark indices used by the Authority are set out in the annual report for the Fund (see Investment Commentary, page 35).

Asset allocation

There was no change to the Fund's strategic asset allocation during the year. With the exception of property, and cash which is being held pending the further funding of property investment managers, all asset classes were within their rebalancing tolerances at 30 June 2005 and were maintained within the rebalancing tolerances during the year.

The Authority has appointed three investment managers to manage property investments for the Fund. Funding of property is expected to be completed by the last quarter of 2005.

Further detail is set out in the Investment Commentary on page 35.

Website

In April 2005, the Board relaunched the Authority's website – www.gsfa.govt.nz - and updated its corporate identity. This was timed to coincide with the transition of the GSF Schemes administration from AXA to Datacom.

The website is easy to navigate around and contains comprehensive information on both the Authority and the Fund. The content explains how the Authority operates and its governance, and profiles the Board and Management. Under the section on the Fund are a number of reports and policies, information on the GSF Schemes' administrator and the latest available data on investment returns. We update the investment returns every quarter on the website and provide comparisons with benchmarks.

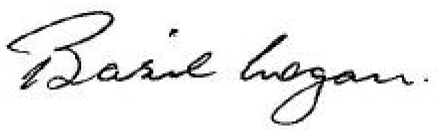
I am sure the website will prove itself a most useful tool, especially as technology develops and becomes more affordable, and as increasing numbers of our members show a preference for accessing information in this way. The website will give all members and other interested people immediate access to our latest results, as well as any changes the Board makes to its policies, investment strategies and personnel.

The website, like all other aspects of our operations, will be kept under continuous review and improvement.

Conclusion

The Authority thanks Ministers of the Crown and members of Parliament, Government officials and advisers, for working constructively with us during the year.

In conclusion I am indebted to my fellow Board members for their excellent advice and support and to the Management team and staff for their expertise and hard work throughout the year.



Basil Logan
Chairman
Government Superannuation Authority Board

STATEMENT OF GOVERNANCE AND ACCOUNTABILITY

The Government Superannuation Fund Authority ("the Authority") was established as a Crown Entity by section 15A of the Government Superannuation Fund Act 1956 ("the Act") and became an autonomous Crown entity under the Crown Entities Act 2004. The business of the Authority is to manage the assets, and administer the Schemes of the Government Superannuation Fund ("the Fund") in accordance with the Act.

Section 15G of the Act specifies that the Government Superannuation Fund Authority Board ("the Board") is responsible for the business of the Authority.

Government Superannuation Fund Authority Board

The Minister of Finance appointed the following seven members to the Board:

Basil Logan, Chairman, (appointed 2001, reappointed 2003) is also the Chairman of Opus International Consultants Limited.

David May, Deputy Chairman, (appointed 2001, reappointed 2004) was formerly Chief Executive of Jacques Martin NZ Ltd and Managing Director of Colonial Life NZ Ltd. He is Chairman of the Guardians of New Zealand Superannuation, and a director of Southern Cross Healthcare.

Colin Blair OBE, (appointed 2001, reappointed 2003) was formerly a Partner of the accounting firm Deloitte, and was the Retirement Commissioner until February 2003.

Helen Bowie (appointed 2001, reappointed 2003) is a partner of Chapman Tripp Sheffield Young.

Tim McGuinness (appointed 2001, reappointed 2004) is a Board member of the Earthquake Commission, a trustee of the Global Retirement Trust and a trustee of the Globus NZ Pension Plan. He previously held senior investment management positions at Royal & Sun Alliance and Norwich Union Investment Management.

Ralph Stockdill (appointed 2002) held senior management positions at the Department of Labour in the employment relations area before his retirement. Immediately before his appointment to the Board, Mr Stockdill was a member of the Executive of the Government Superannuitants' Association.

During the year the Minister re-appointed Mr Stockdill as a Board member for a further term of three years from 1 April 2005.

Susie Weaver (appointed 2001, reappointed 2002) is a principal of Weaver Consulting Ltd and former General Manager of Investments at Armstrong Jones (now ING (NZ)).

Remuneration of the Board members

Remuneration of the Board members is in accordance with the rates set by the Minister of Finance.

Responsibilities and operations of the Board

The Board is responsible for all decisions relating to the business of the Authority.

The Board has established four committees with specific responsibilities for Audit & Risk Review, Investments, Schemes and Responsible Investing. The Chairman is an ex-officio member of all committees.

As required by the Act, the Board does not delegate the following powers:

- the power of delegation;
- the power to grant power of attorney; and
- the power to appoint schemes' administration managers, investment managers, other service providers, and custodians.

The Board held 11 regular meetings during the year, one special meeting to review strategic issues, and an investment workshop.

Indemnity

During the financial year, the Authority entered into a Deed of Indemnity with each Board member whereby it agreed to indemnify the Board member (subject to certain exceptions) for certain costs and liabilities in respect of excluded acts and omissions (being acts and omissions in good faith and in performance or intended performance of the Authority's functions) to the maximum extent permitted by the Crown Entities Act 2004.

The indemnity provided by the Authority does not protect the Board member against any liability, claim, or proceeding of any kind, for any dishonesty or fraud, or anything else that either:

(a) as a matter of public policy cannot be indemnified at law; or

(b) is criminal liability that the Authority has determined, in its absolute discretion, should be excluded from the indemnity.

The Authority has determined that all criminal liability, other than strict liability offences, should be excluded from the scope of the indemnity. Broadly speaking, strict liability offences are those for which no intent needs to be established.

Auditor

The Auditor-General is the auditor of the Authority. The Auditor-General has appointed Michael Wilkes of Deloitte to act on his behalf.

Management team

The Authority and the Board of Trustees of the National Provident Fund ("NPF") have formed a joint venture company, Annuitas Management Limited ("Annuitas"). Each organisation has entered into a management services agreement ("MSA") with Annuitas.

The main function of Annuitas is to provide staff ("Management") who act in managerial and secretarial roles on behalf of the Authority and NPF. The MSA between Annuitas and the Authority contains delegations of authority to enable Management to carry out the day-to-day management of the Authority's investment, custody and schemes' management arrangements. In the case of schemes' management, the delegation includes interpretation of the provisions of the GSF Schemes and exercise of discretionary powers in accordance with the Statement of Provisions, Policies and Procedures, subject to appropriate consultation with the Board.

The Management team is:

Alan Langford	Chief Executive
Euan Wright	Chief Financial Officer
Philippa Drury	General Manager, Schemes
Denise Healey	General Manager, Investments (to 17 June 2005)
Paul Bevin	General Manager, Investments (from 19 July 2005)
Nicky Rumsey	Manager, Investments

STATEMENT OF RESPONSIBILITY

The financial statements of the Government Superannuation Fund Authority ("the Authority") for the year ended 30 June 2005 have been prepared in accordance with section 41 of the Public Finance Act 1989.

The Government Superannuation Fund Authority Board ("the Board") is responsible for the preparation of the financial statements, and the judgments made in the process of producing those statements.

The Board confirms that internal control systems have been established and maintained during the period to assure reasonable reliability and integrity of financial and non-financial reporting.

In our opinion, the attached financial statements and reports for the Authority fairly reflect the financial position, as at 30 June 2005, and the financial performance and the cash flows of the Authority for the year ended 30 June 2005.

Basil Logan

Basil Logan
Chairman
Government Superannuation Fund Authority Board

Alan Langford
Chief Executive

7 September 2005

STATEMENT OF SERVICE PERFORMANCE

Output Class O1 – Management of the Government Superannuation Fund

This output class provides investment and schemes' management for the Government Superannuation Fund ("GSF or the Fund").

Outputs in this class are:

- management of the GSF assets;
- interpretation of the provisions of the Government Superannuation Fund Act 1956 ("the Act"), and exercising the statutory powers under the Act;
- management of the GSF Schemes, including the Agreement between the Authority and the Administrator of the GSF Schemes; and
- overall financial management of the Fund, including reporting on its liabilities and the Crown's financial obligations to the Fund.

The performance targets are set out in the Government Superannuation Fund Authority's Statement of Intent 2004/2005.

Investment management

PERFORMANCE TARGET	PERFORMANCE ACHIEVED
Finalise policies, standards and procedures for investing in property.	Achieved. The policies, standards and procedures for property have been incorporated into the Authority's Statement of Investment Policies Standards and Procedures (see page 61) and in the investment mandates with the three managers of property portfolios.
Engage and manage investment managers to give effect to its property investment strategy.	Achieved. The Authority has appointed two managers to manage international portfolios of listed property securities and one manager to manage an international portfolio of unlisted property securities. The three property managers were partly funded during the year.
Rebalance assets between asset classes as required to maintain the strategic asset allocation within agreed ranges.	Achieved. A monthly re-balancing procedure has been in effect since November 2003. The monthly rebalancing maintained the asset classes within their rebalancing tolerances during the year.
Monitor and review the performance of the appointed investment managers.	Achieved. Monthly reports were received from each of the investment managers, which provided details of their performance, positions and strategies.

	The performance returns were independently checked by the Custodian and any discrepancies investigated. The investment managers also provided monthly certificates confirming they had complied with the terms of their mandates. The major highlights of performance and any exceptional issues or breaches were reported to the Board. Each of the managers of active portfolios presented to the Board during the year and, at that time, a report on their longer term performance was provided to the Board. The investment adviser, Russell Investment Group Limited, has also held regular meetings with each investment manager and provided information to the Board and Management on those meetings, together with any changes in rankings. This is ongoing work.
Implement its policies with respect to investing to avoid prejudice to New Zealand's international reputation as a responsible member of the world community.	Achieved. The Authority appointed two specialist investment-screening organisations to advise on whether the Fund's investments, in portfolios managed on an active basis, could prejudice New Zealand's international reputation as a responsible member of the world community. In addition two people, with extensive international experience, were appointed to advise the Authority whether countries, which have issued securities held in the international fixed interest portfolios, could prejudice New Zealand's international reputation. The actively managed portfolios and the countries were reviewed every six months and reports provided to the Authority. The final decision as to whether an individual investment could prejudice New Zealand's international reputation, and should be sold, is made by the Board. During the year no investments were accepted by the Authority as prejudicing New Zealand's international reputation.

Continue to develop then implement policies with respect to ethical investment.	Partially achieved. The Authority determined that its policies, to avoid prejudice to New Zealand's international reputation as a responsible member of the world community, largely covered its responsibilities with respect to ethical investment. Further work is to be undertaken in the next financial year by the Board and Management to determine whether any additional policies need to be developed.
Carry out the annual review of the Statement of Investment Policies, Standards and Procedures.	Achieved. The annual review of the Statement of Investment Policies, Standards and Procedures ("SIPSP") was completed in May 2005. The SIPSP is an operational document which is subject to amendment as circumstances change, for example a new asset class is added to the strategic asset allocation for the Fund. The annual review is intended to examine the SIPSP in total to determine whether it remains an appropriate and relevant framework for the Authority's investment strategy. No significant changes were made to the SIPSP as a result of the annual review. The SIPSP was updated on 6 August 2005.
Document the governance and management procedures relating to the investment process.	Achieved. Management maintained and continuously updated an Investment Operations Manual that covers the governance and management procedures relating to the investment process. This is ongoing work.

Over the year implementation of the Fund's strategic asset allocation has developed as set out below:

Asset Class	**Strategic Asset Allocation Target %**	**Actual Asset Allocation at 30 June 2004 %**	**Actual Asset Allocation at 30 June 2005 %**
NZ Fixed Interest	14.0	14.1	14.5
International Fixed Interest	21.0	22.5	20.8
NZ Equities	15.0	16.4	16.2
International Equities	42.5	39.8	41.3
Property	7.5	-	4.9
Cash and short-term investments	-	7.2	2.3
TOTAL	**100.0**	**100.0**	**100.0**

With the exception of cash, which is being held pending the further funding of property investment managers, and property, all asset classes were within their rebalancing tolerances at 30 June 2005 and were maintained within the rebalancing tolerances during the year. The Authority expects to complete its allocation to property by the last quarter of 2005.

Schemes' administration

PERFORMANCE TARGET	**PERFORMANCE ACHIEVED**
The GSF Schemes' Administration Manager's performance will be monitored and maintained in accordance with the requirements of the Schemes' Administration Management Agreement between the Authority and AXA New Zealand, including service levels to contributors, annuitants and employers.	Achieved. AXA, the GSF Schemes' Administration Manager up to the termination date of the Management Agreement between the Authority and AXA in April 2005, delivered the services required by the Agreement. Service delivery was certified quarterly by AXA, as required by the Agreement. Datacom Employer Services Limited was appointed as GSF Schemes' Administration Manager from 26 April 2005. Datacom also delivered the services required by the Agreement between the Authority and Datacom in the period to 30 June 2005. The Agreement with Datacom sets out higher standards for the delivery of services than those that applied to AXA. Datacom largely met the standards for the two months it administered the GSF Schemes. This was accepted by the Authority as two months is too short to reasonably assess performance.
The Statement of Provisions, Policies and Procedures will be maintained and, subject to consultation with interested parties, amended to record policy changes made by the Authority.	No changes were required or made to the Statement of Provisions, Policies and Procedures, which was published by the then Superintendent of the Fund on 28 September 2001.
Submissions from the GSF Schemes' Administration Manager will be dealt with in accordance with the Act and the published policies. All submissions to be responded to within five working days.	Achieved. All schemes decisions were made in accordance with the Act and the published policies. The 199 submissions from the GSF Schemes' Administration Manager were responded to within five working days.
Appeals against decisions made by, or on behalf of the Authority, will be responded to in accordance with the Act. The Authority's report to the Appeals Board to be provided at least 14 days before each scheduled hearing date.	Achieved. The three appeals made during the period were reported to the Appeals Board at least 14 days before the scheduled hearing. Two appeals, against decisions made by the Authority, were declined by the Appeals Board and one was allowed.

Sufficient funding will be provided to the GSF Schemes' Administration Manager to ensure all benefit payments are able to be made as they become due.	Achieved. Sufficient funding to meet benefit payments was provided to the GSF Schemes' Administration Manager by the due dates.
Actuarial data on the Fund, required for the Crown accounts, will be provided in accordance with the timetable agreed with Treasury.	Achieved. Actuarial data required for the Crown accounts was provided to Treasury by the agreed dates.
The tender for the role of Schemes' Administration Manager beyond 30 April 2005 (when the present contract with AXA New Zealand expires) will be completed and transition of the administration function to the new manager effected.	Achieved. A tender was held for the role of Schemes' Administration Manager. During the tender, the incumbent, AXA New Zealand, withdrew, advising that its strategic focus was on continuing to grow its own superannuation and funds management schemes. Datacom Employer Services Limited was appointed as the new Administration Manager of the GSF Schemes. The Authority, AXA and Datacom all worked towards achieving a seamless transition with contributors, annuitants and employers noticing no change in the level and quality of services, with entitlements continuing to be calculated accurately and paid on time. The objective was achieved with the transition being effected over ANZAC weekend 2005.
Communications will be sent to contributors, annuitants and employers regarding the activities of the Authority, the performance of the Fund and the transition to the new Schemes Administration Management Agreement.	Achieved. Communications were sent to all contributors, annuitants and employers covering these topics and other matters.

Other

A review will be undertaken of the performance of Annuitas personnel under the Management Services Agreement ("MSA") between the Authority and Annuitas.	Achieved. A review was undertaken of the performance of Annuitas personnel (who act in managerial and secretarial roles on behalf of the Authority) under the MSA between the Authority and Annuitas. The Board was very satisfied with the performance of Annuitas personnel in their managerial and secretarial roles on behalf of the Authority.

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF FINANCIAL PERFORMANCE
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000 Actual		Notes	**2005 $000 Actual**	2005 $000 Forecast
	Revenue			
13	Interest received		**11**	11
526	Other revenue, including Bowen space rental		**605**	521
11,480	Transfer from the Government Superannuation Fund	1	**12,758**	12,523
12,019	**Total revenue**		**13,374**	13,055
	Expenses			
3,050	Schemes administration		**3,073**	3,038
6,108	Investment management and custody	2	**6,932**	6,876
2,861	Operating	3	**3,369**	3,141
12,019	**Total expenses**		**13,374**	13,055
-	**Net operating result**		-	-

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF FINANCIAL POSITION
AS AT 30 JUNE 2005

2004 $000 Actual		Notes	**2005 $000 Actual**	2005 $000 Forecast
	Public equity			
-	General fund		-	-
-	**Total public equity**		-	-
	Represented by:			
	Current assets			
206	Cash at bank		**364**	130
1,981	Receivables and prepayments	4	**2,658**	1,496
2,187	**Total current assets**		**3,022**	1,626
	Current liabilities			
2,187	Payables	5	**3,022**	1,626
2,187	**Total current liabilities**		**3,022**	1,626
-	**Net assets**		-	-

The Financial Statements were approved by the Government Superannuation Fund Authority Board on 7 September 2005.

Basil Logan
Chairman
Government Superannuation Fund Authority Board

Colin Blair
Chairman
Audit and Risk Review Committee
Government Superannuation Fund Authority Board

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000 Actual		Note	**2005 $000 Actual**	2005 $000 Forecast
	Cash flows from operating activities			
	Cash was provided from:			
10,973	Government Superannuation Fund	1	**11,869**	12,517
13	Interest		**11**	11
532	Other		**789**	521
11,518			**12,669**	13,049
	Cash was disbursed to:			
(11,666)	Operating expenses		**(12,511)**	(13,039)
(11,666)			**(12,511)**	(13,039)
(148)	**Net cash flows from operating activities**		**158**	10
(148)	Net (decrease) increase in cash held		**158**	10
354	Opening cash brought forward		**206**	120
206	**Closing cash balance**		**364**	130

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 30 JUNE 2005 - Continued

Reconciliation of Net Operating Result to Net Operating Cash Flows

2004 $000 Actual		**2005 $000 Actual**	2005 $000 Forecast
-	Net operating result	-	-
	Movements in working capital items:		
(603)	Receivables and prepayments	**(677)**	(6)
455	Payables	**835**	16
(148)	**Net cash flows from operating activities**	**158**	10

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF MOVEMENT IN PUBLIC EQUITY
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000 Actual		**2005 $000 Actual**	2005 $000 Forecast
-	**Public equity at beginning of the period**	-	-
-	Net operating result	-	-
-	**Total recognised revenues and expenses for the period**	-	-
-	**Public equity at end of the period**	-	-

These statements are to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF COMMITMENTS
AS AT 30 JUNE 2005

Section 22 of the Government Superannuation Fund Amendment Act 2001 ("the Amendment Act") vested in the Authority the whole of the leasehold interest in floors 3 and 4 at 33 Bowen Street, Wellington ("the Bowen space"). The Bowen space lease terminates in February 2009. The annual lease payment is subject to three yearly reviews.

The Authority has entered into subleases with the Ministry of Economic Development ("MED") and Accident Compensation Corporation ("ACC") for the Bowen space. The MED and ACC subleases are to 31 January 2009 . The future commitments stated below are gross commitments at current rental rates, before netting off rental income from subleases.

In terms of section 15E (1) of the Government Superannuation Fund Act 1956 (the Act), the Authority's expenses are reimbursed by the Government Superannuation Fund, which recovers them from the Crown, as provided for in section 95 of the Act, and from other employers. Accordingly, any shortfall between the lease commitments and the sub-lease rental income is not onerous to the Authority.

Other operating commitments include non-cancellable contracts for building services.

2004 $000 Actual		**2005 $000 Actual**
-	**Capital commitments approved and contracted**	-
	Non-cancellable operating commitments	
2,419	Accommodation lease	1,885
816	Other operating commitments	640
3,235	**Total operating commitments payable (as detailed below)**	2,525
	Term classification for accommodation lease commitments	
523	Not later than one year	520
520	Later than one year and not later than two years	520
1,376	Later than two years and not later than five years	845
-	Later than five years	-
2,419	**Total lease commitments**	1,885
	Term classification for other operating commitments	
176	Not later than one year	177
176	Later than one year and not later than two years	177
464	Later than two years and not later than five years	286
-	Later than five years	-
816	**Total other operating commitments**	640

These statements are to be read in conjunction with the Statement of Accounting Policies and Notes to the Financial Statements.

STATEMENT OF COMMITMENTS
AS AT 30 JUNE 2005 – Continued

The contract with AXA New Zealand to administer the Government Superannuation Fund Schemes ('the Schemes') expired on 30 April 2005. In terms of section 19(1) of the Act the Authority has appointed Datacom Employer Services Limited to administer the Schemes for a term of six years from 1 May 2005. In terms of a separate agreement between AXA, the Authority and Datacom, to facilitate the transition Datacom tookover the administration of the GSF Schemes on 26 April 2005.

2004 $000 Actual		**2005** **$000** **Actual**
	Non-cancellable contractual commitments	
2,542	Schemes administration not later than one year	2,263
-	Schemes administration later than one year and not later than two years	2,197
-	Schemes administration later than two years and not later than five years	6,741
-	Schemes administration later than five years	1,935
2,542	**Total non-cancellable contractual commitments payable**	**13,136**

On 3 November 2003 the Authority entered into a new agreement with Annuitas Management Limited, a joint venture company formed by the Authority and the Board of Trustees of the National Provident Fund, to provide secretarial and executive support to the Board. This agreement, although cancellable on twelve months written notice, is for an initial term of four years.

Estimated commitments under this agreement are:

2004 $000 Actual		**2005** **$000** **Actual**
1,000	Management services not later than one year	1,000
1,000	Management services later than one year and not later than two years	1,333
1,333	Management services later than two years and not later than five years	-
3,333		**2,333**

These statements are to be read in conjunction with the Statement of Accounting Policies and Notes to the Financial Statements.

GOVERNMENT SUPERANNUATION FUND AUTHORITY
STATEMENT OF CONTINGENT LIABILITIES
AS AT 30 JUNE 2005

The Authority has an obligation under contract to redecorate the Bowen space on 17 February 2009. In terms of section 15E (1) of the Act, the Authority's expenses are reimbursed by the Government Superannuation Fund which recovers them from the Crown, as provided for in section 95 of the Act, and other employers. Accordingly, the Authority's obligation does not constitute a liability of the Authority.

There were no contingent liabilities as at 30 June 2005.

These statements are to be read in conjunction with the Statement of Accounting Policies and Notes to the Financial Statements.

STATEMENT OF ACCOUNTING POLICIES

The following policies have been applied in the preparation of the financial statements

(i) Reporting entity and statutory base

The Government Superannuation Fund Authority ("the Authority") was established as a Crown entity by section 15A of the Government Superannuation Fund Act ("the Act") and became an autonomous Crown entity under the Crown Entities Act 2004. The core business of the Authority is to manage the assets and administer the schemes of the Government Superannuation Fund.

These financial statements have been prepared in accordance with section 41 of the Public Finance Act 1989.

Separate financial statements have been prepared for the Government Superannuation Fund ("the Fund") in terms of section 93 of the Act.

(ii) Measurement base

The financial statements are prepared on the historical cost basis. The reporting currency is in New Zealand dollars.

(iii) Particular accounting policies

The following particular accounting policies, which materially affect the measurement of financial performance, financial position, and cash flows, have been consistently applied:

(a) Forecast figures

The forecast figures are those approved by the Authority Board at the beginning of the period and presented in the Authority's Statement of Intent.

The forecast figures have been prepared in accordance with generally accepted accounting practice, and are consistent with the accounting policies adopted by the Authority Board for the preparation of the financial statements.

(b) Goods and services tax ("GST")

The Authority makes principally exempt supplies for GST purposes as it manages superannuation schemes. From 1 January 2005, GST was imposed on certain services supplied from outside New Zealand. The affected transactions for the Authority are mainly fees incurred in relation to the custody of assets and investment reports. Apart from GST on transactions relating to the lease of levels 3 and 4 of 33 Bowen Street, Wellington ("the Bowen space"), which are recoverable as input tax, GST is included in expenditure.

(c) Taxation

As a public authority in terms of the Income Tax Act 1994 the Authority is exempt from income tax.

(d) Statement of cash flows

The statement of cash flows has been prepared using the direct approach.

- *Cash and cash equivalents*

Cash and cash equivalents consist of current accounts in banks, used in the day-to-day cash management of the activities of the Authority, and are unconditionally convertible to cash within two working days.

- *Operating activities*

Operating activities include all receipts of revenues and investment income, and payments of expenses.

- *Investing activities*

Investing activities relate to the acquisition, holding, and disposal of fixed assets.

- *Financing activities*

Financing activities relate to changes in equity capital structure.

(e) Operating leases

Section 22 of the Government Superannuation Fund Amendment Act 2001, ("the Amendment Act") vested in the Authority the Bowen space. The lease of the Bowen space is classified as an operating lease. Payments under the lease are recognised as expenses in the periods in which they are incurred.

(f) Financial instruments

The Authority is party to financial instruments as part of its normal operations. These financial instruments include bank accounts, debtors, and creditors. All financial instruments are recognised in the Statement of Financial Position. All revenues and expenses in relation to financial instruments are recognised in the Statement of Financial Performance.

All financial instruments are shown at their estimated fair values.

(g) Accounting for Joint Ventures

On 28 September 2001, the Authority and the Board of Trustees of the National Provident Fund ("NPF") formed a joint venture company, Annuitas Management Limited ("Annuitas"), to provide secretarial and executive support under management services agreements with both organisations. The Authority has a 50% ownership in Annuitas, but does not equity account for Annuitas as this is deemed to be immaterial. The authorised, issued and paid up capital of Annuitas is $2.

(iv) Reporting period

The reporting period is the year ended 30 June 2005. Comparative figures are for the year ended 30 June 2004.

(v) Changes in accounting policy

There were no changes in accounting policies during the year. All policies have been applied on a basis consistent with those used in the prior year.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 JUNE 2005

1 Transfer from the Government Superannuation Fund

In terms of section 15E (1) of the Act, the administrative expenses of the Authority, including investment management and custody expenses, are reimbursed by the Government Superannuation Fund ("Fund"). Both the Crown and other employers reimburse the Fund under section 95 of the Act for the Authority's expenses. In the reporting period, as certified by the Government Actuary:

- the Crown contributed 84% of the Authority's investment management and custody expenses reimbursed by the Fund, and other employers contributed the balance of 16%.
- the Crown contributed 78% of the Authority's other operating expenses reimbursed by the Fund, and other employers contributed the balance of 22%.

2 Investment management and custody

2004 $000		**2005** **$000**
5,347	Investment management expenses	**6,048**
761	Custodian expenses	**884**
6,108	Total	**6,932**

3 Operating expenses

2004 $000	Operating expenses include:	**2005** **$000**
120	Audit	**121**
14	Other assurance fees paid to Auditor	**28**
172	Board fees and expenses	**166**
707	Gross rental and outgoings – Bowen space	**691**
923	Annuitas	**981**

4 Receivables and prepayments

2004 $000		2005 $000
1,784	Government Superannuation Fund	**2,649**
197	Other receivables	**9**
1,981	Total receivables and prepayments	**2,658**

5 Payables

2004 $000		2005 $000
1,514	Investment management	**2,011**
353	Professional services	**732**
17	Trade creditors	**-**
246	Other creditors	**249**
57	Annuitas Management Limited	**30**
2,187	Total payables	**3,022**

6 Financial instruments

(a) Credit risk

Credit risk is the risk that a third party will default on its obligation to the Authority, causing the Authority to incur a financial loss. Financial instruments, which potentially subject the Authority to credit risk, consist principally of cash and receivables.

The Authority has a minimal credit risk in its holdings of cash, bank deposits, and receivables.

The Authority does not require any collateral or security to support financial instruments.

There is no significant concentration of credit risk other than in the Government Superannuation Fund.

The maximum amount of credit risk for each class is the carrying amount in the Statement of Financial Position.

(b) Currency risks

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates.

The Authority has no exposure to currency risk.

(c) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates.

The Authority has no significant interest rate risk.

(d) Fair values

The fair values of financial instruments are equivalent to the carrying amounts disclosed on the Statement of Financial Position.

7 Employee remuneration

The Authority has no employees.

Annuitas Management Limited ("Annuitas"), a joint venture company formed by the Authority and the Board of Trustees of the National Provident Fund ("NPF"), provides staff who act in management and secretarial roles for both organisations.

8 Board fees

Board members were paid the following fees during the period.

2004 $		**2005** $
	Chairman	
37,400	Basil Logan	37,400
	Deputy Chairman	
23,376	David May	23,376
	Members	
18,700	Colin Blair	18,700
18,700	Helen Bowie	18,700
18,700	Tim McGuinness	18,700
18,700	Ralph Stockdill	18,700
18,700	Susie Weaver	18,700

The Authority also met Board members' travel expenses, where applicable, to attend Board meetings, and for travel on matters directly related to the business of the Authority.

9 Related party information

The Authority is an autonomous Crown entity.

In terms of section 19(1) of the Act the Authority has appointed Datacom Employer Services Limited to administer the GSF Schemes for a term of six years from 1 May 2005.

The Authority has entered into various transactions with Government Departments, and Crown organisations on an arm's length basis in the normal course of business. These transactions are not considered to be related party transactions

In a joint initiative, the Authority and the Guardians of the New Zealand Superannuation Fund have appointed specialist screening organisations to assist with the implementation of policies, standards and procedures for avoiding prejudice to New Zealand's reputation as a responsible member of the world community. A cost – sharing agreement has been agreed. David May (Deputy Chairman) is Chairman of the Guardians of New Zealand Superannuation.

Colin Blair (Board member) was a member of the Board of Trustees of the National Provident Fund until 31 July 2004.

During the reporting period, the Authority paid Annuitas $981,000 (2004: $923,000) for management and secretarial services.

10 Actual versus forecast

Upward fluctuations in market values of investments resulted in greater investment management and custody expenses than the forecast set out in the Statement of Financial Performance on page 14.

In addition, effective from 1 January 2005 legislation applied GST to certain services supplied from outside New Zealand. This had the effect of increasing the accounting and reporting costs included in custody expenses.

Operating expenses are greater than forecast, partly due to costs involved in the implementation of the facility that provides an option for members of the GSF Police sub-scheme to transfer to the Police Superannuation Scheme.

Deloitte.

AUDIT REPORT
TO THE READERS OF THE GOVERNMENT SUPERANNUATION FUND AUTHORITY'S FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2005

The Auditor-General is the auditor of Government Superannuation Fund Authority (the Authority). The Auditor-General has appointed me, Michael Wilkes, using the staff and resources of Deloitte, to carry out the audit of the financial statements of the Authority, on his behalf, for the year ended 30 June 2005.

Unqualified Opinion

In our opinion the financial statements of the Authority on pages 9 to 26:

- comply with generally accepted accounting practice in New Zealand; and
- fairly reflect:
  - the Authority's financial position as at 30 June 2005;
  - the results of its operations and cash flows for the year ended on that date; and
  - its service performance achievements measured against the performance targets adopted for the year ended on that date.

The audit was completed on 7 September 2005, and is the date at which our opinion is expressed.

The basis of the opinion is explained below. In addition, we outline the responsibilities of the Government Superannuation Fund Authority Board and the Auditor, and explain our independence.

Basis of Opinion

We carried out the audit in accordance with the Auditor-General's Auditing Standards, which incorporate the New Zealand Auditing Standards.

We planned and performed our audit to obtain all the information and explanations we considered necessary in order to obtain reasonable assurance that the financial statements did not have material misstatements, whether caused by fraud or error.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements. If we had found material misstatements that were not corrected, we would have referred to them in the opinion.

The audit involved performing procedures to test the information presented in the financial statements. We assessed the results of those procedures in forming our opinion.

Audit procedures generally include:

- determining whether significant financial and management controls are working and can be relied on to produce complete and accurate data;
- verifying samples of transactions and account balances;
- performing analyses to identify anomalies in the reported data;
- reviewing significant estimates and judgements made by the Board;
- confirming year-end balances;
- determining whether accounting policies are appropriate and consistently applied; and
- determining whether all financial statement disclosures are adequate.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements.

We evaluated the overall adequacy of the presentation of information in the financial statements. We obtained all the information and explanations we required to support the opinion above.

Responsibilities of the Government Superannuation Fund Authority Board and the Auditor
The Board is responsible for preparing financial statements in accordance with generally accepted accounting practice in New Zealand. Those financial statements must fairly reflect the financial position of the Authority as at 30 June 2005. They must also fairly reflect the results of its operations and cash flows and service performance achievements for the year ended on that date. The Board's responsibilities arise from the Public Finance Act 1989.

We are responsible for expressing an independent opinion on the financial statements and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001 and section 43(1) of the Public Finance Act 1989.

Independence
When carrying out the audit we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the Institute of Chartered Accountants of New Zealand.

In addition to the audit we provided further assurance services around the transition of the Government Superannuation Fund administration, which is compatible with independence requirements. Other than the audit and these assignments, we have no relationship with or interests in the Authority.

Michael Wilkes
DELOITTE
On behalf of the Auditor-General
WELLINGTON, NEW ZEALAND

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Solicitors:
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Crown Law
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Banker:
Bank of New Zealand

Auditor:
Michael Wilkes
Deloitte
on behalf of
The Auditor-General
PO Box 1990
Wellington

GOVERNMENT SUPERANNUATION FUND

INTRODUCTION

On behalf of the Government Superannuation Fund Authority ("the Authority"), I have pleasure in presenting this report on the GSF Fund ("the Fund" or "GSF") for the year ending 30 June 2005. The report is made in accordance with section 93B of the Government Superannuation Fund Act 1956 ("the Act").

The Fund dates back to 1948 when it was established to provide a way for state sector employees to save for their retirement. Contributors make regular payments to the Fund and, in return, on retirement, receive a defined level of income. Employers, which are not funded directly by the Government, pay contributions as set by the Government Actuary, as the amount necessary to fund the balance of their employees' entitlements. The Government has never paid employer contributions in respect of its own employees. Instead, it meets the balance of the costs of the employees' entitlements as they become payable. The Fund was largely closed to new members in 1992.

In 2001, the Government Superannuation Fund Authority ("the Authority") was established to manage the Fund's assets and administer the GSF Schemes.

This annual report sets out how the assets of the Fund are invested, the annual results for the financial year ending 30 June 2005, information on membership and various other matters required by the Act.

Information on the Authority covering governance, Schemes' administration, Board members and service performance can be found in the Authority's annual report on page 1.

Investment results

The Fund's pre-tax investment return for the year was 11.83%. The after-tax return was 7.38%. This compares with the after-tax return of the median superannuation scheme, in the Watson Wyatt Investment Performance Survey (covering 78 superannuation schemes) for the year ended 30 June 2005, of 7.92%. The average after-tax return for the Fund over the last three years was 6.11%. This compares with the median average after-tax return in the Watson Wyatt survey, over the same period, of 5.96%.

The Fund's asset classes performed in line with their respective benchmarks. The overall Fund return was favourably influenced by the performance of New Zealand equity markets and, to a lesser extent, international fixed interest markets.

The Authority takes a long-term view of its investment strategy for the Fund. It is confident that, by investing in a diversified portfolio, in the long-run the effects of volatility will be minimised and the long-term return objective, of outperforming a portfolio invested entirely in New Zealand Government Stock, will be achieved.

The Authority regularly reviews its investment strategy and the asset allocation for the Fund to ensure they remain appropriate and consistent with legislative requirements, and best practice. The performance of the investment managers appointed by the Authority is also regularly reviewed to ensure that they are complying with the terms of the mandates and, where appropriate, are adding value to the Fund.

Membership

Although the GSF Schemes were closed to new members in July 1992, and the Pacific Island sub-schemes closed on 22 October 1995, the GSF Schemes will continue to have a very substantial membership for many years. As at 30 June 2005, there were 22,241 contributors (2004: 23,719) to the GSF Schemes and 47,587 annuitants (2004: 47,695), a total of 69,828 members (2004: 71,414). Further details are set out in the Membership Commentary on page 39.

Mortgage finance

No new mortgages are being granted. The GSF mortgage portfolio, as at 30 June 2005, was 11 mortgages totalling $0.206 million (30 June 2004: 20 mortgages totalling $0.3 million), with an average earning rate of 5.06 % for the year (30 June 2004: 5.25 %) after-tax and mortgage administration charges.

Basil Logan.

Basil Logan
Chairman
Government Superannuation Authority Board

REGULATORY STATEMENT

In accordance with the Superannuation Schemes Act 1989 the Authority states that to the best of its knowledge and belief, for the financial year ended 30 June 2005,

i all contributions required to be made to the Fund, under the Government Superannuation Fund Act 1956, ("the Act") have been made or accrued.

ii all benefits required to be paid from the Fund under the Act have been paid.

iii due to the partially funded nature of the Government Superannuation Fund Schemes, the market value of assets did not match the accrued benefit liability of the Fund by \$11,431 million (2004: \$10,167 million). The deficiency is covered by Section 95 of the Act, which requires the Minister of Finance to appropriate funds from public money to meet the annual deficiency in payments from the Fund.

iv all employer contributions paid were in accordance with the most recent recommendations of the Government Actuary.

Basil Logan.

Basil Logan
On behalf of the Government Superannuation Fund Authority

7 September 2005

STATEMENT OF RESPONSIBILITY

The financial statements of the Government Superannuation Fund ("the Fund") for the year ended 30 June 2005 have been prepared in accordance with Section 93 of the Government Superannuation Fund Act 1956.

The Government Superannuation Fund Authority ("the Authority") is responsible for the preparation of the financial statements and the judgments made in the process of producing those statements.

The Authority confirms that:

- internal control systems have been established and maintained during the year to assure reasonable reliability and integrity of these financial statements.

- the investment policies, standards, and procedures for the Fund, commencing on page 61, have been complied with.

In our opinion, the attached financial statements and reports fairly reflect the net assets, as at 30 June 2005, and the changes in net assets and the cash flows of the Fund, for the year ended 30 June 2005.

Basil Logan
On behalf of the Government Superannuation Fund Authority

Alan Langford
Chief Executive

7 September 2005

INVESTMENT COMMENTARY

There was no change to the Fund's strategic asset allocation during the year. Investment into property commenced during the year and is being undertaken on a progressive basis. All other asset classes were maintained within their rebalancing tolerances, set as part of the strategic asset allocation, as illustrated in the following table.

Asset Class	**Actual at 30 June 2004**		**Actual at 30 June 2005**		**Strategic Asset Allocation Target**
	$000	**%**	**$000**	**%**	**%**
NZ Fixed Interest	473,128	14.1	512,961	14.5	14.0
International Fixed Interest	760,156	22.5	733,065	20.8	21.0
NZ Equities	550,442	16.4	571,762	16.2	15.0
International Equities	1,338,940	39.8	1,462,430	41.3	42.5
Property	-	-	173,894	4.9	7.5
Cash and short term investments	242,251	7.2	79,019	2.3	-
	3,364,917	**100.0**	**3,533,131**	**100.0**	**100.0**

Investment management

The Authority has appointed experienced New Zealand and international managers to manage the various asset classes. The managers appointed by the Authority are listed in the Directory at the end of this report.

Investment performance

The Fund's pre tax investment return was 11.83%. The surplus after tax represents a return on average net assets of 7.38%.

In the long term, the performance of the Fund will be assessed by comparing the Fund's return (after tax) with the NZX New Zealand Government Stock Gross Return Index (after tax) plus 2.5% per annum over rolling ten year periods.

For the current year the surplus after tax of 7.38% can be compared with the return from the NZX New Zealand Government Stock Gross Return Index (after tax), plus 2.5% per annum, of 7.74%.

The table below compares the pre tax investment returns by asset class and for the Fund for the financial years ended 30 June 2004 and 2005.

Asset Class	**Year ended 30 June**	
	2004	**2005**
	%	%
NZ Fixed Interest	2.05	7.82
International Fixed Interest	6.86	12.32
NZ Equities	21.13	21.34
International Equities	20.87	9.05
Property*	-	11.82
Cash and short term investments	5.48	6.81
Total Fund	12.62	11.83

*Part-year

All asset classes produced good returns during 2005 with New Zealand equities repeating last year's excellent result. The return from international equities, while less than 2005, was greater than that from New Zealand fixed interest. Both New Zealand and international fixed interest produced better returns than 2004.

The volatility of investment returns and the range of results across sectors confirm the benefits of investing in a diversified portfolio and the need to assess the investment performance of the Fund over the longer term.

An analysis of, and commentary on, the returns from each asset class against the benchmark index for the current financial year follows.

New Zealand Cash 6.81%

The NZX 90 day Bank Bill Index return was 6.82% for the same period.

Short-term interest rates in New Zealand are largely guided by the Reserve Bank (RBNZ) Official Cash Rate (OCR). The RBNZ uses the OCR as a tool to manage the inflation rate within its 1-3% target range.

The 'stronger for longer' New Zealand economy saw the RBNZ continue to tighten monetary policy over the year, raising the OCR in a series of 0.25% steps from its opening level of 5.75% to 6.75%. Robust economic activity, particularly in areas such as retail sales and the housing market, put upward pressure on inflation and gave the RBNZ cause for concern that its 3% upper target would be breached.

Cash has been held in the transition period, more lately to fund the planned investment in property, rather than as part of the long-term strategic asset allocation of the Fund. For this reason a return close to that of the index is seen by the Board as an acceptable result.

New Zealand Fixed Interest 7.82%

The NZX Government Stock Gross Return return was 8.10% for the same period.

Returns from fixed interest investments are a combination of interest income and capital gains or losses as market yields fall (generating gains) or rise (generating losses). New Zealand yields are influenced by both domestic and global factors.

Despite the strength of the New Zealand economy, which gave rise to a 1% increase in the OCR, longer-term interest rates fell on the back of lower yields offshore (please refer to International Fixed Interest comments). The 10-year Government bond yield fell from 6.35% to 5.71% over the year, generating capital gains for investors.

During the year both New Zealand fixed interest managers marginally underperformed the benchmark indices. Both had managed the portfolio in anticipation of New Zealand interest rates rising, when in fact they had declined in line with offshore rates.

International Fixed Interest 12.32%

The Lehman Brothers Global Aggregate Index (hedged in New Zealand dollars), return was 12.80% for the same period.

To the surprise of many, including US Federal Reserve Chairman, Alan Greenspan, bond yields fell in all major markets over the year. While economic data was somewhat mixed and the price of oil spiked sharply higher, the movements occurred against a backdrop of the Federal Reserve increasing its official cash rate from 1.25% to 3.25%. Instead it appeared that other factors, such as buying by Asian central bank and European pension funds, drove yields lower. In the key US market, the headline Government 10-year yield finished down 0.66% at 3.92%. The Japanese 10-year yield fell by a similar level, while moves were even more pronounced in the United Kingdom and, more particularly, Germany, where the 10-year yield closed down 1.18% at 3.13%.

During the year two of the international fixed interest managers outperformed the benchmark and one underperformed.

New Zealand Equities 21.34%

The Russell/JB Were Index return was 20.99%.

The New Zealand share market again posted a significant gain over the year. The market was supported by strong earnings growth, reflecting the robust New Zealand economy, and a run of corporate activity. Newly listed children's apparel retailer, Pumpkin Patch, returned an excellent 121%, while Fletcher Building (up 63%) and Hallenstein Glasson (up 54%) also produced excellent returns. At the other end of the spectrum, Air New Zealand was the laggard for the second consecutive year, falling 24%, while Fisher & Paykel Appliances (down 21%) and Nuplex (down 9%) also disappointed. With a return of 12%, market heavyweight Telecom underperformed the market.

International Equities 9.05%

The benchmark index is the weighted average return of the modified indices of the 'grey list' countries, as defined in part A of schedule 3 in the Income Tax Act 1994, 75% hedged in New Zealand dollars. The return for this index was 9.15% for the year.

On the back of generally positive economic news, international share markets also built on the previous year's excellent result. In local currency terms, international shares rose by 11% on average, with the UK market's 15% return leading the way. European shares also performed strongly, the US market was up 4%, while Japanese shares disappointed with the Nikkei Index losing 2%. Further appreciation in the New Zealand dollar once again reduced the extent of the gains. The Authority's policy to hedge 75% of the foreign currency exposure removed some of this negative exchange rate effect.

As the Fund's investments in international shares and the hedging programme are passively managed a return in line with the index is the anticipated outcome. The Authority has resolved to progressively increase the hedge percentage from 75% commencing when the New Zealand dollar is assessed to have reached fair value.

Property 11.82%

The index is the UBS Warburg Global Real Estate Investors Only Total Return Index hedged into New Zealand dollars. The Fund was only invested in property for part of the year. During this period the return for the index was 13.07%.

The spectacular run global property has enjoyed over the past few years continued over the last six months. The broad based rally was supported by strong property market fundamentals, lower bond yields, rising share markets, and significant capital flows as investors increased their allocations to the sector.

As the Fund's investment in property was only made part way through the year it is too early to assess the performance of the three managers of property portfolios.

MEMBERSHIP COMMENTARY

The movement in contributors during the past five years was:

Year ended 30 June	Total Contributors	Change	% Change
2001	29,094	(2,151)	(6.88)
2002	26,990	(2,104)	(7.23)
2003	25,253	(1,737)	(6.44)
2004	23,719	(1,534)	(6.07)
2005	22,241	(1,478)	(6.23)

Contributors by schemes were:

Number 2004	GSF Scheme	Number 2005	% of Total
19,244	General Scheme	18,200	81.83
1,847	Armed Forces	1,576	7.09
2,359	Police	2,224	10.00
187	Prison Officers	169	0.76
59	Judges	50	0.22
23	Parliamentarians	22	0.10
23,719	Total contributors at end of year	**22,241**	**100.00**

The movement in the number of contributors during the year was:

Number 2004		Number 2005
25,253	Contributors at beginning of year	23,719
13	Contributors reinstated	-
(1,077)	Retirements	(1,137)
(40)	Withdrawals from the Fund	(35)
(45)	Death before retirement	(23)
(302)	Cessation of employment before retirement	(208)
(83)	Transfer to other funds	(75)
23,719	Total contributors at end of year	**22,241**

The movement in the number of annuitants during the past five years was:

Year ended 30 June	Total Annuitants	Change	% Change
2001	47,347	24	0.05
2002	47,474	127	0.27
2003	47,779	305	0.69
2004	47,695	(84)	(0.18)
2005	47,587	(108)	(0.23)

The movement in number of annuitants during the year was

Number 2004		Number 2005
47,779	Annuitants at beginning of year	47,695
1,040	New retiring allowances	1,130
860	New allowances to spouses	833
(81)	Allowances deferred	(117)
(1,903)	Discontinued allowances	(1,954)
47,695	Total annuitants at end of year	**47,587**

There were 5,895 deferred pensions at 30 June 2005 (included under contributors) (2004: 5,778)

The movement in total number of members during the past five years was

Year ended 30 June	Total Contributors	Total Annuitants	Total Members	Decrease During Year
2001	29,094	47,347	76,441	(2,127)
2002	26,990	47,474	74,464	(1,977)
2003	25,253	47,779	73,032	(1,432)
2004	23,719	47,695	71,414	(1,618)
2005	22,241	47,587	69,828	(1,586)

From 1996 the number of annuitants has exceeded the number of contributors. The present ratios are:

	2004	%	2005	%
Contributors	23,719	33	22,241	32
Annuitants	47,695	67	47,587	68
	71,414	100	69,828	100

Granting a charge over contributions

In the year to 30 June 2005, 83 charges (2004: 130) were registered by the Fund in favour of chargeholders as security over individual contributor’s contributions.

GOVERNMENT SUPERANNUATION FUND
STATEMENT OF CHANGES IN NET ASSETS
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000 Actual		Notes	**2005 $000 Actual**	2005 $000 Forecast
	Increase in assets from:			
	Investing activities			
	Investment revenue			
78,367	Interest, dividend and other income	1	**80,708**	111,929
315,353	Changes in net market values of investment assets	2	**279,073**	138,564
393,720			**359,781**	250,493
	Operating activities			
	Operating revenue	3		
9,993	Crown		**10,367**	10,181
1,487	Other employers		**2,391**	2,342
11,480			**12,758**	12,523
	Operating expenses	3		
(6,108)	Investment management and custody		**(6,932)**	(6,876)
(5,372)	Administration		**(5,826)**	(5,647)
(11,480)			**(12,758)**	(12,523)
393,720	Surplus before tax and membership activities		**359,781**	250,493
(76,822)	Income tax expense	4	**(115,747)**	(45,389)
316,898	Surplus after tax and before membership activities		**244,034**	205,104
	Membership activities			
	Contributions			
502,194	Government	5	**554,509**	566,341
83,254	Members		**79,947**	71,650
16,920	Other entities		**16,922**	16,138
602,368			**651,378**	654,129
(727,179)	**Benefits paid**	6	**(747,709)**	(762,762)
(124,811)	**Net benefits paid**		**(96,331)**	(108,633)
192,087	**Net increase in net assets**		**147,703**	96,471
3,181,618	Opening net assets available to pay benefits		**3,373,705**	3,354,664
3,373,705	**Net assets available to pay benefits**		**3,521,408**	3,451,135

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

GOVERNMENT SUPERANNUATION FUND
STATEMENT OF NET ASSETS
AS AT 30 JUNE 2005

2004 $000 Actual		Notes	**2005 $000 Actual**	2005 $000 Forecast
	Investments			
	Fixed interest – New Zealand			
347,853	NZ Government stock		**281,029**	351,179
25,742	State, Crown owned/Govt guaranteed securities		**30,885**	60,785
38,885	Other bonds and securities		**47,319**	77,106
2,592	Local authority bonds		**2,576**	2,560
643,130	**Fixed interest – International**		**693,626**	737,443
	Equities			
522,069	New Zealand		**566,273**	526,745
1,269,413	International		**1,388,273**	1,492,445
-	**Properties**		**175,174**	263,372
	Others			
354	Mortgages	7	**206**	150
572,891	Short-term investments		**478,831**	-
3,422,929	**Total investments**		**3,664,191**	3,511,785
	Current assets			
12,268	Cash at bank		**17,722**	10,000
104,496	Receivables and prepayments	8	**205,538**	49,544
4,383	Other receivables	9	**4,602**	2,500
10,760	Income tax receivables		**-**	5,723
131,907	**Total current assets**		**227,862**	67,767
3,554,836	**Total assets**		**3,892,053**	3,579,552
	Less liabilities			
148,317	Other payables	12	**326,874**	125,417
3,872	Benefits payable		**2,726**	3,000
28,942	Deferred tax liability	4	**41,045**	-
181,131	**Total liabilities**		**370,645**	128,417
3,373,705	**Net assets available to pay benefits**		**3,521,408**	3,451,135

The Financial Statements were approved by the Government Superannuation Fund Authority Board on 7 September 2005.

Basil Logan
Chairman
Government Superannuation Fund Authority Board

Colin Blair
Chairman
Audit and Risk Review Committee

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

GOVERNMENT SUPERANNUATION FUND
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000 Actual		**2005 $000 Actual**	2005 $000 Forecast
	Cash flows from operating activities		
	Cash was provided from:		
546,677	Government contributions	**565,270**	574,711
80,345	Members' contributions	**76,135**	71,632
19,336	Other entities	**20,606**	16,190
73,295	Interest and dividends	**83,608**	66,167
4,978	Other	**4,255**	847
	Cash was disbursed to:		
(773,097)	Benefit payments	**(748,311)**	(761,609)
(64,000)	Income tax	**(91,589)**	(47,199)
(11,201)	Operating expenses	**(12,105)**	(12,517)
(123,667)	**Net cash flows from operating activities**	**(102,131)**	(91,778)
	Cash flows from investing activities		
	Cash was provided from:		
7,662,007	Maturities and sales of investment assets	**8,571,754**	8,301,382
308	Mortgage repayments	**154**	150
	Cash was disbursed to:		
(7,549,933)	Purchase of investment assets	**(8,464,323)**	(8,209,754)
112,382	**Net cash flows from investing activities**	**107,585**	91,778
(11,285)	Net increase/(decrease) in cash held	**5,454**	-
23,553	Opening cash brought forward	**12,268**	10,000
12,268	**Closing cash balance**	**17,722**	10,000

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

Reconciliation of net change in net assets to net operating cash flows

2004 $000		2005 $000
192,087	Net increase in net assets	147,703
	Non-cash items	
13,756	Increase in deferred tax liability	12,103
(40)	Capitalised interest	(23)
7	Mortgage management expense	4
13,723		12,084
	Add: Movements in working capital items	
(39,929)	(Increase) decrease in receivables and prepayments	1,324
(26,061)	(Increase) in investment receivables	(102,365)
315	(Increase) decrease in other receivables	(219)
(934)	(Increase)/decrease in tax receivable	10,760
32,052	Increase in Crown contributions received in advance	2,318
68,968	Increase (decrease) in investment payables	174,170
86	Increase in other creditors	776
-	Increase in tax payable	1,293
(1,843)	(Decrease) in benefits accrued	(1,146)
32,654		86,911
	Add: Items classified as investing activities	
(3,871)	(Increase) decrease in accrued interest portion of bonds	2,049
(315,353)	Net (gains) on investments	(279,073)
26,061	Increase in investment settlement receivables	102,365
(68,968)	(Increase) decrease in investment settlement payables	(174,170)
(362,131)		(348,829)
(123,667)	**Net cash out flows from operating activities**	**(102,131)**

The following statements are made as at 30 June 2005

2004 $000		Note	2005 $000
Nil	Contingent liabilities		Nil
10,167,000	Unfunded liability	11	11,431,000
Nil	Trust Money		Nil

This statement is to be read in conjunction with the Statement of Accounting Policies and the Notes to the Financial Statements.

JUDGES SUPERANNUATION ACCOUNT
STATEMENT OF CHANGES IN NET ASSETS
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000		**2005 $000**
	Income from operations *	
9,222	Government contributions	10,945
755	Members contributions	496
9,977		11,441
	Expenditure *	
	Allowances:	
7,559	Retirements	8,035
1,207	Allowances capitalised	2,153
1,211	Spouses and children	1,253
9,977		11,441
-	Net changes	-

PARLIAMENTARY SUPERANNUATION ACCOUNT
STATEMENT OF CHANGES IN NET ASSETS
FOR THE YEAR ENDED 30 JUNE 2005

2004 $000		**2005 $000**
	Income from operations *	
2,914	Government contributions	2,978
235	Members contributions	251
3,149		3,229
	Expenditure *	
	Allowances:	
2,593	Retirements	2,687
-	Allowances capitalised	-
556	Spouses and children	542
-	Refunds	-
3,149		3,229
-	Net changes	-

* These figures are incorporated in the Government Superannuation Fund Statement of Changes in Net Assets.

These statements are to be read in conjunction with the Statement of Accounting Policies and Notes to the Financial Statements.

STATEMENT OF ACCOUNTING POLICIES

The following policies have been applied in the preparation of the financial statements:

(i) *Reporting entity and statutory base*

The financial statements of the Government Superannuation Fund ("GSF or the Fund") are prepared pursuant to section 93B(1) of the Government Superannuation Fund Act 1956 ("the Act").

The Fund was established by section 13 of the Act. It consists of various defined benefit superannuation schemes as prescribed in the Act. Pursuant to section 19H of the Act, the schemes are registered under the Superannuation Schemes Act 1989.

(ii) *Measurement base*

The financial statements are prepared on a going concern basis. The following general accounting policies have been adopted in the preparation of these statements:

(a) assets are measured at net market values; and

(b) the reporting currency is New Zealand dollars.

(iii) *Particular accounting policies*

The following particular accounting policies, which significantly affect the measurement of financial performance, financial position, and cash flows, have been applied:

Reporting requirements

The financial statements have been drawn up in accordance with Financial Reporting Standard FRS-32: *Financial Reporting by Superannuation Schemes*, and with the provisions of relevant legislative requirements.

Reporting period

The reporting period is the year ended 30 June 2005. Comparative figures are for the year ended 30 June 2004.

Valuation of investments

Investment assets are valued as follows:

Type	**Method**
NZ Government Stock	Net market value
Equities	Net market value
Other bonds and debt securities	Net market value
Local Authority bonds	Net market value
Property	Net market value
Mortgages	Realisable value

Valuation of interest rate contracts

Cross currency and interest rate swaps are stated at net market value.

Financial instruments

The following methods have been used to estimate the fair value of each major class of financial instrument:

Financial instrument	**Method**
Cash and call deposits	Realisable value
Short term investments	Net market value
Investments	Net market value
Mortgages	Realisable value
Receivables and prepayments	Realisable value
Creditors	Realisable value

Off balance sheet financial instruments

In the normal course of business, and if appropriate, the investment managers, appointed by the Government Superannuation Fund Authority, enter into transactions involving off balance sheet financial instruments in order to manage the Fund's exposure to risk. These include foreign exchange contracts, swaps, financial options and futures. Investments not taken up as hedging transactions are valued at market rates prevailing at the reporting date. The resulting gains and losses are recognised in the Statement of Changes in Net Assets.

Investment income

Dividend income is recorded on the ex-dividend date. Interest and other investment income are accounted for on an accrual basis. Certain investment expenses are directly charged against investment income. Gains and losses on the sale of equities are determined by using the average cost of equities sold and are recorded on the settlement date.

All realised and unrealised gains and losses at the end of the year are included in the Statement of Changes in Net Assets.

Taxation

Income tax expense is recognised on the surplus before tax and membership activities, adjusted for permanent differences between taxable and accounting income. The income tax expense, charged to the Statement of Changes in Net Assets, includes both the current year liability and the deferred tax on the movement in timing differences, after allowing for non-assessable income and non-deductible expenses.

The liability method of accounting for income taxation is applied on a comprehensive basis. The tax effect of all timing differences, between taxable and accounting income, is recognised in the Statement of Net Assets as a future tax benefit, or a deferred tax liability. The future tax benefit, or deferred tax liability, is stated at the income tax rate prevailing at balance date. The future tax benefit is not recognised until the realisation of the benefit is virtually certain.

Foreign currency transactions

Transactions in foreign currencies are translated to New Zealand currency at the exchange rates in effect at the transaction date. Assets and liabilities denominated in foreign currencies, including forward exchange contracts, are translated at the closing rates of exchange at the balance date. The resulting gains or losses are recognised in the Statement of Changes in Net Assets.

Repurchase agreements (REPOs)

Securities sold under agreements to repurchase are retained within the investments and accounted for accordingly. Liability accounts are used to record the obligation to repurchase.

Statement of cash flows

- *Basis of preparation*

The statement of cash flows has been prepared using the direct approach.

- *Cash and cash equivalents*

Cash and cash equivalents consist of current accounts in banks, used in the day-to-day cash management of the Fund, and are unconditionally convertible to cash within two working days.

- *Operating activities*

Operating activities include all receipts of contributions and investment income, and payments of benefits and expenses.

- *Investing activities*

Investing activities relate to the acquisition, holding, and disposal of investments. Investments can include securities not falling within the definition of cash.

Consolidation

The Fund's financial statements include the Judges Superannuation Account and the Parliamentary Superannuation Account.

(iv) Changes in accounting policies

There were no significant changes in accounting policies during the year. Certain comparative figures have been reclassified and restated to ensure consistency with the current year.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 JUNE 2005

1 Interest, dividends, and other income

2004 $000		**2005 $000**
26,695	NZ Government stock	22,646
3,345	State, Crown owned/Government guaranteed securities	2,785
623	Local Authority bonds	188
2,307	Other bonds and securities	2,084
19,972	International fixed interest	21,853
-	International listed properties	16
2,628	Short term and call deposits, including treasury bills	3,178
21,519	Dividends (New Zealand equities)	25,146
-	Dividends (International listed properties)	1,763
40	Mortgages to members	23
1,238	Other sources	1,026
78,367	Total	**80,708**

2 Changes in net market values of investment assets

2004 $000		**2005 $000**
(21,167)	NZ Government stock	4,729
(1,868)	State, Crown owned/Government guaranteed securities	(735)
(214)	Local Authority bonds	(17)
(1,658)	Other bonds and securities	1,062
13,788	International fixed interest (including hedging gains)	61,430
16,584	Short term investments	17,350
72,255	New Zealand equities	71,856
237,633	International equities (including hedging gains)	113,267
-	International listed properties (including hedging gains)	9,659
-	International unlisted properties (including hedging gains)	472
315,353	Total	**279,073**

3 Operating revenue and expenses

In terms of section 15E (1) of the Act, the administrative expenses of the Government Superannuation Fund Authority ("the Authority"), including investment management and custody expenses, are reimbursed by the Fund. Both the Crown and other employers reimburse the Fund under section 95 of the Act for the Authority's expenses. In the reporting period, as certified by the Government Actuary:

- the Crown contributed 84% of the Authority's investment management and custody expenses reimbursed by the Fund, and other employers contributed the balance of 16%.

- the Crown contributed 78% of the Authority's other operating expenses reimbursed by the Fund, and other employers contributed the balance of 22%.

4 Income tax expense

2004 $000		**2005 $000**
393,720	Surplus before tax and membership activities	359,781
	Plus taxation effect of permanent differences:	
(139,410)	Non-assessable/deductible investment (gains)/ losses	14,299
-	Withholding tax credits	233
9,550	Imputation credits	11,259
263,860		385,572
87,074	Income tax @ 33%	127,239
-	Less withholding tax credits	(233)
(9,550)	Less imputation credits	(11,259)
(702)	Prior year adjustment	-
76,822	Tax expense	**115,747**
	The taxation charge is represented by:	
63,226	Current tax	103,644
14,298	Deferred tax	12,103
(702)	Prior year adjustment	-
76,822		115,747
	Movement in deferred taxation	
(15,186)	Opening balance	(28,942)
(14,298)	Deferred portion of current period tax expense	(12,103)
542	Prior year adjustment	-
(28,942)	Deferred tax liability	**(41,045)**

5 Government contributions

2004 $000		**2005 $000**
490,058	Public Service superannuation benefits	540,586
9,222	Judges superannuation benefits	10,945
2,914	Parliamentarians superannuation benefits	2,978
502,194	Total	**554,509**

Funding arrangements:

There is no requirement on the Crown to fully fund the GSF Schemes. The basis of funding to meet benefits is partly from contributors' contributions, as set out below, and the surplus after tax, the balance being the contributions from the Government and non-departmental employers. Reliance is placed on the provisions in the Act for the Crown to ensure that sufficient funds are available, or will be available, to pay benefits as they fall due.

Members Contribution %	**GSF Scheme**	**Employer Contribution %**
	General Scheme	
6.5	Non-funding	6
6.5	Funding except Islands*	Between 6 and 10
6.5	Islands	6
	Special Schemes	
7.6	Armed Forces	15.4
7.5	Police	16.1
8.5	Prison Officers	Nil

*As the employer contribution rate is subject to age and gender of contributors, it is different from one employer to another.

6 Benefits paid

2004 $000		**2005 $000**
531,172	Pension entitlements	540,634
57,548	Allowances capitalised	76,398
85,492	Spouses and children	87,089
	Refunds:	
29,168	Cessation of employment	25,484
11,379	Transfers to other schemes	8,537
11,292	Cessation of membership	9,082
1,128	Death	485
727,179		**747,709**

7 Mortgages

The Housing New Zealand Corporation manages mortgages previously granted to members of the Fund.

8 Receivables and prepayments

2004 $000		2005 $000
	Receivables:	
-	Crown contributions - operating	1,526
649	Members' contributions	83
1,282	Other entities' contributions	738
2,183	Interest and dividends	989
52,796	Investment settlements receivable	155,161
	Prepayments:	
47,586	Benefits	47,041
104,496	Total	**205,538**

9 Other receivables

2004 $000		2005 $000
4,256	Past service contributions	4,518
127	Pension entitlements	84
4,383	Total	**4,602**

10 Actuarial valuation

Section 94 of the Act 1956 requires that, at least every 3 years or at shorter intervals as directed by the Minister of Finance, the Government Actuary shall examine the financial position of the Fund. On 22 August 1999, the Minister directed an annual valuation to be carried out. The latest published valuation was made at 30 June 2004, and the report, dated 30 November 2004, was tabled in Parliament on 24 March 2005.

11 Liability for accrued benefits

The Government Actuary valued the accrued benefits of the Fund, as at 30 June 2005, to calculate the unfunded past service liability (UPSL) for inclusion in the Crown's Financial Statements for the year ended 30 June 2005. The Government Actuary's report is dated 27 July 2005.

The projected aggregate funding method, based on balance date membership data, was used in the valuation. This method requires the benefits payable from the Fund, relating to service up to the valuation date, to be estimated, and then discounted to the valuation date. The valuation is carried out in accordance with generally accepted accounting practice (GAAP), as considered appropriate by the Crown for the determination of the UPSL. In particular, it requires the liability in respect of the projected benefit payments to be discounted at appropriate after-tax rates derived from Government Stock market prices, as at valuation date.

Significant assumptions, used in the valuation of accrued benefits for inclusion in the Crown Financial Statements were:

2004 %		**2005 %**
	After-tax discount rates	
4.1	- year 1	4.1
4.0	- year 2	3.9
4.2	- year 3	3.9
4.3	- year 4 to year 5	3.7
4.4	- year 6	3.7
4.4	- year 7	3.8
4.4	- year 8	3.8
4.4	- year 9	3.8
4.4	- year 10	3.8
4.4	- year 11 and thereafter	3.8
	CPI	
2.0	- year 1	2.0
2.0	- year 2 to year 7	2.0
2.0	- year 8	2.0
2.0	- year 9	2.0
2.0	- year 10 and thereafter	2.0
	Annual salary increase excluding promotional effects	
3.0	- year 1	3.0
3.0	- year 2 to year 7	3.0
3.0	- year 8	3.0
3.0	- year 9	3.0
3.0	- year10 and thereafter	3.0

Rates of mortality, morbidity and withdrawal are based on scheme experience, that experience being used to adjust standard published tables where available.

UPSL

2004 $000		**2005 $000**
13,541,000	Total accrued benefits as at end of year	14,952,000
3,374,000	*less* Net assets available to pay benefits	3,521,000
10,167,000	Total UPSL as at end of year	**11,431,000**

The UPSL has increased by $1.26 billion between 30 June 2004 and 30 June 2005. The increase was largely caused by reductions in the discount rates used by the Government Actuary (see above) ($865 million) and changes to pensioner mortality rates ($375 million), offset by the surplus after tax made by the Fund, during the year ended 30 June 2005, being greater than assumed by the Government Actuary (reduction of $104 million).

Vested benefits

Vested benefits are benefits payable to members as a whole under the conditions of the GSF Schemes, if they ceased being members on balance date.

Under the terms of the GSF Schemes, the total liability for accrued benefits vested with members, as at 30 June 2005, is $14,757 million (30 June 2004: $13,343 million).

Purchase of additional benefits

Additional payments of $4.382 million (2004: $4.502 million), to acquire further benefits, were made during the year by members with pre-entry service, or on early retirement.

12 Other payables

2004 $000		**2005** **$000**
48	Crown receipts	398
886	Use of money interest payable	441
52	Unallocated contributions	57
1,784	Government Superannuation Fund Authority	2,649
30,151	Crown contributions in advance - benefits	34,371
1,901	Crown contributions in advance - operating	-
-	Income tax payable	1,293
113,495	Investment settlements payable	287,665
148,317	Total	**326,874**

13 Financial instruments

(a) Credit risk

In the normal course of its business the Fund incurs credit risk with the New Zealand Government, state owned enterprises, local authorities, financial institutions and other debtors.

The Fund invests in New Zealand dollar denominated fixed interest securities, equities, secured mortgages, and foreign currency denominated fixed interest securities and equities in accordance with the Statement of Investment Policies, Standards and Procedures (“SIPSP”).

The SIPSP contains credit and exposure policies to limit credit risks from the Fund’s investments.

(b) Foreign currency risks

The Fund is exposed to foreign currency risk by investing in foreign currency denominated fixed interest securities and equities. From April 2002, international equities have been 75% hedged into New Zealand dollars by foreign exchange contracts. From March 2003 the benchmark index for the management of international fixed interest portfolios has been 100% hedged to the United States dollar. The managers of international fixed interest portfolios are permitted under their mandates to hedge the portfolios in the range 90 – 110% to United States dollars by way of foreign exchange contracts. The currency exposure in the international fixed interest portfolios between United States dollars and New Zealand dollars is 100% hedged by foreign exchange contracts.

The face value of the foreign currency contracts, with respect to foreign currency exposure at the end of the year, is as follows:

2004 $000		**2005 $000**
948,328	Foreign currency contracts for international equities	1,027,449
763,372	Foreign currency contracts for international fixed interest securities	732,318
-	Foreign currency contracts for international property	120,514
1,711,700	Total	**1,880,281**

Foreign currency transactions are translated to New Zealand dollars at exchange rates in effect at the date of the transactions.

(c) Interest rate risk

Weighted Average effective interest rates and maturity periods are: -

2005	Effective Interest Rate	0-6 Months $000	6-12 Months $000	12-24 Months $000	24-60 Months $000	Over 60 Months $000	Total $000
Monetary Assets							
NZ Government stock	5.82%	-	10,605	13,673	103,688	153,063	281,029
State, Crown/Govt guaranteed	6.49%	-	13,764	5,929	8,963	2,229	30,885
Other bonds and securities	6.77%	-	3	12,056	8,918	26,342	47,319
Local authority bonds	6.79%	-	-	-	2,576	-	2,576
International fixed interest	3.30%	3,536	10,197	32,635	172,705	474,553	693,626
Mortgages	5.06%	206	-	-	-	-	206
Cash at bank	6.90%	17,722	-	-	-	-	17,722
Short-term investments	5.28%	442,402	36,429	-	-	-	478,831

2004	Effective Interest Rate	0-6 Months $000	6-12 Months $000	12-24 Months $000	24-60 Months $000	Over 60 Months $000	Total $000
Monetary Assets							
NZ Government stock	6.16%	-	96,836	33,020	6,015	211,982	347,853
State, Crown/Govt guaranteed	6.30%	3,193	-	14,485	5,890	2,174	25,742
Other bonds and securities	7.15%	-	-	(162)	26,305	12,742	38,885
Local authority bonds	6.76%	-	-	-	2,592	-	2,592
International fixed interest	3.93%	4,151	2,003	23,119	139,753	474,104	643,130
Mortgages	5.25%	354	-	-	-	-	354
Cash at bank	5.77%	12,268	-	-	-	-	12,268
Short-term investments	4.53%	572,891	-	-	-	-	572,891

(d) Interest rate exposures

The Fund's SIPSP provides the investment managers the ability to use interest rate hedging instruments, within specified limits, to hedge interest rate exposures.

There were no interest rate hedging instruments outstanding as at 30 June 2005 (2004: Nil).

(e) Fair values

The carrying values of the Fund's assets and liabilities are equivalent to their fair values.

14 Related parties

In terms of sections 81W(2), 88(2) and 95(1) of the Act, the Minister of Finance pays into the Fund out of public money any deficiency in benefits payable to contributors and annuitants.

The Fund has business transactions with the Crown, Government Departments, Crown Entities, and State Owned Enterprises together with a number of other public sector entities on an arm's length basis. These transactions are not considered related party transactions except for the following:

The Fund has invested a significant proportion of its assets in New Zealand Government Stock. The Fund's interests are disclosed in the Statement of Net Assets.

The Authority managed the Fund's assets and administered the GSF Schemes. For the year ended 30 June 2005, the Fund paid the Authority $12.758 million (2004: $11.480 million) for operating expenses, as detailed in the Statement of Changes in Net Assets. In turn, the Fund was reimbursed by the Crown and other employers, as set out in Note 3.

15 Actual versus forecasts

- Investment revenues are subject to the volatile nature of investment markets, this being the principal reason for the variance between the forecast and actual changes in net market values of investment assets.
- Upward fluctuations in market values of investments resulted in greater investment management and custody expenses than the forecast set out in the Statement of Changes in Net Assets on page 41. In addition, effective from 1 January 2005 legislation applied GST to certain services supplied from outside New Zealand. This had the effect of increasing the accounting and reporting costs included in custody expenses.
- Administration expenses are greater than forecast, partly due to costs involved in the administration of the transfer from the GSF Police sub-scheme to the Police Superannuation Scheme.
- The forecast benefit payments are actuarially estimated and cannot be projected with accuracy as actual payments are dependent on factors beyond the Authority's control, such as early retirements, redundancies, or unexpected salary changes.

Deloitte.

AUDIT REPORT
TO THE READERS OF THE GOVERNMENT SUPERANNUATION FUND'S FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2005

The Auditor-General is the auditor of Government Superannuation Fund (the Fund). The Auditor-General has appointed me, Michael Wilkes, using the staff and resources of Deloitte, to carry out the audit of the financial statements of the Fund, on his behalf, for the year ended 30 June 2005.

Unqualified Opinion

In our opinion the financial statements of the Fund on pages 41 to 57:

- comply with generally accepted accounting practice in New Zealand; and
- fairly reflect:
    - the Fund's net assets as at 30 June 2005; and
    - the changes in net assets and cash flows for the year ended on that date.

The audit was completed on 7 September 2005, and is the date at which our opinion is expressed.

The basis of the opinion is explained below. In addition, we outline the responsibilities of the Government Superannuation Fund Authority Board and the Auditor, and explain our independence.

Basis of Opinion

We carried out the audit in accordance with the Auditor-General's Auditing Standards, which incorporate the New Zealand Auditing Standards.

We planned and performed our audit to obtain all the information and explanations we considered necessary in order to obtain reasonable assurance that the financial statements did not have material misstatements, whether caused by fraud or error.

Material misstatements are differences or omissions of amounts and disclosures that would affect a reader's overall understanding of the financial statements. If we had found material misstatements that were not corrected, we would have referred to them in the opinion.

The audit involved performing procedures to test the information presented in the financial statements. We assessed the results of those procedures in forming our opinion.

Audit procedures generally include:

- determining whether significant financial and management controls are working and can be relied on to produce complete and accurate data;
- verifying samples of transactions and account balances;
- performing analyses to identify anomalies in the reported data;
- reviewing significant estimates and judgements made by the Board;
- confirming year-end balances;
- determining whether accounting policies are appropriate and consistently applied; and
- determining whether all financial statement disclosures are adequate.

We did not examine every transaction, nor do we guarantee complete accuracy of the financial statements.

We evaluated the overall adequacy of the presentation of information in the financial statements. We obtained all the information and explanations we required to support the opinion above.

Responsibilities of the Government Superannuation Fund Authority Board and the Auditor

The Board is responsible for preparing financial statements in accordance with generally accepted accounting practice in New Zealand. Those financial statements must fairly reflect the net assets of the Fund as at 30 June 2005. They must also fairly reflect the changes in net assets and cash flows for the year ended on that date. The Board's responsibilities arise from the Government Superannuation Fund Act 1956.

We are responsible for expressing an independent opinion on the financial statements and reporting that opinion to you. This responsibility arises from section 15 of the Public Audit Act 2001 and section 93A of the Government Superannuation Fund Act 1956.

Independence

When carrying out the audit we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the Institute of Chartered Accountants of New Zealand.

Other than the audit, we have no relationship with or interests in the Fund.

Michael Wilkes
DELOITTE
On behalf of the Auditor-General
WELLINGTON, NEW ZEALAND

STATEMENT OF INVESTMENT POLICIES, STANDARDS, AND PROCEDURES

DATED 6 August 2005

Currency of Statement

The Statement of Investment Policies, Standards and Procedures was last updated, as at 6 August 2005, and was current, as at 7 September 2005. Please note the Government Superannuation Fund Authority ("the Authority") is required to review the investment policies, standards and procedures for the Government Superannuation Fund ("the Fund") at least annually, and may choose to do so more regularly. Accordingly, the Statement of Investment Policies, Standards and Procedures ("SIPSP") is subject to change at any time.

INTRODUCTION

This document is dated 6 August 2005 . It replaces the previous document dated 5 May 2005. The amendments to the 5 May 2005 document (and previous amendments) are recorded in the version control document called "SIPSP Amendments".

This document is intended to assist the governance and management of the investment of the Fund.

The first part of the document sets out the investment policies, standards and procedures required under the Government Superannuation Fund Act 1956 ("the Act"). The second part describes the current investment structure and the specific investment parameters currently applied to the investment of the Fund.

Government Superannuation Fund Act 1956

The Act requires that the Authority must:

> *"… invest the Fund on a prudent, commercial basis and, in doing so, must manage and administer the Fund in a manner consistent with -*
>
> *(a) best-practice portfolio management; and*
>
> *(b maximising return without undue risk to the Fund as a whole; and*
>
> *(c) avoiding prejudice to New Zealand's reputation as a responsible member of the world community."*
>
> [Section 15J(2) of the Act]

Section 15L of the Act requires that:

> *"(1) The Authority must establish, and adhere to, investment policies, standards, and procedures for the Fund that are consistent with its duty to invest the Fund on a prudent, commercial basis, in accordance with section 15J.*
>
> *(2) The Authority must review those investment policies, standards, and procedures for the Fund at least annually."*

Section 15M sets out 11 items that must be covered, as a minimum, in the statement of investment policies, standards, and procedures. Section 15M is reproduced in full as Appendix 1.

STATEMENT OF INVESTMENT BELIEFS

The Authority appreciates that one of the hallmarks of successful investment organisations is the development and adoption of a clear set of investment beliefs to communicate shared values and to provide a starting point for investment actions. Accordingly the Authority Board ("the Board") adopted the following set of Investment Beliefs on 3 August 2005. It is intended that the Beliefs are continuously reviewed and formally reviewed as part of the annual statutory review of the SIPSP.

1. **Higher returns are associated with higher risks**.
   Investors demand a return premium to compensate them for investing in risky assets.

2. **Setting the asset policy mix is the most important investment decision.**
   Setting, managing and monitoring the appropriateness of the strategic asset allocation is the key investment management function. Although active management may be engaged to seek additional sources of return to the underlying asset class returns, their additional impact on the risk and return characteristics of the portfolio is secondary compared to the risks and returns of the underlying markets themselves.

3. **Diversification reduces risk**.
   Total investment risk can be reduced for any given return target by investing in a diversified range of asset classes that gives exposure to different sources of return which are complementary, or not closely related and, within an asset class, by investing across a range of industries, countries and companies. Diversification reduces risk but has a proportionately lesser effect on returns. A portfolio, that is well-diversified across asset classes and well-diversified within those asset classes, will deliver more consistent returns over time than a less diversified portfolio.

4. **Market timing is not a reliable source of return because of the short term unpredictability of returns.**
   Asset values and returns are determined largely by expectations about fundamental factors that drive future cash flows and by the discount rates applied to those cash flows. In the short term, returns fluctuate randomly as new information is incorporated into asset prices. Returns are also affected by uncertainty, temporary influences and sentiment in the short term. These random components (sometimes referred to as "noise") make predicting returns very difficult over short periods and hence market timing is not a reliable source of return. Over longer periods, the more stable components of return become more evident.

5. **Nevertheless, account should be taken of unusual asset price behaviour**.
   Asset prices deviate significantly from normal relationships from time to time, increasing the risk of abnormal future returns, ie asset price 'bubbles' do occur. Notwithstanding the difficulty of market timing, it is appropriate to take account of this risk in implementing major investment decisions.

6. **Control of costs is important.**

Investment returns should be considered net of all costs. Costs can be incurred in the form of fees, commissions, transaction expenses, and market impact costs. Costs can also be structural such as deviations from the strategic asset allocation, maintenance of the management structure and unduly constraining investment managers' ability to add value.

7. **Markets vary in their efficiency, and market inefficiencies offer skillful managers the opportunity to add value.**

The more inefficient the market, the greater the opportunities for skilful active managers to out-perform the returns from a well –diversified passively held portfolio through analysis and research, and by exploiting market inefficiencies. It is possible to identify skilful managers by thorough research, The greater expected returns from active management should be weighed against the higher costs and any tax implications involved with active management. Rewards to active management will be maximized by engaging skilful managers with diversified investment approaches over the broadest possible number of independent investment decisions.

PART 1: MATTERS REQUIRED UNDER THE ACT

(Section references are to sections of the Act)

1 THE CLASSES OF INVESTMENTS IN WHICH THE FUND IS TO BE INVESTED AND THE SELECTION CRITERIA FOR INVESTMENTS WITHIN THOSE CLASSES (SECTION 15M (A))

The Board has determined that the Fund shall be invested in the following general asset classes:

International equities;
New Zealand equities;
Property;
New Zealand fixed interest;
International fixed interest; and
New Zealand cash and short-term securities

Currency hedging and derivative instruments will form part of the Fund's investment strategy.

The Fund may be invested in other asset classes or in specific sub-categories of the asset classes listed above in the future.

The selection criteria for investments within the current asset classes are:

1.1 International equities

1.1.1 the international equity securities that comprise the broad-based passively managed international equity products that have current IRD binding rulings enabling gains to be accumulated free of taxation in New Zealand;

1.2 New Zealand equities

1.2.1 the equity securities and securities convertible into equity securities of companies that are either:

1.2.1.1 listed on the New Zealand Stock Exchange (NZX) and resident in New Zealand for tax purposes; or

1.2.1.2 are included in the NZSX50 Index.

1.3 Property

1.3.1 shares or units in companies or trusts that invest principally in real property that are listed on recognised* stock exchanges.

1.4 New Zealand fixed interest

1.4.1 debt instruments issued or guaranteed by the New Zealand Government or an agency of the New Zealand Government;

1.4.2 New Zealand dollar denominated debt instruments issued by New Zealand entities that have debt ratings, as rated by a recognised international rating agency, satisfactory* to the Board;

1.5 International fixed interest

1.5.1 debt instruments denominated in foreign currencies that are issued or guaranteed by foreign governments or government agencies that are satisfactory* to the Board;

1.5.2 corporate credit and asset-backed or collateralised instruments denominated in foreign currencies that are issued or guaranteed by entities that are satisfactory* to the Board;

1.6 Cash

1.6.1 New Zealand dollars and, as specifically provided for in the relevant investment management contracts, foreign currencies held in the Portfolio for liquidity purposes;

1.6.2 fixed interest securities and short dated money market instruments with a short-term debt rating, as rated by a recognised international rating agency, satisfactory* to the Board.

1.7 Currency Management

<u>International Equities</u>

1.7.1 foreign exchange hedging contracts relating to the currencies of the "grey list" countries (Australia, Canada, Germany, Japan, United Kingdom and the United States of America) and New Zealand.

1.7.2 foreign exchange hedging contracts where the counterparties have an appropriate* short-term credit rating measured by a recognised international rating agency.

<u>International fixed interest</u>

1.7.3 foreign exchange hedging contracts relating to the currencies in which the securities that comprise international fixed interest portfolio are denominated.

1.7.4 foreign exchange hedging contracts where the counterparties have an appropriate* short-term credit rating measured by a recognised international rating agency.

<u>Property – segregated portfolios</u>

1.7.5 Foreign exchange hedging contracts relating to the currencies (or their close proxies) in which the securities that comprise property portfolio are denominated.

1.7.6 Foreign exchange hedging contracts where the counterparties have an appropriate* short-term credit rating measured by a recognised international rating agency.

<u>Property – pooled products</u>

1.7.7 In accordance with any selected managers' currency hedging policy and practice.

1.8 Derivatives

Managers are permitted to use derivative instruments. The policies, standards and procedures with respect to derivative instruments are presented in section 7.

***Details of the Board's current debt and credit rating criteria, counter-party limits and which stock exchanges are "recognised" for the purpose of the Property mandates are presented in Part 2: Current Investment Structure of the Fund.*

2 THE DETERMINATION OF BENCHMARKS OR STANDARDS AGAINST WHICH THE PERFORMANCE OF THE FUND AS A WHOLE, CLASSES OF INVESTMENT, AND INDIVIDUAL INVESTMENTS WILL BE ASSESSED. (SECTION 15M(B))

2.1 Determination of Benchmarks

The benchmarks for the Fund as a whole and for individual asset classes are selected to be consistent with the risk and return assumptions that underpinned determination of the strategic asset allocation for the Fund*.

2.2 Assessment of Performance

The Board recognises that investment performance objectives are expected to be met over the medium term. From year to year, investment returns may not meet those medium term objectives.

Investment performance is measured:

2.2.1 before the deduction of any fees due to the investment managers; and

2.2.2 after transaction costs have been deducted (but before custodian costs are deducted).

<u>Performance of the Fund as a whole</u>

The performance of the Fund as a whole will be assessed by comparing the Fund return (after tax) with the NZX New Zealand Government Stock Gross Index return (after tax) plus 2.5% per annum over rolling ten-year periods. This performance measure will be monitored at least annually.

<u>Classes of investment</u>

The performance of classes of investment will be assessed by comparing the actual performance of the investment managers for that asset class with the benchmark for that asset class plus any return value-added component the Board has decided is appropriate*. Investment managers' performances are generally considered over rolling three-year periods and managers are required to meet mandate compliance criteria.

Investment managers are also to be compared to other managers in the same asset class.

**Details of the Board's current benchmarks and value-added requirements are presented in Part2: Current Investment Structure of the Fund.*

3 STANDARDS FOR REPORTING THE INVESTMENT PERFORMANCE OF THE FUND (SECTION 15M(C))

3.1 Reporting by the Investment Manager

The investment management mandates should contain such reporting provisions to enable the Board to determine the managers' compliance with the investment contract and success in meeting the Board's investment objectives.

The periodic reports should cover:

3.1.1 reviews of the portfolio managed by the particular investment manager for the Board ('the Portfolio') including performance reporting and Portfolio valuations;

3.1.2 certification that the terms of the investment contract have been met including certification that the Portfolio has not been leveraged;

3.1.3 reconciliation of Portfolio accounts with those of the custodian;

3.1.4 a statement of any voting right issues.

The Board will review the managers' investment performance quarterly and investment managers will be required to meet with the Board on an annual basis.

3.2 Reporting by the Custodian

In respect of each investment manager, the custodian is to provide the reports required by the Authority to enable monitoring and review of managers' performance.

Those reports should include:

3.2.1 the overdraft position of each Portfolio;

3.2.2 accounting matters including Portfolio valuation;

3.2.3 reconciliation of Portfolio values and cash flows with the investment managers;

3.2.4 investment performance measurement and analysis;

3.2.5 taxation matters; and

3.2.6 reports of compliance with mandate specific restrictions.

4 ETHICAL INVESTMENT, INCLUDING POLICIES, STANDARDS, OR PROCEDURES FOR AVOIDING PREJUDICE TO NEW ZEALAND'S REPUTATION AS A RESPONSIBLE MEMBER OF THE WORLD COMMUNITY (SECTION 15M(D))

PART A: POLICIES, STANDARDS AND PROCEDURES FOR AVOIDING PREJUDICE TO NEW ZEALAND'S REPUTATION AS A RESPONSIBLE MEMBER OF THE WORLD COMMUNITY

4.1 Policies

In formulating Standards relating to managing and administering the Fund consistent with avoiding prejudice to New Zealand's reputation as a responsible member of the world community, the Board is conscious of:

4.1.1 the requirements of the Act. For example, the Board recognises that the manner in which the management and administration of the Fund is organised through its governance and management processes is one important aspect of the Standards and Procedures developed under the Act's mandate;

4.1.2 the public nature of the Fund and of the identity of the Fund's key stakeholders (namely the Crown, public service employers, contributors and pensioners). The pensioners and contributors of the GSF comprise a large group of retired, and currently working, New Zealand public servants whose GSF membership provides Crown underwritten benefits in retirement. These pensioners and contributors represent a cross-section of the past and present New Zealand public service.

In order to be workable, the Standards that are formulated need to be:

4.1.3 based to the extent possible on objective criteria; and

4.1.4 capable of practical implementation.

4.2 Standards

Active Investments

The Authority's obligations to manage and administer active investments of the Fund in a manner consistent with avoiding prejudice to New Zealand's reputation as a responsible member of the world community apply in relation to the investment in:

- fixed interest securities (other than public debt) issued by, and equity in, corporate entities (together "corporate securities"). This definition may be updated from time to time to include other asset classes;
- fixed interest securities issued by central governments, entities guaranteed by central governments, local authorities and quasi-government organisations (together "public debt"); and
- products which aggregate the investments of multiple investors and manage them under a common investment mandate (referred to as "pooled investment products").

4.2.1 *Corporate Securities*

4.2.1.1 In establishing and reviewing whether an active investment in a security of a corporate entity gives rise to a risk of prejudice to New Zealand's reputation as a responsible member of the world community, the Authority will have regard to (amongst other considerations):

i. information obtainable from the public domain on reasonable enquiry on whether the corporate entity has, in the last three years, been judged by a court or tribunal of competent jurisdiction to have materially breached domestic laws of any State relating to:

- human rights;
- labour and employment;
- the environment;
- arms trading; or
- trans-national organised crime and countering terrorism;

and such judgment (or if more than one in the past three years, all of them) relates to a material part of or is materially significant to the corporate entity's business; and

ii. information and advice received by the Authority that the corporate entity is on the basis of credible evidence widely regarded in the world community as having participated in:

- serious infringements of relevant international standards in relation to human rights, labour or the environment; or
- other reprehensible conduct;

of such a nature that prejudice may be caused to the reputation of an investor in the securities of that corporate entity; and

iii. any economic or other sanctions that New Zealand applies.

4.2.1.2 The reputation risk may be eliminated where:

i. the corporate entity has rectified its business practices and publicly demonstrated compliance over a reasonable period with any relevant laws or international standards previously breached; or

ii. the relevant economic or other sanctions are lifted.

4.2.2 *Public Debt*

4.2.2.1 Active investment in public debt by the Authority will give rise to a risk of prejudice to New Zealand's reputation as a responsible member of the world community where information (which is reasonably obtainable from the public domain on reasonable enquiry) establishes that the country of domicile of the issuing entity is a country which the Board considers gives rise to a risk of prejudice to New Zealand's reputation as a responsible member of the world community should the Authority invest in public debt of that country.

4.2.2.2 In establishing and reviewing whether a country falls within 4.2.2.1 above, the Board will have regard to (amongst other considerations):

i. information and advice received by the Board that indicates that a country is on the basis of credible evidence widely regarded in the world community as having participated in:

- serious infringements of international standards in relation to human rights, labour, or the environment, or
- other reprehensible conduct;

of such a nature that prejudice may be caused to the reputation of an investor in the public debt of that country; and

ii. information received by the Board indicates that the country has been subject to international censure (including the imposition of sanctions) by New Zealand and the wider world community in relation to matters referred to in paragraph 4.2.2.2 i.

4.2.2.3 The reputation risk may be eliminated where advice received by the Board indicates that the country has rectified its practices and is no longer subject to international censure.

4.2.3 *Pooled Investment Products*

In determining whether an investment in a pooled investment product gives rise to prejudice to New Zealand's reputation in the world community, the Board will assess whether investment in the product itself gives rise to a risk of such prejudice.

Passive Investments

4.2.4 It is anticipated that, in determining whether a passive or index equity investment product gives rise to prejudice to New Zealand's reputation in the world community, the Board will assess the index which the product tracks, and whether investment in the product per se gives rise to a risk of such prejudice.

4.2.5 The Board envisages that some of the passive or index international equity investment products it will consider investing in will include close to 1,000 underlying securities. The Board's view is that in these cases it is the overall index (and not each underlying security) which must be examined to determine whether there is a risk to New Zealand's reputation in investing in such a product.

4.2.6 The Board will review its assessment under 4.2.4 and 4.2.5 above, should there be a material change in the passive product, including the composition and/or weighting of the underlying securities of the passive product.

4.3 Procedures

4.3.1 The Authority will engage external experts and advisors (including screening and research agencies) to supply advice to the Board to enable it to formulate and monitor the Standards in accordance with the requirements of the Act.

4.3.2 For the purposes of applying 4.2.2.1 above in an efficient manner, the Authority may, in consultation with the external experts and advisors it has engaged:

4.3.2.1 consider only the countries in which the Board is invested or intends to invest; and

4.3.2.2 out of those countries, establish a list of countries which the Board considers do not give rise to risk of prejudice to New Zealand's reputation should the Authority invest in public debt of that country.

4.3.3 The Board shall review any such list under 4.3.2.2 at no less than six monthly intervals, and more frequently should;

4.3.3.1 it receive advice at any time that a more frequent review is appropriate;

4.3.3.2 the list of countries under 4.3.2.2 above changes. In this case, only the additional country or countries shall be reviewed.

4.3.4 The Board will ensure that all of the investment managers of the Fund are aware of these Policies, Standards and Procedures.

4.3.5 If the Board determines, based on advice from its external experts, advisors or managers, that an investment under an active mandate does not meet the Standards, the Board will refrain from making the investment. If an existing investment under an active mandate fails to meet the Standards, the following procedures will apply:

4.3.5.1 a strategy will be developed to exit the investment in a manner that has regard to 15J(2)(a) and (b) and is approved by the Board, in consultation with the relevant investment manager(s);

4.3.5.2 the exit process will be monitored by the Board;

4.3.5.3 the relevant investment manager(s) will be notified if and when the investment in the corporate security or public debt no longer contravenes the Standards.

PART B: Other Ethical investment policies, standards and procedures

4.4 It is the view of the Board, from its initial research, that widespread application of ethical standards is relatively new. Where ethical standards have been applied, there is considerable variety in the method, breadth, and application of those standards.

4.5 It is also the view of the Board that there are developing views on the extent to which an ethical policy resulting in the narrowing of investment options could compromise investment criteria the same as or similar to those of section 15J(2). The Board's policies, standards and procedures for ethical investment must be consistent with all of the requirements under section 15J(2).

4.6 It is recognised that the Policies, Standards, and Procedures for avoiding prejudice to New Zealand's reputation as a responsible member of the world community covers matters associated with ethical investment. The Board will use the experience that it gains in implementing these Policies, Standards and Procedures for avoiding prejudice to New Zealand's reputation to inform itself with respect to any further development of ethical investment policies, standards and procedures.

PART C: Review of policies standards and procedures

4.7 The policies, standards and procedures set out above shall be reviewed periodically and in any event at no less than 12 monthly intervals.

5 THE BALANCE BETWEEN RISK AND RETURN IN THE OVERALL FUND PORTFOLIO (SECTION 15M(E))

Risk and return for the overall Fund is balanced with a strategic portfolio that meets the Board's investment objective for the Fund of:

5.1 achieving an average rate of return (after tax) at least equal to the NZX New Zealand Government Stock Gross Index return (after tax) plus 2.5% per annum measured over rolling ten year periods [Note 1].

5.2 having no more than a 1 in 10 chance in any one year of a loss in the total Fund being greater than $100 million (after tax).

Note 1 This is expected to generate improved investment performance over the life of the Fund of approximately $1,200m.

6 THE FUND MANAGEMENT STRUCTURE (SECTION 15M(F))

6.1 Policy

The Board has determined that the following components of the Fund management structure should be out-sourced:

6.1.1 advisory services – legal, tax advisory, actuarial, investment advisory and audit services;

6.1.2 investment management;

6.1.3 custodian / investment back office; and

6.1.4 secretariat and management services.

6.2 Procedures

Selection of managers for these roles will take into account, among other criteria specific to the role:

6.2.1 best-practice portfolio management;

6.2.2 the skills and experience the manager brings to the role;

6.2.3 the substance and viability of the manager;

6.2.4 the costs that can be expected to be incurred;

6.2.5 the potential for cost savings and other efficiency gains; and

6.2.6 the existence of appropriate risk management structures.

Generally, unless specific circumstances require a different approach, the selection of managers will be contestable and conducted through a request for proposal and interview process.

Investment management mandates and guidelines shall be prescribed in a manner to best achieve the investment objective of the Board. In particular, mandates shall include: eligible investments, performance measurements, constraints and exposure limits including country and issue exposures, use of derivatives, and reporting requirements.

Managers will be regularly reviewed against the criteria above to determine their suitability for their role.

6.3 Governance

The Board is charged with overall governance responsibilities for the investment of the Fund, among other functions. The Board has appointed a board Investment Committee to address specific investment issues. The investment committee is provided with authority from the Board in each instance to make particular decisions on those issues.

The Board itself retains the power of appointment of managers and custodians within the Fund management structure.

The current management structure for the Fund is presented in Part 2: Current Investment Structure of the Fund.

7 THE USE OF OPTIONS, FUTURES, AND OTHER DERIVATIVE FINANCIAL INSTRUMENTS (SECTION 15M(G))

Section 15C of the Act requires the prior approval of the Minister of Finance to be sought where the Authority intends to "enter into a derivative transaction or amend the terms of that transaction (where derivative transaction includes swaps, options, futures and any combinations of those things) ."

In accordance with this provision, the Board sought and received the approval of the Minister of Finance (see letter dated 17 October 2001 and 19 January 2005) to use derivative financial instruments subject to certain conditions.

7.1 Statement of Investment Policies, Standards, and Procedures - derivative instruments.

Derivative financial instruments (derivatives) are financial contracts whose value depends on, or is derived from underlying assets, and includes futures contracts, forward currency contracts, forward interest rate contracts and options.

In relation to derivatives, "effective exposure" means the exposure to the underlying asset or liability that arises from holding the derivative. For futures and forward contracts, the effective exposure is the value of the underlying asset or liability at current market rates. For options contracts, determination of the effective exposure takes accounts of the 'delta' of the option (the sensitivity of the option value to changes in the value of the underlying asset or liability).

DERIVATIVES (EXCLUDING FORWARD FOREIGN EXCHANGE CONTRACTS)

7.2 Policy

7.2.1 Derivatives may only be used for the purposes of managing, lessening, hedging or protecting against movements in interest rates, discount rates, values or prices in relation to permitted investments;

7.2.2 Derivative transactions must be in the form of a derivative over the same asset class as the physical position;

7.2.3 Derivatives are not to be used to leverage the portfolio;

7.2.4 The holding of derivatives must be fully supported by cash, short-term debt instruments readily convertible to cash or permitted investments (but excluding derivatives) under the relevant mandate when measured on an effective exposure basis;

7.2.5 At all times, the value of all derivative positions measured on an effective exposure basis must not result in portfolio liabilities exceeding portfolio assets;

7.2.6 The effective duration of any derivatives, shall be taken into account for the purposes of determining compliance with the duration limits of fixed interest portfolios;

7.2.7 The determination of the exposure to any company, security or market shall take into account the exposure resulting from derivatives for the purposes of determining compliance with portfolio exposure limits;

7.2.8 The amount of derivatives in a portfolio is limited by either limiting exposure to individual counter-parties or limited by specifying total derivative exposure in the portfolio.

7.3 Procedures

Valuation

7.3.1 The value of derivatives, which comprise futures and options contracts, are measured on an effective exposure basis.

7.3.2 The value of other derivatives are measured by a best practice market model determined and used by the Custodian.

7.3.3 Revaluations of derivatives will be undertaken on at least a weekly basis.

Instruments

Derivative instruments traded on recognised exchanges may be entered into.

Over-the-counter options, interest rate swaps, forward rate agreements may also be entered into or held in the portfolio subject to each counterparty having an appropriate credit rating as measured by a recognised rating agency for counter party risk and appropriate contractual arrangements (for example, an ISDA agreement) being in place between the manager and each counter party.

The Board recognises that, where it invests in pooled products offered by investment managers, it may be indirectly investing in derivatives. All investment managers are required to provide the Board with a copy of their policies relating to derivatives securities trading risk and to manage their derivative exposures in accordance with those policies.

DERIVATIVES – FOREIGN EXCHANGE CONTRACTS

7.4 Policy

Derivatives relating to foreign exchange may be used for the purposes of managing and hedging currency exposures held within the Fund and for the purposes of purchasing or selling foreign currencies required for the settlement of foreign exchange transactions. Derivatives are not to be used to leverage the Fund, which would require the Authority to borrow on behalf of the Fund.

The net exposure to foreign currencies (after taking into account hedging positions) in the relevant portfolios are to be in accordance with the Board's hedging policy for that asset class*.

In general and where applicable, currency exposures are to be hedged directly as opposed to proxy-currency hedging with a highly correlated third currency to reduce the primary exposure - for example using a United States dollar hedge to reduce a Canadian dollar exposure. However proxy-currency hedging is permitted where direct hedging is impractical, for example in thinly traded markets where suitable foreign exchange hedging contracts are unavailable or where the costs and administration of direct hedging small exposures are out-weighed by proxy-currency hedging.

Appropriate parameters* for hedging using proxy currency will be established with the currency managers.

7.5 Procedures

Foreign exchange hedging contracts may be entered into only with counterparties that have credit ratings approved by the Board and measured by a recognised rating agency for counterparty risk.

Contractual arrangements (for example, an ISDA agreement) must be in place between the manager and each counterparty in a form suitable to the Board.

Appropriate operational ranges* will be established with managers around the determined hedge ratio to avoid excessive costs of continually adjusting the hedge to the precise hedge ratio

Each fund manager and the transition manager must have risk management policies and procedures in place that address counterparty risks suitable to the Board.

**Details of the Board's hedging policies for each asset class, operational ranges for currency hedging and proxy-currency hedging are presented in Part 2: Current Investment Structure of the Fund.*

8 THE MANAGEMENT OF CREDIT, LIQUIDITY, OPERATIONAL, CURRENCY, MARKET, AND OTHER FINANCIAL RISKS (SECTION 15M(H))

8.1 Credit risk

8.1.1 Managers of New Zealand fixed interest investments are only permitted to invest:

8.1.1.1 in New Zealand fixed interest securities issued by:

i. the New Zealand Government or agency of the New Zealand Government;

ii. entities guaranteed by the New Zealand Government; or

8.1.1.2 in entities with an appropriate* long-term debt rating as measured by a recognised rating agency;

8.1.1.3 a specified maximum of the Portfolio in fixed interest securities not issued or guaranteed by the New Zealand Government or agency of the New Zealand Government.

8.1.2 Managers of New Zealand fixed interest investments must ensure the maximum exposure to any single issuer other than the New Zealand Government is within specified bounds.

8.1.3 Managers of New Zealand fixed interest investments must ensure the maximum exposure issuers other than the New Zealand Government is within specified bounds that depend on the credit rating of those issuers;

8.1.4 Managers of international fixed interest investments are only permitted to invest:

8.1.4.1 in debt instruments denominated in foreign currencies issued or guaranteed by:

i. foreign governments or agencies; or

ii. entities guaranteed by foreign governments; or

8.1.4.2 entities with an appropriate* long-term debt rating as measured by a recognised rating agency;

8.1.4.3 a specified maximum of the Portfolio in debt securities not issued or guaranteed by foreign governments or agencies.

8.1.5 Managers of international fixed interest investments must ensure the maximum exposure to any single issuer other than foreign governments or agencies is within specified bounds.

8.1.6 In respect of foreign currency management

8.1.6.1 Any forward contracts entered into must be with entities that have an appropriate* minimum credit rating as determined by an international credit rating agency for counter-party risk; and

8.1.6.2 appropriate contractual arrangements (for example, an ISDA Agreement) must be in place between the currency manager and the counterparty.

8.1.7 In respect of cash and short-term fixed interest securities

8.1.7.1 any cash balances must be held in an interest bearing account with the custodian;

8.1.7.2 any short-term securities must have an appropriate* short-term debt rating as measured by a recognised rating agency.

8.2 Liquidity Risk

Liquidity risk is the risk that a security cannot be sold when required or that the price achieved is significantly different from the quoted price.

Liquidity risk is managed by:

8.2.1 requiring, except as specifically authorised by the Board, managers to only invest in securities traded on recognised exchanges;

8.2.2 where investment in securities that are not traded on recognised markets are authorised by the Board, controlling exposure to those securities;

8.2.3 requiring managers, within the terms of their individual contracts, to hold diversified portfolios;

8.2.4 limiting the credit rating* of the fixed interest and cash investments to minimum levels .

8.3 Operational Risk

8.3.1 engaging an independent global custodian to separate the investing function (undertaken by the investment managers) from the transaction settlement, recording and reporting of investment activities (as undertaken by the global custodian).

8.3.2 requiring investment managers and the custodian to:

8.3.2.1 provide the Board with third party covenants or assurances against these events;

8.3.2.2 have in place insurance arrangements to cover claims in those events;

8.3.2.3 have in place and regularly confirm the existence and efficiency of internal policies and controls to address those risk; and

8.3.3 compliance reporting by investment managers, the custodian and the external auditors.

8.4 Currency Risk

Currency risk is the risk that the foreign currency denominated assets will lose value due to the effect of an adverse exchange rate movement.

Currency risk is managed by:

8.4.1 engaging a currency manager to manage the international equities and property currency exposure in accordance with the hedging ratio for that asset class;

8.4.2 specifying the bounds within which the international fixed interest managers may take on currency exposures relative to a benchmark that is fully hedged to United States dollars; and

8.4.3 engaging a currency manager to implement a passive hedge to New Zealand dollars for the international fixed interest portfolio's value in United States dollars.

The instruments that managers may use and the credit worthiness of the counterparties are detailed in the investment management contract with respective managers.

8.5 Market Risk

8.5.1 requiring investment managers to manage their portfolios within defined market exposure limits. Those limits include:

8.5.1.1 New Zealand fixed interest.

i. duration limits relative to the duration of the benchmark;

ii. maximum limits on non-Government investments.

8.5.1.2 New Zealand equities.

The Investment Mandates for active management are to contain exposure limitation criteria to control market risk. Those criteria may include:

i. Limits on the percentage weight of any individual company in the portfolio relative to its benchmark weight;

ii. Limits on investment in companies not represented in the benchmark;

iii. Limits on investment in any individual company not represented in the benchmark; and

iv. Limits on the maximum investment in any individual company.

8.5.1.3 International Equities

i. the investments are to be passively managed at benchmark weights.

8.5.1.4 International Fixed Interest

i. duration limits relative to the duration of the benchmark;

ii. maximum limits on non-Government investments;

iii. maximum limits on exposure to single entities (excluding governments).

8.5.1.5 Property

i. maximum and minimum limits on regional exposures relative to those exposures in the benchmark;

ii. limits on investments not represented in the benchmark; and

iii. limits on exposures for individual investments.

8.5.1.6 Currencies

i. For international equities, a passive hedge approach to management of the hedge ratio relative to the currency exposures of the benchmark.

ii. For international fixed interest, hedging the currency exposure of the portfolio back into the United States dollar while allowing positions to be held in individual currencies within specified risk control bounds. The United States dollar value of the international fixed interest portfolio is fully hedged to New Zealand dollars under a passive hedge approach.

iii. For listed property, a passive hedge approach relative to bounds around the currency exposures of the benchmark. Proxy-currency hedging is permitted for minor currency exposures to reduce compliance costs.*

**See Part 2: Current Investment Structure of the Fund for details*

9 THE RETENTION, EXERCISE OR DELEGATION OF VOTING RIGHTS ACQUIRED THROUGH INVESTMENTS (SECTION 15M(I))

9.1 Active Management

Policy

Investment managers are required to give full consideration to all voting opportunities and shall vote on all substantive issues affecting the Authority's portfolio.

Investment managers must vote on those issues in the best interests of the Fund and in accordance with the managers' voting guidelines and having regard to the Authority's statutory requirements of section 15J(2) of the Government Superannuation Fund Act 1956 (as amended).

Any conflicts or inconsistencies between the best interests of the Fund, investment managers' guidelines, the Government Superannuation Fund Act 1956 (as amended) or the Crown shall be referred to the Authority.

Standards

A 'substantive issue' is one which has the potential to materially affect the value of the Authority's investment in that entity in the near future.

Investment managers are required to establish and adhere to voting guidelines.

Each year the investment manager must update those guidelines and provide a copy to the Authority.

Material changes to the voting guidelines must be advised in writing to the Authority.

Procedures

Investment managers are required to report all voting decisions to the Authority quarterly (at the end of March, June, September and December).

Investment managers must brief the Authority on substantive issues prior to voting and provide reasons for voting decisions, as required by the Authority.

When an investment manager refers a voting proposal to the Authority, Management will prepare a report outlining the voting situation and recommending a voting course of action. On limited occasions this may involve receiving an independent report.

If the voting proposal involves the Crown, the Board will consider application for a waiver from the New Zealand Stock Exchange associated persons rules to enable investment managers to vote either for or against the proposal as they determine.

9.2 Passive Management and Pooled Investment Products

The Board recognises that, consistent with the IRD binding rulings on passively managed products and the aggregation of investors in pooled investment product, it is not able to exercise the voting rights attached to the underlying investments.

10 THE METHOD OF, AND BASIS FOR, VALUATION OF INVESTMENTS THAT ARE NOT REGULARLY TRADED AT A PUBLIC EXCHANGE. (SECTION 15(J))

Generally, the investments of the Board are to be regularly traded on recognised exchanges.

Where investments are held that are not regularly traded on recognised exchanges, for example unlisted pooled investments or over the counter derivatives, for year end independent pricing will be obtained on material investments (either through the Board's custodian or from another source).

For monthly valuations, the Board will either:

- Obtain an independent price for each security; or
- Use the Fund Managers prices, if an independent price cannot be obtained

11 PROHIBITED OR RESTRICTED INVESTMENTS OR ANY INVESTMENT CONSTRAINTS OR LIMITS. (SECTION 15M(K))

Prohibited or Restricted Investments

Except as required to control risks (as set out under section 8 above) and in accordance with the Board's ethical investment policy there are no specifically prohibited or restricted investments. However each investment management contract specifies those investments that constitute permitted investments and managers may not invest other than in those permitted investments.

Specific written authorisation from the Board is required to invest outside of the prescribed permitted investments. The Board will consider such investments as they arise on application from the investment manager

Investment Constraints and Limits

The Board has developed constraints and limits in respect of each investment class to control risks (see section 8 above). It has also determined limits to the exposure to each investment class to ensure the investment objective of the Fund is not compromised by excessive deviation from the Fund's strategic asset allocation.

The Authority is precluded from controlling any other entity or from holding such a percentage of the voting rights of another entity that would require it to seek control of that entity. See section 15K of the Act. Limits on the maximum holding that can be held in each issuer address this.

APPENDIX 1 SECTION 15M OF THE ACT

15M Contents of statements of investment policies, standards, and procedures

A statement of investment policies, standards, and procedures must cover (but is not limited to)-

(a) the class of investments in which the Fund is to be invested and the selection criteria for investments within those classes; and

(b) the determination of benchmarks or standards against which the performance of the Fund as a whole, classes of investment, and individual investments will be assessed; and

(c) standards for reporting the investment performance of the Fund; and

(d) ethical investment, including policies, standards, or procedures for avoiding prejudice to New Zealand's reputation as a responsible member of the world community; and

(e) the balance between risk and return in the overall Fund portfolio; and

(f) the Fund management structure; and

(g) the use of options, futures, and other derivative financial instruments; and

(h) the management of credit, liquidity, operational, currency, market, and other financial risks; and

(i) the retention, exercise or delegation of voting rights acquired through investments; and

(j) the method of, and basis for, valuation of investments that are not regularly traded at a public exchange; and

(k) prohibited or restricted investments or any investment constraints or limits.

PART 2: CURRENT INVESTMENT STRUCTURE OF THE FUND

1 ASSET CLASSES

The Fund shall be invested in the following general asset classes:

International equities;
New Zealand equities;
Property assets;
International fixed interest;
New Zealand fixed interest;
New Zealand cash and short-term securities

In addition, the currency exposure associated with international investing will be managed and exposures to the asset classes will be constrained around their strategic benchmark.

1.1 International Equities

1.1.1 the strategic benchmark allocation is to be 42.5% of the total Fund assets

1.1.2 the strategic benchmark for monitoring purposes will be the modified MSCI grey list* index expressed in New Zealand dollars;

1.1.3 international equities are to be managed passively in broad based international equities products which have binding IRD rulings exempting them from New Zealand taxation on capital gains; and

1.1.4 two passive managers are to be appointed.

*comprising Australia, Canada, Germany, Japan, United Kingdom and the United States of America.

1.2 New Zealand Equities

1.2.1 the strategic benchmark allocation is to be 15.0% of total Fund assets;

1.2.2 the universe of permitted investments is to be equity securities of companies either:

1.2.2.1 listed on the New Zealand Stock exchange and resident in New Zealand for tax purposes; or

1.2.2.2 included in the NZSX50 Index;

1.2.3 permitted investments also include certain convertible debt instruments and options provided the equities to which they relate satisfy the permitted investment criteria stated above;

1.2.4 the benchmark index for monitoring purposes is to be the Russell / J B Were Gross Tradeable Index; and

1.2.5 at least two active managers with complementary investment styles are to be appointed.

1.3 Property Assets

1.3.1 the strategic benchmark allocation is to be 7.5% of total Fund assets;

1.3.2 the benchmark index for portfolio monitoring purposes is to be the UBS Warburg Global Real Estate Total Return Investors Only Index hedged to New Zealand dollars;

1.3.3 up to 15% of the property portfolio may be invested in securities not represented in the benchmark;

1.3.4 at least two active managers are to be appointed;

1.3.5 managers of segregated portfolios will be measured and monitored relative to the unhedged benchmark expressed in United States dollars;

1.3.6 managers of pooled investment products will be measured and monitored relative to the benchmark hedged to New Zealand dollars.

1.4 International Fixed Interest

1.4.1 the strategic benchmark allocation is to be 21% of total Fund assets ;

1.4.2 a minimum of 30% of the international fixed interest portfolio must be allocated to domestic government issuance.

1.4.3 the benchmark index for portfolio monitoring purposes is to be a modified version of the Lehman Brothers Global Aggregate Bond Index hedged to New Zealand dollars;

1.4.4 at least two active managers are to be appointed;

1.4.5 managers will be measured and monitored relative to the benchmark hedged to United States dollars.

1.5 New Zealand Fixed Interest

1.5.1 the strategic benchmark allocation to New Zealand fixed interest investments is to be 14% of total Fund assets ;

1.5.2 up to 50% the New Zealand fixed interest portfolio may be allocated to non-sovereign issues;

1.5.3 the benchmark index for monitoring purposes is to be the NZX New Zealand Government Stock Gross Return Index;

1.5.4 at least two active managers are to be appointed.

1.6 Cash

1.6.1 there is to be no cash allocation in the strategic benchmark allocation;

1.6.2 managers appointed to manage equities and property are to be permitted to hold up to 5% of their portfolios in cash for liquidity and operational purposes.

1.7 Asset Allocation and Rebalancing

1.7.1 asset allocation is to be managed passively that is, no attempt will be made to add value by deliberately and actively over-weighting particular asset classes at the expense of others. However, developments in tactical asset allocation or strategic tilting will be actively monitored with respect to their applicability to the Fund;

1.7.2 each month the Fund's actual asset allocation will be checked against the rebalancing ranges. Asset allocations will be allowed to fluctuate within their permitted rebalancing ranges and taking known cash flows for the next month into account, transactions will be undertaken to ensure compliance with those rebalancing ranges;

1.7.3 the permitted ranges relative to the strategic benchmark allocations within which the actual allocation may vary before rebalancing is required are:

1.7.3.1 Subject to total growth assets (equities plus property assets) being between 62% and 68% of total Fund assets:

i. international equities between 39% and 46% of total Fund assets;

ii. New Zealand equities between 12% and 18% of total Fund assets; and

iii. Property assets between 4% and 11% of total Fund assets.

1.7.3.2 Subject to total income assets (fixed interest assets) being between 32% and 38% of total Fund assets:

i. international fixed interest being between 19% and 23% of total Fund assets; and

ii. New Zealand fixed interest being between 12% and 16% of total Fund assets.

1.7.4 where an asset class is outside of its rebalancing range, it is rebalanced to the point half-way between the strategic asset allocation for that asset class and the breached rebalancing range.

1.8 Currency Management

International Fixed Interest

1.8.1 the international fixed interest portfolio currency hedging benchmark will be to be fully hedged to the New Zealand dollar;

1.8.2 currency management will be implemented by:

1.8.2.1 having the United States dollar as the base currency of the portfolio and permitting the investment managers to manage currency exposures to between 70% and 130% on the net asset value of the portfolio in United States dollar terms; and

1.8.2.2 engaging a currency manager to implement a passive hedge of 100% of the United States dollar value of the portfolio to New Zealand dollars.

International Equities

1.8.3 the currency hedge ratio for international equities is to be a maximum of 80% hedged on an after tax basis (approximately 120% hedged before tax);

1.8.4 the hedge ratio will be permitted to vary between + 10% and –10% around the pre-tax hedge ratio before being required to be re-balanced to be within that range;

1.8.5 the hedge will be implemented by taking currency hedging position only in currencies represented in the international equities benchmark index; and

1.8.6 the currency exposure will be managed passively by a specialist currency manager.

Property

1.8.7 the property portfolio currency benchmark is the currency exposure of the underlying property portfolio fully hedged to the New Zealand dollar;

1.8.8 the hedge will be implemented by taking currency hedging positions in major currencies. The manager may hedge using close proxies for minor currencies represented in the property portfolio to save administration costs. A minor currency is one that has a weight of less than 1% in the property portfolio.

Implementation:

1.8.9 Implementation strategies for significant asset allocation changes or the addition of new asset classes may include a staged entry or exit programmes to achieve investing and disinvesting goals.

1.9 Summary

The Fund and asset class features are summarised in the following tables.

Table 1: Strategic Benchmark and Asset Class Rebalancing Ranges

Asset class	**Weight**	**Rebalancing Range**
International equities	42.5%	39% to 46%
New Zealand equities	15.0%	12% to 18%
Property assets	7.5%	4% to 11%
Total growth assets	***65%***	***62% to 68%***[1]
International fixed interest	21%	19% to 23%
New Zealand fixed interest	14%	12%to 16%
Total fixed interest	***35%***	***32% to 38%***[1]
International equities pre-tax hedge ratio (max)	120%	110% to 130%
Property hedge ratio to NZ dollars	100%	95% to 105%
International fixed interest hedge ratio to US dollars	100%	70% to 130%
International fixed interest hedge ratio US to NZ dollars	100%	100%

[1] The rebalancing ranges for individual asset classes are subject to the total growth assets and total fixed interest assets rebalancing ranges.

Table 2: Asset Class Benchmarks and Return Performance Targets

Asset Class	Benchmark	Return Value Added Target
International equities	Modified 'grey list' MSCI Index (75% hedged)	Nil
New Zealand equities	Russell/J B Were Gross Tradeable Index	3.0% per annum
Property – segregated portfolio	UBS Warburg Global Real Estate Total Return Investors Only Index expressed in United States dollars	2.5% per annum
Property – pooled portfolio	UBS Warburg Global Real Estate Total Return Investors Only Index 100% hedged to New Zealand dollars	Nil
International fixed interest	Lehman Brothers Global Aggregate Index 100% hedged to United States dollars but excluding New Zealand Government securities	1.0% per annum
New Zealand fixed interest	NZX New Zealand Government Stock Gross Index	0.6% per annum
Currency – international equities	Currency weights of modified 'grey list' MSCI Index (75% hedged to NZD before tax)	Nil
Currency – property – segregated portfolio	Currency weights of underlying segregated property portfolio	Nil
Currency – international fixed interest	100% hedged to New Zealand dollars according to a pre-determined pricing formula	Nil

2 RISK CONTROL

To control risk the following constraints are applied to the Fund's investments

2.1 International Equities

2.1.1 The investments are passively managed at benchmark weights;

2.1.2 The tracking error of the passive product to its benchmark will be monitored.

2.2 New Zealand Equities

2.2.1 The maximum investment (including the effect of any derivatives) in any individual company must not exceed 5% of the issued capital of that company;

2.2.2 The investment in any individual company must not vary from its benchmark weight by more than the following limits (subject to a minimum of zero):

The greater of plus or minus:

2.2.2.1 5% of its benchmark weight; and

2.2.2.2 half its benchmark weight.

Provided that:

2.2.2.3 no more than 20% of the Portfolio may be invested in companies not in the benchmark; and

2.2.2.4 no more than 5% of the Portfolio may be invested in any single company not in the benchmark.

2.2.3 Underwriting or sub-underwriting of share issues is permitted up to a maximum of 5% of the net asset value of the Portfolio;

2.2.4 The use of derivatives must not exceed 20% of the net asset value of the portfolio measured on an effective exposure basis;

2.2.5 Up to 5% of the net asset value of the portfolio may be held in cash and short-term securities that meet the criteria for cash and short-term securities below.

2.2.6 The tracking error of the portfolio relative to the benchmark is expected to be below 5%.

2.3 Listed Property – segregated portfolio

2.3.1 Permitted investments are shares or units in companies or trusts that invest principally in real property and are traded on recognised stock exchanges and cash;

2.3.2 The "recognised stock exchanges" are presented in Appendix II. Investment in securities traded on other stock exchanges must be notified by the manager at least 5 working days before investment;

2.3.3 A minimum of 95% of the portfolio must be invested in non-cash permitted investments;

2.3.4 Regional (North America, Europe and Asia / Pacific) exposures must be within 15% of the respective regional exposures in the benchmark;

2.3.5 No more than 15% of the portfolio may be invested in non-benchmark investments; and

2.3.6 The tracking error of the portfolio measured over rolling three-year periods is expected not to exceed 6.0%.

2.4 Listed Property – pooled products

The risk minimisation parameters are those of the product and as such are only indirectly under the control of the Authority. Those parameters include:

2.4.1 Limits on regional exposures relative to the exposures of the benchmark;

2.4.2 A minimum number of stocks to be held in respect of each region;

2.4.3 Maximum limits on the exposure to non-benchmark stocks and to single stocks.

2.5 International Fixed Interest

2.5.1 Permitted investments are debt securities that are:

2.5.1.1 Denominated in the currencies represented in the benchmark; and

2.5.1.2 Either are included in the benchmark or have a long-term credit rating of at least AA- as rated by the Standard and Poor's Corporation;

2.5.2 The average market value-weighted quality of the portfolio must be no lower than A+;

2.5.3 A minimum of 30% of the international fixed interest portfolio must be allocated to domestic government issuance;

2.5.4 The maximum exposure to any non-Government single entity is 5% of the net asset value of the portfolio;

2.5.5 Where a maximum exposure to derivative securities is prescribed it is 30% of the net asset value of the portfolio. If no maximum is prescribed the maximum exposure to a single counter-party is 5% of the net asset value of the portfolio;

2.5.6 The following duration limits apply:

2.5.6.1 The duration of the portfolio must be within 2.5 years of the duration of the benchmark at all times;

2.5.6.2 The duration of the dollar bloc portion of the portfolio must be within 2 years of the benchmark duration of that portion;

2.5.6.3 The duration of the Euro bloc portion of the portfolio must be within 2 years of the benchmark duration of that portion;

2.5.6.4 The duration of the Japanese portion of the portfolio must be within 2 years of the benchmark duration of that portion.

2.5.7 The tracking error of the portfolio measured over rolling three-year periods is expected not to exceed 2.5%

2.6 New Zealand Fixed Interest

2.6.1 Permitted investments are New Zealand fixed interest securities issued by:

2.6.1.1 The New Zealand Government or agency of the New Zealand Government;

2.6.1.2 New Zealand Entities guaranteed by the New Zealand Government; or

2.6.1.3 New Zealand Entities with a long term (in excess of 180 days) debt rating of not less than A3 as rated by Moody's Investor Service or A- as rated by Standard and Poor's Corporation;

2.6.2 The maximum exposure to any single issuer other than the New Zealand Government or agency of the New Zealand Government or entities guaranteed by the New Zealand Government is 5% of the net asset value of the Portfolio for issuers with a Standard and Poors long-term rating of AA- or better and 4% for issuers with a Standard and Poors long-term rating of A+, A or A-;

2.6.3 The maximum exposure to any single issuer other than the New Zealand Government or agency of the New Zealand Government or entities guaranteed by the New Zealand Government is 5% of the net asset value of the Portfolio;

2.6.4 The duration of the portfolio must be within plus or minus 1.5 years of the duration of the benchmark;

2.6.5 Managers of the New Zealand fixed interest portfolio are permitted to enter into repurchase agreements relating to New Zealand government debt instruments. Provided that:

2.6.5.1 Where no derivatives are held in the portfolio, the total face value of all repurchase agreements must not exceed 40% of the net asset value of the portfolio; and

2.6.5.2 Where derivatives are held in the portfolio, the combined total value of all derivatives plus the total value of all repurchase agreements must not exceed 50% of the net asset value of the portfolio; and

2.6.5.3 The value of derivatives alone must not exceed 20% of the net asset value of the portfolio.

2.7 Cash and Short-term Fixed Interest

2.7.1 The maturity of the investments is not to exceed 180-days;

2.7.2 Any short-term securities must have a short-term (not exceeding 180 days) debt rating of not less than Prime -1 as rated by Moody's Investor Services or A1 as rated by Standard and Poor's Corporation.

2.7.3 Any cash balances must be held in an interest bearing account with the custodian;

2.8 Foreign currency management

<u>International equities</u>

2.8.1 Only forward contracts relating to currencies of countries represented in the underlying international equity portfolio are permitted (those countries are: Australia, Canada, Germany, Japan, United States and United Kingdom);

2.8.2 At all times the currency exposure of any country in the currency management portfolio plus the currency exposure of that country in the Authority's International Equity portfolio must be within 10 percentage points of the currency exposure of that country in the currency benchmark but may not be less than 0%.

2.8.3 The overall New Zealand dollar currency exposure of the currency management portfolio plus New Zealand dollar currency exposure of the Authority's International Equity Portfolio shall remain in the range of +10% to +10% of the pre – tax hedge ratio.

2.8.4 Any forward contracts entered into must be with entities that have a short-term credit rating of A1 or higher as determined by Standard and Poor's Corporation (or as an alternative rating agency is used a rating of equivalent standing);

2.8.5 Appropriate contractual arrangements (for example, an International Swap Dealers' Association (ISDA) Agreement) must be in place between the currency manager and the counterparty;

2.8.6 Currencies are passively managed within bounds around benchmark weights (as shown in Table 2 above);

2.8.7 The effect of the currency management portfolio is to result in the tracking error of the currency component of the Authority's international equity portfolio relative to the currency benchmark to be within 0.20%;

2.8.8 No single counter-party may hold derivatives that expose that counter-party to more than 25% of the currency management portfolio.

2.9 International fixed interest

The performance of the international fixed interest managers is measured relative to the benchmark 100% hedged to United States dollars. Managers are permitted to deviate from the 100% hedged position within the following constraints:

2.9.1 Exposure to authorised currencies must remain within 10% of their exposure in the benchmark;

2.9.2 The cumulative currency exposure of the portfolio must not exceed 30% of the net asset value of the portfolio.

2.9.3 An ISDA Agreement must be in place between the managers and any counterparty.

The New Zealand dollar / United States dollar currency exposure of the portfolio is 100% hedged to New Zealand dollars and passively managed according to an agreed pricing formula by a contracted currency manager.

Property

2.9.4 Forward contracts relating to currencies of countries represented in the underlying property portfolio and their close proxies where the currency exposure is less than 1% of the total exposure of the portfolio are permitted;

2.9.5 At all times the currency exposure (allowing for any hedging by proxy currencies) of any country in the currency management portfolio plus the currency exposure of that country in the Authority's property portfolio must be within 10 percentage points of the currency exposure of that country in the currency benchmark but may not be less than 0%.

2.9.6 The overall New Zealand dollar currency exposure of the currency management portfolio plus New Zealand dollar currency exposure of the Authority's property portfolio shall remain in the range 90% to 110%.

2.9.7 Any forward contracts entered into must be with entities that have a short-term credit rating of A1 or higher as determined by Standard and Poor's Corporation (or as an alternative rating agency is used a rating of equivalent standing);

2.9.8 Appropriate contractual arrangements (for example, an ISDA Agreement) must be in place between the currency manager and the counterparty;

2.9.9 The effect of the currency management portfolio is to result in the tracking error of the currency component of the Authority's property portfolio relative to the currency benchmark to be within 0.30%;

2.9.10 No single counter-party may hold derivatives that expose that counter-party to more than 25% of the currency management portfolio;

2.9.11 The value of all derivative securities when measured on a market equivalent basis, held in the currency management portfolio open at any one time must not exceed 100% of the net asset value of the currency management portfolio.

3 CURRENT MANAGEMENT STRUCTURE

The Board has determined and implemented the following investment management structure for the Fund:

3.1 appointment of a global custodian to provide the appropriate separation of functions between the investing function (undertaken by the investment managers) and the transaction settlement, recording and reporting of investment activities (under taken by the global custodian).

3.2 all GSF assets, apart from cash holding required for operational liquidity purposes, are to be held under custody unless specifically authorised otherwise by the Board.

3.3 cash required for operational liquidity purposes is managed by the Authority's Management;

3.4 contracted investment managers:

3.4.1 at least two international equities managers products to mitigate manager and product risk;

3.4.2 two New Zealand equities managers with complementary styles to mitigate manager and style risk;

3.4.3 two property managers with complementary styles to mitigate manager and style risk;

3.4.4 three international fixed interest managers with complementary styles to mitigate manager and style risk;

3.4.5 two New Zealand fixed interest managers with complementary styles to mitigate manager and style risk;

3.4.6 a specialist currency manager to manage the currency hedging exposure associated with the international equities investment.

TABLE OF CURRENT INVESTMENT MANAGERS AND CUSTODIAN

Asset Class	Investment Managers
International equities	AMP Capital Investors New Zealand Limited
	BNZ Investment Management Limited
New Zealand equities	Alliance Capital Management New Zealand Limited
	TOWER Asset Management Limited
Property	AMP Capital Investors New Zealand Limited LaSalle Investment Management (Securities) LP
International fixed interest	Goldman Sachs Asset Management International
	Pacific Investment Management Company LLC
	Wellington Management Company LLP
New Zealand fixed interest	Alliance Capital Management New Zealand Limited
	AMP Capital Investors New Zealand Limited
Residual portfolio	AMP Capital Investors New Zealand Limited
Currency	ANZ National Bank Limited
	State Street Global Advisors Australia Limited
Custodian	J P Morgan-Chase Bank

3.5 Joint Venture with Board of Trustees of the National Provident Fund. The Authority , in a joint venture with the Board of Trustees of the National Provident Fund, has established Annuitas Management Limited to provide management services to the Board. The prime function of Annuitas is to provide staff who act in management roles on behalf of the Authority. Management is responsible for :

3.5.1 the economical management of the activities and planning for the Authority,

3.5.2 the identification and implementation of appropriate strategies for the Authority to meet its obligations under the Act and its objectives from time to time

3.5.3 administration and board secretarial;

3.5.4 financial and accounting;

3.5.5 management of external advisors;

3.5.6 management of contracted services including investment management services;

3.5.7 contract compliance monitoring;

3.5.8 liaison with Crown agencies;

3.5.9 reporting to the Board.

APPENDIX II

Recognised Stock Exchanges for Segregated Property Portfolio.

"Recognised Stock Exchange" means any stock exchange that enforces rules, procedures and requirements sufficiently similar to the New Zealand Stock Exchange. For the purposes of the property portfolio managed by LaSalle Investment Management (Securities) LP and at the date of this Statement of Investment Policies. Standards, and Procedures the following stock exchanges are "recognised stock exchanges":

- New York Stock Exchange;
- American Stock Exchange;
- London Stock Exchange;
- Stockholm Stock Exchange;
- Singapore Stock Exchange;
- Amsterdam Stock Exchange;
- Tokyo Stock Exchange;
- Italian Stock Exchange;
- Frankfurt Stock Exchange;
- Paris Stock Exchange;
- Helsinki Stock Exchange;
- Toronto Stock Exchange;
- Brussels Stock Exchange;
- Australian Stock Exchange;
- Vienna Stock Exchange;
- Stock Exchange of Hong Kong;
- Swiss Exchange;
- Osaka Securities Exchange

DIRECTORY

Government Superannuation Fund Authority Board
Basil Logan (Chairman)
David May (Deputy Chairman)
Colin Blair
Helen Bowie
Tim McGuinness
Susie Weaver
Ralph Stockdill

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Schemes Administrator:
AXA New Zealand
(Government Superannuation Fund Schemes Administration)
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Datacom Employer Services Limited
(Government Superannuation Fund Schemes Administration)
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(from 26 April 2005)

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Tax adviser:
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Government Actuary
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INVESTMENT MANAGERS:

New Zealand fixed interest
AMP Capital Investors (New Zealand) Limited
Alliance Capital Management New Zealand Limited

International fixed interest
Pacific Investment Management Company LLC
Goldman Sachs Asset Management
Wellington Management Company LLP

New Zealand equities
Alliance Capital Management New Zealand Limited
Tower Asset Management Limited

International equities
AMP Capital Investors (New Zealand) Limited
Bank of New Zealand Investment Management Limited

Property
AMP Capital Investors (New Zealand) Limited
LaSalle Investment Management (Securities) L.P.
RREEF America REIT II, Inc

Currency management

State Street Global Advisors, Australia, Limited	International Equities
ANZ National Bank Limited	International Fixed Interest

GOVERNMENT
SUPERANNUATION FUND
AUTHORITY

GOVERNMENT SUPERANNUATION FUND
Te Pūtea Penihana Kāwanatanga